

The Critical Challenges of Using QuickBooks Online for Law Firms

By Caren Schwartz, Associate of 35*45 Consulting
Written in partners with CosmoLex

Table of Contents

Table of Contents	1
Introduction	2
Part 1: Trust Accounting Challenges	3
Part 2: Legal Billing Challenges	5
Setting Rates	5
Invoicing	5
Payment Allocation	6
Part 3: Client Cost Tracking Challenges	7
Final Takeaway	8
About the Author	9

Introduction

It's no secret that across a wide range of industries QuickBooks is a very popular accounting solution. Ask anyone, what comes to mind when they think of accounting software and more than likely QuickBooks will be one of the first things you hear come out of their mouth. Now that QuickBooks has moved into the cloud (as QuickBooks Online), and is available as an on demand solution, more businesses are turning to it for their accounting needs.

Unfortunately for law firms, QuickBooks and QuickBooks Online (QBO) present unique challenges specific to the practice of law. Law firms have very specific rules and regulations and, because of that, they have very specific needs when it comes to their accounting solutions. The areas of trust accounting, billing, and cost tracking make it difficult for firms to use a general accounting solution like QuickBooks or QBO.

We'll look at the challenges faced by law firms in a three-part series: Part 1 will focus on trust accounting challenges and how they relate to QBO, Part 2 will address the legal billing challenges associated with QBO, and finally, in Part 3 we'll review client cost tracking.

Part 1: Trust Accounting Challenges

When it comes to trust/IOLTA accounting, law firms must carefully track fund balances by client and matter. The firm must be careful not to overdraw from a particular client's fund account, and the firm must be able to show that the money in the bank account matches the sum of all clients' individual client ledgers. All of this must be tracked and reported on an individual client matter basis.

While QBO can track funds by client and matter when carefully using the trust bank account, a matching trust liability account, and including the client matter on each transaction, there is no way to prevent the overdraw of a client's fund account. The firm must be careful to run reports before any withdrawal is done to make sure the money is available. Since there are no automatic controls, it is possible to write a check against the wrong trust bank account, deposit a trust check into the wrong bank account, or forget to include the client name on the check or deposit. This makes it impossible to properly track to whom the funds belong, which can lead to improper handling of a client's funds, as you don't know if they have money or if their money has been used.

While QBO can produce a report that shows the activity and balance by matter, there is no way to run a summary report, showing just the balance for each client. This makes it harder to do quick monitoring. It can also be difficult to create a report that shows only the clients with current balances and remove anyone whose balance has gone to zero. Accounting software designed for law firms such as [PCLaw](#), [Tabs3](#) or [CosmoLex](#) will generally include a feature that prevents negative trust account balances by client and/or matter.

Creating a 3-way reconciliation report, required in many states, is difficult. It can be done, but it requires multiple reports and some work in excel to make the presentation easier to follow. First, you must print the bank reconciliation report and look at uncleared transactions to identify whose money is outstanding. This requires looking at individual transactions, as the ownership is not shown on the reconciliation report. Next, you need to create a report that shows trust activity by client, based on the trust liability account. The liability account has to be reconciled to zero to remove clients that no longer have funds, limiting the length of the report.

Finally, the trust activity report needs to be sent to excel to get a grand total and, if desired, to get a single line for each client.

QBO allows you to do bank reconciliations monthly or at any time desired. There is limited ability to lock down the data, but there are reports available that can show what changes have been made if something was incorrectly changed. The ability to download data makes it easy to make sure all transactions are present, but you must be careful that all transactions are properly coded, including the customer, as this is not automatic or necessarily correct when downloaded.

One additional area of trust accounting that can be problematic is keeping the client apprised of trust activity. Whether the firm does this to inform the client or because of local requirements, it is a manual process. Legal specific accounting software will generally offer the option to show the trust balance and/or activity on the invoice. With QBO you must create an individual report for each client and then determine the best way to send that to the client.

