# CPA Practice Management Pro Tips

By Fred Lindsley

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Introduction

The following is a compendium of a lifetime of CPA professional “Tips”. I will be sharing my anecdotal journey for the purpose of helping CPA’s and accountants young and old.

A few comments before we begin about the journey I made from the CPA profession to the software business – how I migrated from a 25 year career as a successful CPA to the business of software development and created ImagineTime Practice Management Software for CPA and Accounting firms.

During the early 1980’s microcomputers were just coming on the scene. They were expensive at the time – $12,000 dollars, but much less expensive than the earlier generation Digital Equipment (DEC) and IBM minicomputers. The desire for increased efficiency led our firm to purchase an Altos computer system running CP/M – a precursor to DOS.

The first system used large floppy disks. Later we added a very expensive 10 megabyte hard drive at a cost of $3,000 dollars. Amazingly, today you can purchase a USB drive that holds 32 gigabytes of storage for $10 dollars. This is the result of Moore’s law – the doubling of the number of transistors on integrated circuits every 18 months.

A few months later we upgraded to the multiuser system (concurrent cpm86 operating system) and purchased eight dumb terminals and keyboards for the staff in the office. That system had a 40 megabyte hard drive at a cost of $5,000 dollars. It was around this time that the first DOS based IBM PC arrived using the slower Intel 8088 microchip. The Altos system used the faster 8086 microchip.

I desperately wanted to automate client monthly bookkeeping and financial statement preparation. In the early days there were very few vendors producing general ledger programs for accountants using the less expensive microcomputer platform. It was the availability of a general ledger program
written by Micronetics Software that actually led us to make the decision to purchase the Altos system.

Using microcomputers during this period of early development was similar to being a pioneer. You never knew when something might burn down your cabin (hard drive). The Altos was very fast compared to the slower PC's, but the hard drives crashed every six months or so, this necessitated the purchase of a very expensive and also unreliable tape backup system to make sure our data was safe – Ha!

During that initial period the staff was preparing our billing by hand. Once a month we would gather up all the timesheets and post the hours and extended dollar amounts to a lengthy 13 column spreadsheet – one row for each client. We had one column for last month’s work in progress, a column for new time, billed time and ending work in progress. We also showed a similar reconciliation for billed amounts. To determine what should be billed we had to refer back to the manual time sheets.

We used our memories and discussions with the staff to prepare the invoices in a manner that we hoped would convince clients to pay for services rendered. I soon realized this process was taking too much time! We were losing money by failing to accurately document time and expenses. Carryovers of time from one period to the next became even more difficult to manage and invoice.

Analysis of staff productivity trends was extremely time consuming and was prepared manually similar to the thirteen column spreadsheet from 1984 shown below:
I began the search for an automated billing system. We eventually ended up purchasing a time and billing system from the only vendor that offered a product that ran on ccpm86. We were disappointed that the software turned out to be buggy and unreliable. Every few months the system would crash and we would be forced to re-key opening balances – but at least we had detail work in progress reports from the previous month; that in itself was a big improvement!

The programmer we used for bug fixes was difficult to work with and often unavailable during a crisis. Even then, the same program bugs often resurfaced the next day. On one such occasion, I noticed from his documentation that the software language was written by Data Access Corporation in Miami – just a short hour from our offices in Fort Lauderdale, Florida. Soon after, I signed up for a week of course instruction and the rest is history. Within six months we were using our own software! Now I had no one to blame for the bugs but myself.
Years later in 1997, just before Y2K, I began writing what was to become that basis for ImagineTime software. During the 1999 Fort Lauderdale Accounting Show, we sold enough software to start a new company!

**How to start your Accounting Firm in Four Steps**

I would like to encourage those of you who are just starting out or have had setbacks. Never give up. Speaking from a challenging personal background, I spent most of my high school years surfing and absent from school. My dismal grades at graduation suggested anything but a career as a CPA. However, with my father’s help, I was able to get accepted to a small liberal arts college in Wisconsin under the condition that I earn good grades in the first year of study. I helped to pay for my education by building log cabins with my Dad during breaks and in the summer months. While attending college in Wisconsin, two professors – one accounting and the other philosophy – inspired me and literally changed my thinking and my life. I am so grateful for their help.

I transferred at the beginning of my third year and graduated from Stetson University in 1972 with a Bachelors in Business Administration and respectable grades. However, I had no clue as to what type of work I should seek and was not prepared for reality.

My family wouldn’t support me, so I needed a job right away. My father had been in sales, so I tried to secure a position selling life insurance. The insurance company personnel tests suggested the accounting profession – too introspective for sales they said. Feeling rebuffed, I knuckled down and accepted a straight commission job selling pots and pans door-to-door; no pride in that. Not surprisingly, a few years later this single experience gave me the courage to start my own accounting firm.

I ditched the sales job several months later and moved to Florida. In trying to figure out what to do with my life, I remembered enjoying the accounting courses taken in college. After spending the better part of a day at the state
employment agency, I followed up on a lead for a bookkeeping job and secured a position as an entry level bookkeeper. Over the next twelve month period, I learned the basics of monthly bookkeeping, tax preparation, general ledger accounting and financial statement presentation. I also learned to efficiently use an adding machine. During my first week I was instructed to add the phone book – a humiliating, finger strengthening exercise. I also learned to survive in an office where everyone chain smoked all day – myself included. Times have certainly changed. Kicking the habit eight years later was more difficult for me than passing the CPA exam.

I started looking in the paper and found a better paying, albeit, short-term position working for a construction company as the assistant to the controller. During this time, I began attending night school to get the additional courses necessary for a major in accounting. Several months after starting work, the construction company controller suggested I consider public accounting and offered arrange an interview that led to employment at a large CPA firm in Miami. I was grateful to the controller as this was a “big break”. I commuted over 100 miles a day to my new position as entry level auditor without the benefit of an air conditioned car. It was quite a trick to arrive in a suit each morning looking “neat and pressed” during the summer months of South Florida.

I received a hailstorm of derogatory comments from my peers during my first months at the CPA firm when they realized I had not completed my accounting degree. Why was I allowed to work there? In fact, I had only completed 4 of the 10 or so required courses. This continuous and palpable air of resentment vaporized when I passed the accounting exam one year later at my first sitting in November 1974 – a full three day affair at the time.

I accepted my dream position soon after as a staff accountant working for one of the Big 8 accounting firms. I was hired because I achieved a 4.0 grade point average in my accounting major while being employed full time.
At the time, the Big 8 (now Big 4) preferred to hire students directly from school with no prior work experience. However, I had successfully sold pots and pans for several months, door-to-door, and knew that creativity and persistence could make a difference in what people think of you. I wouldn’t give up and kept calling until ultimately the HR person gave up and offered me the position – $13,000 a year seemed like a lot of money at the time.

Step 1 – Become technically proficient

This is the first and most important step in starting your own practice. I was fortunate to acquire some great educational benefits and experience before I went on my own. You must have something great to offer and be excited about it in order to succeed in a profession. Mediocrity is the first step towards failure.

It goes without saying, short and sweet, you must become technically proficient and confident in your physical and mental skills before even thinking about starting your own firm. Study, engage your skills, and expose yourself to as many situations as possible before going out on your own. Take extra college courses and develop a specialty. Read technical literature and become a “library of information” that colleagues can draw from. Proficiency with the numeric keypad and learning to accurately type at least 30 words a minute is also essential….and much more common today than when I started.

Mentors are very important. Look for a mentor and associate with individuals that are equally smart, or better yet, smarter than you.

I was most fortunate to have several mentors take me under their wing. Respecting their anonymity, no names will be mentioned. However, one particular CPA – call her “Sandy Bell” – taught me about organization and “to do” lists. Until then, I had unsuccessfully tried to remember long lists of important tasks by memory. Sandy instilled in me the need to be very thorough in my work approach and strive for excellence. I really admired and respected her.
There were many others, each with their own special gift that left lasting impressions on me. For example, observing the care other senior auditors took when preparing work papers encouraged me to improve my penmanship and structure my thoughts before writing them down. During that period, personal computers did not exist, so good penmanship was very important.

Step 2 – How to attract new clients

Gratitude for the knowledge and experience gained was not enough. Working ridiculous, 80 plus hour weeks for several years, getting Mono, and making the partners lots of money gave me the motivation to start my own practice. I had no clients or contacts – except for the ones I worked on at the firm.

My only previous experience in getting business was an attempt to moonlight when working as a bookkeeper. I tried soliciting my own clients by handing out business cards and flyers to local strip mall businesses – “Mr. Balance Sheet” – Accounting advice at a modest price” – was the tagline. This effort proved unsuccessful. I wonder why?

It was unethical to solicit the clients of my employer, but I had a suspicion that some of them might join me later if I went out on my own. Outside of that there were a few family friends that were willing to hire me. At this point, I had decided that a partner was necessary to launch the firm. I didn’t have the extra $1,000 in funds necessary to lease the copier – a necessity at the time.

After pooling our funds, vacation, severance pay and the few clients, we signed an inexpensive one–room lease for one year in a four story building in downtown Fort Lauderdale, Florida. Initially, the building tenants became my clients and canvassing ground. I looked for opportunity everywhere and spoke with anyone who would listen.
Business trickled in, some from the phonebook, some from elevator conversations. In the first year, we grossed a little over $40,000 and each netted about a $15,000 salary...we also played a lot of tennis.

Today, social media is so much more helpful in getting started, but it doesn’t replace the handshake, or the smile. Getting a face-to-face encounter with your prospect is the best way to create a memory. Join the Chamber of Commerce, or a meetup.com group in your area where you can get together with other people that are interested in the same thing as you.

Believe it or not, many people are actively searching for a good accountant and can’t find one! Hone your talents and skills and show up for meetings. Listen and ask questions – that’s right “LISTEN”. Ask questions, and offer intelligent comments that are on topic. Don’t drone on about your skills and qualifications; instead, focus on your prospects interests and needs. Get them talking. The topic doesn’t need to have any connection with taxes or accounting. Just express an intelligent opinion and be friendly. The appropriate time to disclose your occupation is when you introduce yourself, but keep it short.

My wife was a corporate sales executive in her own right and the inspiration and marketing visionary behind ImagineTime. She had to repeatedly remind me when we were first starting out not to drone on about the features of our software when speaking to prospective clients – but rather to listen and ask questions about their needs.

This attitude of “offering up” with joy attracts people to you, and before you know it they will ask you if you are taking on work – but, most likely, not at the first or second meeting. You may want to begin part of this process before you leave your current employment.
Step 3 – How to fire your clients

When you first start out, the tendency is strong to take on any client that comes your way. We did this and ended up with some good and some undesirable clients. Just like people everywhere, there is the dishonest client, non-paying client, disorganized client, generous and appreciative client, demanding client that pays and the demanding client that doesn’t pay.

Motivated by fear of being unable to pay our bills, we wasted quite a bit of time and energy on undesirable clients. Frankly, the fees made from this type of client were more than offset by stress and time wasted on a dysfunctional relationship. Do you really want to represent a dishonest client during an IRS audit? If so, you will have to repeatedly practice the phrase “I'll get back to you on that”.

Don’t get me wrong, it’s impossible not to have some irritating and questionable clients. It’s unrealistic to think that you can avoid basic human nature – some folks have very successful “cloaking devices”. However, establish a profile of the type of client you want and the ones you won’t accept. When a client reveals undesirable traits, remove yourself from the relationship as quickly as possible...whether it costs you some money or not.

It is also very helpful to develop a close relationship with a good lawyer. It can be someone you meet on the tennis court, golf course or any venue for that matter. When you’re in a spot, you need someone to check your thinking and help you determine the proper course of action.

Step 4 – Where do I go from here?

Now that you are skilled and proficient, have attracted and weeded out certain clients, you have achieved “lift off” and started your Accounting Practice. You’re in the saddle now and riding the horse, but you may not know how to
reign him in or point him in the right direction. This is where developing successful practice management skills become so important.

Software Solutions to Common Practice Management Pitfalls

After managing two CPA firms for a period of 25 years, in 1999 I changed careers and became a developer of practice management software for the CPA industry. After consulting with thousands of CPA and accounting industry clients, I would like to document some of the most common challenges that arise in practice management.