Verdict: Keeping in mind strict compliance requirement and non-compliance consequences, QBO is not recommended for attorney trust accounting for following key reasons:

- Inability to ensure all funds are tracked to its client matters
- Inability to prevent client ledger overdraft
- Workarounds to generate 3-Way Reconciliation reports
- Inability to lock books post reconciliations to prevent accidental edits

QBO is designed for the general market, including companies with inventory and general services. For many companies, it meets the business needs either on its own or by the use of add-ons. While add-ons can make QBO better meet a company's needs, add-ons can also add additional complexity, cost, and may still not meet all the needs of law firms.

The final suggestion would be when looking for a system to manage their attorney trust accounting, law firms evaluate a program designed to meet the specific challenges of law practice management such as [PCLaw](#), [Tabs3](#) or [CosmoLex](#).

The unique concerns for law firms go far beyond trust accounting. Law firms also need to be mindful of the way they set rates for services and expenses and even the way they invoice clients. In the next part of this article, we'll look at some of the challenges posed in the billing arena of law practice management.

Part 2: Legal Billing Challenges

In part 1 of this article, we looked at the challenges lawyers face related to trust accounting and their use of QBO. Trust accounting is undoubtedly a problem area for firms trying to use QBO, but it isn't the only challenge they face. Attorneys looking to use QBO for billing are also presented with their own unique set of challenges. Law firms need to be mindful of many different things including how they set rates, how invoices are generated, measuring profitability, and even how income is recognized.

Setting Rates

Law firms often charge different rates based on who did the work and/or the type of work done. While a law firm can set a specific rate for each of their individual services, they can not assign clients different rate levels for the same service -- although rates may be negotiated by the client. This may lead to a long service list and confusion in making sure the right service and rate are chosen. The same is true for expenses, which can also have only a single rate. There are add-ons that can make time tracking and rate management easier, but that may add additional levels of complication and coordination.

Invoicing

When generating invoices for matters, we run into another set of challenges. First, we can not assign an invoice layout to a client. Whatever invoice layout is used when you look at the invoice is what is used for all clients. If you change the invoice layout it will use the same layout for the next client. For firms that have clients with different billing requirements, this makes the process complex. Next, there is no draft billing capability. While it is easy to create an invoice for a client and pull in unbilled time and expenses, the editing process is limited. If you realize that an item is on the wrong invoice and remove it from the bill, it will not return to unbilled automatically. QBO does offer an easy way to view transactions and flexibility in

creating on the fly additions to the invoice, but the on the fly additions are not saved if the invoice is deleted. This can be particularly important if you are adding on soft costs since there is no good way to track and add these automatically within QBO since the cost can not easily be entered as a specific client cost to be billed.

The customization ability on invoices is limited. While it can add a nice summary showing balance forward, new charges, and the amount due, there is no way to automatically include who did the work, to sort or to include a timekeeper summary table, a common preference among law firms. In addition, for firms that do electronic billing not only bills can't be formatted for electronic billing, but there is no way to add both an activity code (A code) and a task code (L code) to a billing item.

While you can enter a flat fee for a client, by merely typing it on the invoice, or by the careful use of groups, the ability to measure the profitability of the flat fee based on the time actually worked is difficult.

Some firms make use of an evergreen retainer when, as the trust balance is reduced, the client is asked to provide additional funds to bring the retainer back to a certain level. There is no way to do this automatically in QBO. This means the firm must constantly run reports and correspond with the client to request funds.

Payment Allocation

The final challenge of billing in QBO is the payment allocation. For many law firms, when a partial payment is received, the payment should be applied first to any outstanding costs and then to fees. In QBO, a partial payment is allocated proportionately across all line items on the bill. This lack of control may be an issue for firms that incur substantial advanced client costs.

One final note, while you are warned by the software if you try to change something, and there is an audit trail, QBO does make it possible to modify an invoice after it has gone out or been paid. While this may be intentional, like adding a credit line or correcting a misspelling, one must be careful in any system that is open to modifications.