Regardless of a firm’s size or management style some of the common pitfalls in practice management can be attributed to one of the following two areas:

1. Lack of compatibility, cooperation and unified goals.
2. Failure to effectively implement effective practice management software.

Typical roadblocks against compatibility, cooperation and unified goals

From my experience, a tone of cooperation and mutual respect is always more effective than control and dominance. Would you be surprised to know that many accounting firms have a top-down controlling culture that is both rife with intimidation, suspicion and mistrust? Firm management styles that are driven by ego and intimidation create suspicion and mistrust among employees. This reduces the quality of client service and creates an atmosphere of conflict and disruption. Employees simply don’t work well in this kind of environment and high turnover is a common problem.

One of my first experiences involved a national firm that established its offices by acquiring the firms of local practitioners. One former owner – let’s call him Dave – did not integrate well with the new political environment. As a
young staff accountant, I noticed that the “corporate” partners coming “up the ladder” looked down on Dave – he wasn’t from the same school. This attitude trickled down to the staff who were encouraged not to follow his practices. It was like working for two firms. This created inefficiency since much of the work given to the staff during tax season was from clients that Dave generated years before. Should I do it Dave’s way, or the “right” way?

I personally found Dave to be very engaging and realized why he was so successful in developing business. He was very knowledgeable about taxes and easy to understand and work with. Regardless, he was eschewed by the other ‘corporate’ partners. I don’t think Dave cared since he probably sold his former practice at a nice profit. The lack of unity among the partners in this office reduced client retention and undercut the efficiency of the staff and consequently reduced firm profits.

Another example involves conflicting lifestyles of the owner–partners. A small firm that courts its new clients by taking prospects to long lunches over drinks may not merge well with an individual practitioner that grew up in a family of alcoholics even though their clients may be in the same industry. Sound too personal? Happens all the time.

In the accounting partnership, individual traits and preferences have a huge impact on the success of the firm. The sole practitioner that manages a large firm with a talented support staff might be more successful by virtue of the unified set of goals stemming from the personality of one individual.

The lowest common denominator in the accounting profession is the individual. Each professional develops a set of skills, passes exams, and earns degrees and titles. While there are overlapping skills, there are also many distinctions among individuals. Some individuals may specialize in divorce and expert witness testimony, others tax or audit. The clients you attract are based on your distinct personality and your goals. In order to succeed we must achieve a consensus among the staff and partners concerning common goals and practices.
Ironically, much of the staff accountant’s work is done in isolation. After all, you don’t require someone to hold the keyboard when analyzing fixed assets. However, you may need to ask a question and have someone review your work. You must also be aware of firm policies and procedures.

Uniform practices, quality control, transparency and realistic goals are required to ensure effective firm administration. This contrasts starkly with firms that encourage excessive overtime and not reporting all hours to avoid budget overruns – such policies lead to high staff turnover and always cost the firm more in the long run.

Ideally, individual skills and talents should complement each other. For example, a small firm doing monthly bookkeeping would be well advised to develop a tax specialty rather than attempting SEC financial audits.

In actual practice the variations in partner style and personality among small firms amazed me when I first began developing software for the accounting industry. Some firms were well organized and successful; others had everyone rowing the boat in different directions (some staff without paddles) and operated in chaos without consensus about firm focus, practice development, billing, etc. This type of firm would often have several individuals call with the same technical support question. Many partners cannot agree on simple billing strategies and are unwilling to hold themselves accountable to any kind of realization or collections standard.

Local firms that merge and grow to a size of 30 to 40 individuals often lack consensus about rules of operation. After the initial honeymoon and new letterhead, below the surface is an embattled group of individuals with different goals and agendas. This usually results in large accounts receivables, hidden write-offs, jealousy between the partners and discord among the staff.

In this environment, information about firm results is “managed” often by delay in an attempt to manipulate and control others. As noted earlier, an accepted practice by one partner might be subject to be reprimanded by
another. In this environment partners often make derogatory comments about the other partners directly to the staff. This is a ship that’s about to sink.

Of paramount importance to successful practice management should be the generation of common goals and policies that staff and partners willingly embrace in a common culture. Without positive consensus, your firm will be forced to change or fail.

Failure to effectively implement Practice Management Software

Effective practice management software can help to isolate and, in many cases, avoid some of the common pitfalls previously discussed.

In practice, I have seen a wide variety of software used among firms. Some firms as large as eight to twelve staff are still maintaining manual systems for just about everything except their tax software and general ledger system. Many owners fear a loss of control and refuse to implement new software. Use of spreadsheets for tasks more complex than they were designed is a common avoidance practice and reflects this fear.

Some firms habitually record billable time and accumulate it against progress bills in the hopes that time overruns can be recovered at some point against future work, resulting in multiple pages of time slips that must be re-analyzed each time a new billing is sent out. Partners that claim this is a way to remind them to recover the amount against future invoicing are in reality failing to promptly address the problem. This actually make matters worse by cluttering the database with useless information and violates the principle of matching revenue and expenses in the correct period.

The best way to address an overrun with a client is when it occurs at the point in time when it’s fresh in everyone’s mind. A better practice would be to write–off the time and record the poor realization. Clients with poor realization are not forgotten – fees must be increased, or the client relationship terminated. This can’t occur if the situation is not exposed to daylight.
Successful implementation of time and billing software ensures that partners are held accountable when it comes to productivity, realization and collections. Workflow management systems ensure that partners schedule staff on a timely basis in cooperation with other partners and avoid conflict. This ensures that deadlines and client expectations are met.

In difficult situations when partners disagree it’s very important to have an accurate measurement and tracking software that reports the facts about profit contributions and documents task assignments. Accurate information reduces controversy and allows you to hold individuals accountable to firm profit goals and deadlines. Once you are able to hold people accountable you can more easily make effective decisions about compensation and separation, when appropriate.
Another example from my own experience involved a partner that suffered from addiction that worsened over time. The individual’s productivity dropped and the number of mistakes increased. Initially, chargeable time that should have been written off was hidden in work in process masking the actual contribution of the individual. Deadlines were also missed since the partner in question had refused to implement due date software. After the write–downs were addressed and recorded we were able to measure the partner’s actual contribution to the bottom line and make a fair decision for all concerned. Ultimately, the partnership ended. A good time and billing system was essential in helping us reach this conclusion.

These situations have a human element that’s very painful. In order to be objective and for your firm to not only survive – but thrive – you must have accurate practice management software that measures productivity and your client’s contribution to the bottom line.

The previous report example shows productivity for a particular partner. Work in progress and aged accounts receivable are depicted, along with time slip production, realization, billing write–offs and average number of days to collect – the essential information needed to determine partner effectiveness. When properly implemented, software can bring conflicts into resolution by eliminating confusion and providing factual, irrefutable data.

**Practice Managements Essentials**

**Value Billing or Time & Billing for the local CPA?**

More than a few authors and reviewers in recent years seem to be minimizing the importance of tracking time for billing. Calling it “myopic and prosaic” they promote value billing as a replacement. However, my experience as a former partner in two successful CPA firms has taught me *both value and time based billing are indispensable.*
Value billing is not a new idea, but the terminology oversimplifies the fee setting and invoicing process if viewed as a complete replacement for time tracking. After all, what determines and sets the limits on value?

Keeping track of your time helps verify you are billing correctly. It creates a correlation between the cost of the service provided in relation to the fee charged. If it wasn’t necessary to pay your staff a salary, if all staff were paid on a bonus plan, then all services could be value billed without relation to cost; just pay the staff a percentage. However, since most firms can’t operate using that paradigm and salaries must be paid irrespective of realization and collections, billing staff time appropriately becomes critical. For those not familiar with the value billing process, click here to view the preparation of a sample invoice.

The following are examples of a traditional detail time slip invoice as compared to an invoice with value based components.
## Detail time slip invoice

**Castle Realty**  
1441 S. Ocean Blvd  
Boca Casa, CA 33432

<table>
<thead>
<tr>
<th>Date</th>
<th>Staff</th>
<th>Explanation</th>
<th>Hours</th>
<th>Rate</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>01/14/11</td>
<td>FOL</td>
<td>Compilation of year end financial statements.</td>
<td>1.50</td>
<td>150.00</td>
<td>$225.00</td>
</tr>
<tr>
<td>01/15/11</td>
<td>JAS</td>
<td>Year end adjustments and postings to trial balance.</td>
<td>4.00</td>
<td>50.00</td>
<td>200.00</td>
</tr>
<tr>
<td>01/17/11</td>
<td>FOL</td>
<td>Additional journal entries and account analysis.</td>
<td>2.00</td>
<td>150.00</td>
<td>300.00</td>
</tr>
<tr>
<td>01/20/11</td>
<td>JAS</td>
<td>Statement draft.</td>
<td>2.00</td>
<td>50.00</td>
<td>100.00</td>
</tr>
<tr>
<td>01/21/11</td>
<td>FOL</td>
<td>Review statements.</td>
<td>0.50</td>
<td>150.00</td>
<td>75.00</td>
</tr>
<tr>
<td>01/22/11</td>
<td>FOL</td>
<td>Additional statement revisions.</td>
<td>1.00</td>
<td>150.00</td>
<td>150.00</td>
</tr>
</tbody>
</table>

**Sub total:** 11.00  
**Total:** 1,050.00

<table>
<thead>
<tr>
<th>Date</th>
<th>Staff</th>
<th>Explanation</th>
<th>Hours</th>
<th>Rate</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>01/22/11</td>
<td>JAS</td>
<td>Revise depreciation.</td>
<td>1.00</td>
<td>90.00</td>
<td>90.00</td>
</tr>
<tr>
<td>01/24/11</td>
<td>FOL</td>
<td>Preparation of corporation tax returns - depreciation and Alt-Min.</td>
<td>3.00</td>
<td>150.00</td>
<td>450.00</td>
</tr>
<tr>
<td>01/25/11</td>
<td>FOL</td>
<td>Complete Tax Returns.</td>
<td>1.00</td>
<td>150.00</td>
<td>150.00</td>
</tr>
</tbody>
</table>

**Sub total:** 5.00  
**Total:** 690.00

**Total Engagement Dollars:** $1,740.00

**Total Charges:** 16.00  
**Total:** $1,740.00
The following factors, while not an exhaustive list, can serve as determinants of value when value billing is used in conjunction with time tracking:

1. **Competition**
   Firms in your area may charge lower or higher fees. Clients concerned solely with price may leave your firm for another. Effective time and billing software provides the information and assurance that your services are correctly valued, or if your firm management needs improvement.

2. **Competence**
   There is no replacement for professional competence in the determination of fees. Competence is one of the key factors that ensures quality service. Competence is also required as a business professional to ensure proper management of your cost structure and revenue realization.
3. **Confidence and self-esteem are important.**

Unfortunately, competence may not be recognized by all potential clients. Some potential clients may be best served by a lower cost competitor. Unless you are certain of yourself and confident in your services, you will be afraid to bill for the true value of your services and most likely place an inordinate amount of significance on what the competition is doing. Symptoms of this problem are revealed by the amount of work in progress that remains unbilled on a firm’s pre-billing report. Many CPAs and Accountants prefer to avoid conflict, hoping to resolve any conflict over the value of services at some more convenient and future date. Be assured that a more convenient future date usually never arrives. Good self-esteem ensures that fees are billed in a timely fashion while the memory of the service is still fresh in the client’s mind and facts are clear to assist in the resolution of any conflicts.

4. **Your personal and business relationship with the client**

Trust and confidence are earned over time based on ongoing performance results. The well-informed practitioner is in a position to please his or her clients and provide them with a higher level of service. Good practice management software can put you in the position where your clients will want to pay you more. When was the last time a client sent you a bonus fee?

5. **Listen to your client**

Listening helps you identify and understand their needs. Providing “white space” in conversations instead of showing off knowledge allows the client the necessary time to react to your comments and feel satisfied that they have been heard. Many times clients need a good financial psychologist more than just a number cruncher.