Billing for law firms is unique. Law firms face challenges and requirements that businesses in other industries simply do not. Attorneys should seek out integrated and legal-specific billing and accounting solutions such as [PCLaw](#), [Tabs3](#) or [CosmoLex](#) that have been built to meet their unique needs. Keep reading Part 3 of this series where we will dig further into QBO and its ability to track client costs.

Part 3: Client Cost Tracking Challenges

As an attorney, you act as the fiduciary for your clients. If you run into any issues or suffer any missteps in dealing with their financials it is possible that you or your firm will be subject to ethics violations and other penalties. This means that when it comes to tracking client costs it is extremely important that it is done with the utmost care. Often times the solution you or your firm chooses to use in tracking client costs can have a direct impact on how accurately it is done.

There are a number of tools that make it easy to track costs and pull the costs into QBO including pictures of receipts and “automatic” creation of expense reports. QBO also offers an extensive capability to download from bank and credit card accounts. When downloading, it is important to verify the transactions, to be certain that the charges are valid. For law firms, it is equally important to verify that the coding of the transaction is correct and if appropriate the correct client is charged. If a firm does not properly capture client costs and bill them back to the client in an appropriately timely manner, they may lose substantial revenue.

In addition to verifying client allocation, it is also important to track when the invoice should be paid. QBO allows for setup of payment rules for bills and handles this efficiently. The challenges come when:

- Trying to determine if the client has already paid the firm for the expense so that the vendor should be paid.
- Tracking what bills are being held as 3rd party lien claims which will be paid on settlement

While it is possible to create a report of advanced client costs by client and matter, there is not an easy way to remove those clients whose balance has gone to zero. This can make the report grow over time. While one can reconcile transactions to

remove them from the report, it is not always easy to identify the correct transactions to match, especially when there are multiple payments for the same amount.

Another challenge is handling soft costs, those costs that are not actually paid by direct check, but are billed to the customer. This might include internal copies or postage. As a general rule, these costs must be added to the QBO customer invoice at the time of billing. This makes it easy to miss a cost, costing the firm money.

Final Takeaway

QBO offers many good features and numerous add-ons to expand its capability. It is easy to find someone who “knows QBO”, but it may be more difficult to find someone that truly understands how to properly use QBO in a law firm environment. If or when that bookkeeping professional is found or trained, the challenges discussed throughout this 3-part series may mean that QBO is not the best choice for your law firm, and legal-specific software such as [PCLaw](#), [Tabs3](#) or [CosmoLex](#) should be considered when establishing proper accounting practices. Keep in mind that every law firm is different and has different, unique requirements to manage their office. It’s important that your law firm takes the time to properly assess your current setup and find the software and systems that are right for you.

About the Author

Caren Schwartz is the founder of Time & Cents Consultants, LLC and an associate of 35*45 Consulting Global. She specializes in helping legal and other service professionals select, install and get the most out of their practice management, billing, accounting, and other firm specific technologies. Caren is an Advanced Certified Pro Advisor for QuickBooks® and a certified consultant for a number of popular legal practice management systems including CosmoLex. She is a member of the Intuit Accounting Professionals Trainer and Writers Network and has taught classes for Solo Practice University, SCORE, Scaling New Heights and The Sleeter Group. Caren regularly writes reviews and articles for Technolawyer® and the Insightful Accountant. She is also the author of the book QuickBooks for Law Firms.

CosmoLex is a single solution that lets solo attorneys & small law firms manage their practice, billing, AND accounting, all in one login (No QuickBooks™ required). CosmoLex users can eliminate the need to maintain multiple programs because CosmoLex does it all -- including time & expense tracking, billing, business accounting, trust (IOLTA) accounting, calendaring, task, email & document management, even secure client communications-- in one web-based application. Start your [free CosmoLex trial](#) today!