6. **Labor and billing costs per hour**

Some firms work their staff to death in an attempt to compensate for low invoiced realization rates (the ratio of the amounts invoiced to gross recorded chargeable time). This policy is self-defeating since it leads to low morale and cannot possibly create prosperity and abundance in the long run. Knowledge of hourly labor costs and billing rates assists the practitioner in formulating the cost of delivering services to the client. This knowledge should impact billing decisions just as a profit and loss statement affects earnings per share and the value of a stock.
A good example of how a properly maintained time and billing system can assist the practitioner in value billing and recovering the cost of services is shown in the following graph which depicts the ratio of chargeable time, based on an hourly rate, to the amount actually realized on invoiced services.

The above graph compares, for each staff person, over a one year period, the gross recorded chargeable time included in the amounts invoiced for that time period. Each staff’s performance is further broken down by billing partner. The first staff “Fritz Landon” at left shows invoiced realization for partner “FOL” slightly higher than gross chargeable time, the opposite is true for the last partner “POW” displayed for this staff person.

The slight variations suggest a peaceful coexistence between value billing and the recorded time at standard rates. Are the variations attributable to staff performance or client efficiencies?
Staff Performance Accountability – Who’s Responsible?

While there may be many ways to “successfully” manage your firm, achieving peak performance is not easy. One fundamental step toward optimal performance is to establish a culture of honesty and transparency in your firm. In such a culture you can establish performance goals for your staff and see those goals taken to heart because your staff understands what is expected and trusts performance assessments will be fact based and objective.

Performance is usually assessed on some very basic metrics such as:

1. Quantity of work hours, both chargeable and non-chargeable
2. Efficiency of work
3. Ability to generate clients
4. Ability to work as a team member

It is important to have reporting mechanisms that quantify these goals and allow you to objectively measure performance at periodic intervals. At the same time, you must also evaluate these reports in the context of the firm culture and dynamic using common sense, honesty and realistic expectations: things not necessarily taught in college or tested for on the CPA exam but derived from your native instincts and the school of hard knocks.

In the early days – before computers – our CPA firm spent hours tabulating staff productivity on thirteen column spreadsheets like the example shown below for 1984:
Computer software has made it possible for many firms today to measure staff efficiency by comparing chargeable time to billed realization – a next to impossible task if performed manually. If you click to enlarge the sample report below, you will see the areas where this employee works most efficiently, with the highest hourly rate and lowest fee adjustments and accordingly, the best realization. You will also see the amount of time spent on non-chargeable activities.
Many popular time and billing software products have reports similar to this one. Most also have reports that breakdown the metrics by client and show staff contribution to firm gross revenues by year along with information about staff salary and costs. This allows firms to develop cost multipliers, 2, 3, 4 times cost, etc. and also determine whether that ratio is improving or deteriorating over time. A variety of additional report examples are provided later in this book under the chapter entitled “Effective Practice Management Reporting”.
Reports like this are essential, they should be both implemented and relied upon. As mentioned previously, it is also essential to evaluate performance reports in the context of the firm’s management dynamic and culture.

One of my first jobs out of college was working for a “Big 8” accounting firm. Staff members were expected to generate at least 2,000 chargeable hours a year, as well as continue professional education and assist in practice development. I was given responsibility as a “semi-senior” during the annual audit of a local governmental port authority. Enterprise fund accounting was new to me at the time, and I was excited about implementing the fund accounting methods learned while attending school.

During the audit, however, it became increasingly clear the financial statement presentation of fund accounting was significantly incorrect for prior years. It also became clear the amount of time needed to properly research and correct the issue was not allocated in the budget. This was a fixed fee job.

I received little support when I informed the manager and partner about the problems with the financial presentation in prior years. The manager was not excited about supervising a job that wouldn’t be brought in under budget. The partner was not forthcoming and seemed irritated. In hindsight, I can see that he was probably embarrassed that the presentation was botched the prior year, but because I was proud to be a CPA and felt that it meant something, I corrected the statements on my own time – unpaid overtime – and didn’t record all the time I spent doing this, even though I was told I should. Staff that ran over budget didn’t last long. That was the clear message. The firm’s culture of fear trumped any attempt at transparency and honesty.

The truth is that this client either should have been let go or should have been paying for the resources they consumed. The firm was unwilling to confront that reality, and my own fear of retaliation kept my time reports from revealing the true cost of servicing this client. Performance assessments and reporting tools can only reflect the quality of the data provided, and that input depends on the culture of the firm.
Due Date Management Software – the basics

Many years ago I worked for a small local firm that prepared several hundred 1040’s during tax season. At the time, spreadsheet software was just coming into its own with Lotus 123® having most of the market share. Our firm still managed deadlines on a thirteen column manual spreadsheet that was redone each year.

Individual tax forms not completed by the April due date would be extended on IRS Form 4868. Extensions along with any outstanding taxes were sent certified mail, return receipt requested to ensure that no issues would arise with regard to timely submission. Once the extension was mailed, the client’s 1040 task was marked as extended on the manual spreadsheet.

It was always a concern that an important client from a previous year would not be carried over to the manual spreadsheet for the next year. In this particular year – the early 1980’s – one of the partner’s important clients missed the extension deadline because of an oversight of the kind just described.

As you no doubt are aware, the penalties for late filing are stiff and in cases like these become the responsibility of the preparer. Occasionally, the CPA can plead for mercy and the IRS abates the penalty. Nevertheless, the client becomes aware of the situation and confidence is lost.

Several days after the deadline on my way to lunch, I observed the responsible person take the late extension and walk it to the mailbox outside our office building. Before opening the mailbox, the extension was dropped in the mud. The responsible person then began stepping on the letter, picked it up and twisted it until the address was barely visible. After this unusual procedure, the letter was dropped in the mailbox. Several weeks later, the extension came back approved!

Before considering unscrupulous and extreme steps such as these, I recommend you implement a simple and reliable due date management system.
This system should, at the very least, have the ability to automatically rollover deadlines from one year to the next for any active client. Also, a basic report should ensure that active clients have an in-process or completed task in the system. To minimize time spent during setup, similar client types should be able to be setup as a group through a simple cloning procedure.

Each task in the due date system should have a start and due date, as well as extension and completion dates. The task should also be capable of being assigned to a principal preparer and reviewer. Due dates should auto-calculate based on the characteristics established for the master task. In unusual circumstances, you should be able to override calculated due dates – for example, in the situation where several years 1040’s are prepared well after the original due date but in accordance with an agreed deadline with the IRS.

Tasks should store notes about the status and progress of the work and these notes should be available for review when a fee change is considered or before preparation of next year’s work.

The frequency of tasks should be flexible. Many tasks fall due on weekly, monthly, semi-monthly, quarterly or specific dates, such as an IRS notice response. There should also be some permission mechanism that prevents active tasks from being deleted or reassigned to inactive staff. The ability to break down tasks into several simple stages is also helpful. Shown below is a due date report for 1040’s not competed and waiting to be put on extension.
Due Date Extension Report

Due Date Extension Report – Ctrl+Click to enlarge

The following screenshot displays the split form where the filtered 1040 items are updated and notes made once extensions are completed.

Deadline Management Screen

Deadline Management Screen – Ctrl+Click to enlarge
The due date system should also be capable of generating reports of tasks assigned to staff for a specific date range as well as tasks assigned to particular client groups.

**How necessary are Staff utilization and Workflow planning tools?**

Staff utilization is the productive and efficient use of your firm’s primary resource: available staff hours. The primary goal of any accounting practice is to stay busy and get paid for the work performed. This usually requires some form of workflow tracking, but needs may vary greatly depending on the type and size of the firm.

Workflow as discussed and defined in current accounting publications is broad and somewhat ambiguous. It could, for example, mean the process through which expense receipts are reimbursed to staff. Or it could refer to the stages required in running an audit. For our purposes here, workflow refers to the sequence of steps necessary to accomplish any given process or task.

Starting out, an accounting practice requires clientele, and clients must be convinced your firm’s services will help them. At this stage of growth, little workflow planning is required: work is performed on a schedule that is convenient for the client.

Small one and two person firms grossing under $500,000 a year usually have a good intuitive idea of their capacity and how busy they will be during various peak and downtime periods. The tax season may require working on weekends, but generally the biggest question is when to hire new staff. Workflow and staff utilization planning at this level usually involves a due date monitor that lists the various main tasks, when and by whom each task is accomplished, and whether it is completed or not – not rocket science! While many firms use a Microsoft Excel spreadsheet to accomplish this task, a more standardized relational database is usually less prone to error and more accessible by other members of the firm.
Once a firm moves beyond simple deadline management or grows beyond minimal staffing, detail tracking of workflow becomes necessary in order to effectively measure staff utilization. For example, if your firm has more than 500 clients and performs audits or reviews, year-end as well as tax and monthly services, the questions around staff utilization become more difficult to assess. Are the work requirements well matched to existing staff, or are skill sets missing? Will the staff with the right skill levels be available for the work when it is scheduled? Are some staff underutilized? Over utilized? What staff hiring might you need to accommodate the new clients you are adding?

The effective use of staff at this level generally requires scheduling the work ahead and matching available staff hours with the work requirements and staff skill levels. This involves planning the sequence and timing of steps necessary to accomplish a task or group of tasks or engagements over specific periods: usually months, quarters or years.

In a good workflow management tool, each main task involving more than one or two simple steps can be broken down into specific subtasks, with each subtask then assigned to staff, along with a time requirement, start and due date. These subtasks can often be linked together, so step two proceeds only after completion of step one. Or, alternatively, the subtasks can be defined so any or all of them can be concurrent. Good reporting will now inform you of who is busy doing what, and more importantly, where the potential logjams may occur, as the aggregation of the attributes for these tasks allows us to project detailed staff utilization.
The preceding graph shows budgeted hours for the tax season for two staff: Fritz Landon and Jay Pernell. Just a quick glance shows that Jay is underutilized during the first part of the tax season and that Fritz has too many things scheduled for the week of April 15th.

Combine all this workflow and deadline management with an integrated time and billing system, and you can also discover how closely recorded time records match with projected budgets. With that information, you have the means for determining whether your planning approach is efficient and effective.

Effective Practice Management Reporting Minimizes Write–Offs and Write–Downs

"Firms don't recognize the single biggest controllable cost to the CPA firms is work–in–process write–offs" Rosenberg, M. L. (1994), The 10 Biggest Mistakes CPA Firms Make. The Journal of Accountancy, 177(1), 105–108
Stark statement? Yes. A prosaic one too? Possibly, but a metric that matters intensely nonetheless. Excessive write-offs and write-downs can lead to the outright failure of a firm even in a robust economy. A more common occurrence is reduced profitability that escapes detection and/or correction during good times but becomes a potentially fatal vulnerability to the firm during economic downturns.

There are three main lines of analysis that help to ensure the firm has adequate understanding and control of write-offs and write-downs along with client and staff performance:

- Realization and contribution reporting – the comparison of recorded time to amounts invoiced. Contribution reporting measures the staff’s total contribution to firm revenue, i.e. a staff with average realization may compensate by contributing more revenue through recording more chargeable time.
- Collections – invoice write-offs and bad debts.
- Non-chargeable – excessive time spent on administrative functions that could be handled more efficiently.

Realization reporting should be looked at from four angles.

- Realization and contribution reporting by employee and partner
- Realization reporting by client
- Realization ratio by type of business
- Trend reporting – is performance improving or declining over time?

Graphical Depiction of Realization by Partner and Staff

The ImagineTime graphical analysis that follows illustrates the kind of information needed to allow effective review of realization ratios for employees individually and as a group. It depicts the total chargeable time and net realization percentage by employee grouped by partner for one year – in this example there are three partners shown. The advantage presentation is that you get a quick idea of much each employee produces for each partner. In this graph the first two columns for each partner grouping shows the total time
and realization for the employee “FOL”. It quickly becomes apparent which partner “FOL” works for the most and his contribution in total time and realization.

Realization by Partner and Staff – Ctrl+Click to enlarge

Staff Time Activity by Code

The report example below is prepared to show performance totals by work code for a quarter and year but you can review this information for time periods you specify. The report shows the ratio of chargeable to non-chargeable time and for chargeable time the amounts realized and effective rate per hour.

In this example, the employee had approximately 2,000 chargeable hours of time and additional 400 hours of non-chargeable time – a hard worker. Although this employee has quite a bit of non-chargeable time it hasn’t hurt efficiency – the amount realized of $173,192 as a ratio of the total time at standard rates is almost 95%.
Another useful report would show the hours and ratio of chargeable to non-chargeable time over a user specified range of months and years.

### Staff Activity by Code

<table>
<thead>
<tr>
<th>Staff: Pernell, Joy (Due Date User)</th>
<th>ImagineTime Demo</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Staff Activity by Code</strong></td>
<td><strong>Staff Activity by Client</strong></td>
</tr>
<tr>
<td><strong>Current Period</strong></td>
<td><strong>Year To Date</strong></td>
</tr>
<tr>
<td>From 10/1/2011 to 12/31/2011</td>
<td>From 1/1/2011 to 12/31/2011</td>
</tr>
<tr>
<td>%</td>
<td>Hour</td>
</tr>
<tr>
<td>---</td>
<td>------</td>
</tr>
<tr>
<td><strong>ET</strong> Monthly Compilation Work</td>
<td>31.25%</td>
</tr>
<tr>
<td><strong>ET</strong> Compilation - Year end</td>
<td>26.65%</td>
</tr>
<tr>
<td><strong>ET</strong> Management Advisory - Computer</td>
<td>5.72%</td>
</tr>
<tr>
<td><strong>ET</strong> Management Advisory - Consulting</td>
<td>5.05%</td>
</tr>
<tr>
<td><strong>ET</strong> Review - Analytical Procedures</td>
<td>0.09%</td>
</tr>
<tr>
<td><strong>ET</strong> Preparation of Individual Income Tax Returns</td>
<td>11.25%</td>
</tr>
<tr>
<td><strong>ET</strong> Miscellaneous Income</td>
<td>0.60%</td>
</tr>
<tr>
<td><strong>ET</strong> Preparation of Partnership Tax Returns</td>
<td>6.15%</td>
</tr>
<tr>
<td><strong>ET</strong> Pre - Paid Partnership Tax Returns</td>
<td>7.55%</td>
</tr>
<tr>
<td><strong>ET</strong> Preparation of Corporation Income Tax Returns</td>
<td>0.09%</td>
</tr>
<tr>
<td><strong>ET</strong> Preparation of Corporation Income Tax Returns</td>
<td>0.09%</td>
</tr>
<tr>
<td><strong>ET</strong> Pre - Paid Corporation Tax Returns</td>
<td>14.18%</td>
</tr>
<tr>
<td><strong>ET</strong> Preparation of Payroll Tax Returns</td>
<td>1.12%</td>
</tr>
<tr>
<td><strong>ET</strong> Chargeable: Total</td>
<td>66.70%</td>
</tr>
<tr>
<td><strong>ET</strong> Non-Chargeable: Total</td>
<td>33.30%</td>
</tr>
<tr>
<td><strong>ET</strong> Gross Totals</td>
<td>100.00%</td>
</tr>
</tbody>
</table>

### Additional Notes

Staff Activity by Code – Ctrl+Click to enlarge

Staff Time Activity by Client

Another variation of the previous report shows the same information by client – rather than work code allowing you to quickly determine from among the two presentations the staff’s more profitable work areas and the clients that perform the best under his management.
Staff Chargeable Hours by Month and Year

This report can be used as a good indicator of consistent, deteriorating or improving trends with respect to reported chargeable time. When evaluating the hourly information as a performance indicator you should be aware of the staff realization trends during the same periods.

Invoiced Realization by Client grouped by Staff and Partner

This report shows the time at standard and the amount of billing adjustments recorded for a particular staff within the amounts invoiced for a selected date range. You should also be able to filter this type of report for a...
particular partner. The total hours, rate per hour and realization percentage are also shown.

Another variation of this report (not shown) would depict the realization statistics for paid invoices in a selected period which allows firm management to base compensation and bonus programs on paid rather than invoiced performance.

### Invoiced Realization

#### Activity From 1/1/2011 to 12/31/2011

#### Invoiced Slips & Realization Adjustments [excludes expense]

<table>
<thead>
<tr>
<th>Client Name</th>
<th>Slips @Std</th>
<th>Write Up/Down</th>
<th>Progress</th>
<th>Invoiced Bef Expenses</th>
<th>Hours</th>
<th>Realized Per Hour</th>
<th>Realized Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>FOL - Landon, Fritz O. (power user)</td>
<td>1,052.50</td>
<td>210.00</td>
<td>0.00</td>
<td>0.00</td>
<td>548.50</td>
<td>14.50</td>
<td>118.71</td>
</tr>
<tr>
<td>All Rise Robes &amp; Tassles</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>1,711.75</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>All that Glitters Ain’t Gold</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>777.00</td>
<td>9.35</td>
<td>81.79</td>
</tr>
<tr>
<td>All That Jazz Music Store</td>
<td>1,165.00</td>
<td>388.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>American Trading Co.</td>
<td>352.50</td>
<td>17.00</td>
<td>0.00</td>
<td>0.00</td>
<td>548.50</td>
<td>8.75</td>
<td>145.47</td>
</tr>
<tr>
<td>Anderson, David</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>Bagel Brothers Kosher Distributors</td>
<td>562.50</td>
<td>-17.00</td>
<td>0.00</td>
<td>0.00</td>
<td>548.50</td>
<td>5.75</td>
<td>145.47</td>
</tr>
<tr>
<td>Bartoc, Randolph E.</td>
<td>225.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>225.00</td>
<td>1.50</td>
<td>150.00</td>
</tr>
<tr>
<td>Barton, Cravan</td>
<td>1,396.25</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>1,306.25</td>
<td>8.00</td>
<td>153.28</td>
</tr>
<tr>
<td>Beaches Surf Shop</td>
<td>417.50</td>
<td>-38.00</td>
<td>0.00</td>
<td>0.00</td>
<td>599.50</td>
<td>8.50</td>
<td>114.14</td>
</tr>
<tr>
<td>Big Tass Tugboat, Intl.</td>
<td>0.00</td>
<td>815.00</td>
<td>0.00</td>
<td>0.00</td>
<td>825.00</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>Bissell Deep Cleaning Solutions</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>Bread, Pan</td>
<td>187.50</td>
<td>1.00</td>
<td>0.00</td>
<td>0.00</td>
<td>188.50</td>
<td>1.25</td>
<td>150.80</td>
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<td>Breowski Distributors</td>
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<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
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<tr>
<td>Britchow, Dottie</td>
<td>812.50</td>
<td>12.50</td>
<td>0.00</td>
<td>0.00</td>
<td>825.00</td>
<td>6.50</td>
<td>156.93</td>
</tr>
<tr>
<td>Brooks, Garth</td>
<td>1,050.00</td>
<td>4.00</td>
<td>0.00</td>
<td>0.00</td>
<td>1,054.00</td>
<td>7.00</td>
<td>150.37</td>
</tr>
</tbody>
</table>

Client Snapshot by Initials (Partner)

During the early 1980's I managed a local CPA firm in Fort Lauderdale with three partners. It was very important to know how much each partner contributed to the firm billings. Other information such as realization on invoicing was unavailable. A sample report from those days is shown below:
The next report example shows the performance statistics for a particular type of client or line of business filtered by partner and sorted by descending realization percentage. Shown here is information about the realization rate, collection experience and the amount of receivable and work in progress carry for this partner and client type. It also shows the average days to collect an
outstanding invoice. The realization ratio becomes much less important when the client takes over six months to pay an invoice!

**Client Invoiced Amounts for Selected Periods**

Many CPA’s and accountants want to know specifics about client performance – for example, what clients contribute the most revenue, which areas of work are most profitable and what staff worked on specific clients. The first example that follows lists invoiced clients for a selected period showing useful information such as amounts invoiced, billing adjustments, labor costs, total hours, net realization and other information. You should also, at your option, be able to view this information by work code.
Client Time Slip Activity and Realization by Work Code

When detailed information about client performance is required, the report below shows client performance by work code for a selected period along with a separate presentation of the staff responsible for performing the work. Now you know what areas of work were most profitable and which staff were responsible – the essential information required for effective decision making!

### Client Time Slip Activity & Realization by Workcode

Client ID: "CREAT"

<table>
<thead>
<tr>
<th>Workcode</th>
<th>Activity Description</th>
<th>% Hours</th>
<th>% Arr@Std</th>
<th>Adjust</th>
<th>Net</th>
<th>% Hours</th>
<th>% Arr@Std</th>
<th>Adjust</th>
<th>Net</th>
</tr>
</thead>
<tbody>
<tr>
<td>ACON</td>
<td>Auditing-Confirmations</td>
<td>0.00%</td>
<td>0.00%</td>
<td>0.00%</td>
<td>0.00%</td>
<td>1.00%</td>
<td>0.00</td>
<td>0.00%</td>
<td>0.00%</td>
</tr>
<tr>
<td>M&amp;O</td>
<td>Management Advisory - Consulting</td>
<td>61.62%</td>
<td>50.00%</td>
<td>38.68%</td>
<td>8,652.50</td>
<td>50.00%</td>
<td>0.00%</td>
<td>0.00%</td>
<td>0.00%</td>
</tr>
<tr>
<td>T&amp;D</td>
<td>Taxation Preparation</td>
<td>0.00%</td>
<td>0.00%</td>
<td>0.00%</td>
<td>0.00%</td>
<td>0.00%</td>
<td>0.00</td>
<td>0.00%</td>
<td>0.00%</td>
</tr>
<tr>
<td>T&amp;D</td>
<td>Taxation Preparation</td>
<td>0.00%</td>
<td>0.00%</td>
<td>0.00%</td>
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<td>0.00%</td>
<td>0.00</td>
<td>0.00%</td>
<td>0.00%</td>
</tr>
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<td>T&amp;D</td>
<td>Taxation Preparation</td>
<td>0.00%</td>
<td>0.00%</td>
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<td>T&amp;D</td>
<td>Taxation Preparation</td>
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<td>T&amp;D</td>
<td>Taxation Preparation</td>
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<tr>
<td>T&amp;D</td>
<td>Taxation Preparation</td>
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<tr>
<td>T&amp;D</td>
<td>Taxation Preparation</td>
<td>0.00%</td>
<td>0.00%</td>
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<td>0.00%</td>
<td>1.00%</td>
<td>0.00</td>
<td>0.00%</td>
<td>0.00%</td>
</tr>
<tr>
<td>T&amp;D</td>
<td>Taxation Preparation</td>
<td>0.00%</td>
<td>0.00%</td>
<td>0.00%</td>
<td>0.00%</td>
<td>0.00%</td>
<td>0.00</td>
<td>0.00%</td>
<td>0.00%</td>
</tr>
</tbody>
</table>

### Client Performance Trends

This report helps to determine the profitability trend for a particular client. Shown in the following report are amounts billable (recorded chargeable time) compared to amounts billed, write-offs and receipts for each month in the selected 24 month range.
You should be checking graphs and reports similar to these on a monthly basis at a minimum in order to spot problems quickly. It's also helpful to look at these figures on a quarterly and yearly basis. Doing so will help you ensure that longer time frames show data consistent with shorter time frames and identify seasonal trends for which you should plan.
The Auditor’s Dilemma – The Temptation to Compromise
Principles for Money

Auditing public and nonpublic companies present a myriad of challenges not commonly known to the public. Missing from nonpublic company audits are the oversight regulations of the SEC and the requirement for an audit committee. However, both public and nonpublic company audits test the auditor’s integrity and independence, since management controls the payment of fees.

Small and medium sized auditing firms performing nonpublic company audits usually deal directly with the client, the very same client that pays the engagement fee. This relationship on face value puts the auditor’s integrity in question. After all, self-interest dictates that we grow our firm and establish a profitable practice through serving and establishing long term relationships with our clients. What happens to our independence when the client takes us hostage through non-payment of fees?

That result can occur a number of ways. For instance, subsequent discovery of facts can lead to the issuance of an adverse opinion, or worse, withdrawal from the engagement. Fulfilling our obligation to the public may result in non-payment of fees, lawsuits and loss of the client. Of course, we are better off without this type of client, but is there a better way?

When I started my auditing career in the 1970’s one of my first employers was a national “Big 8” (now “Big 4”) auditing firm with offices based in South Florida. In case you hadn’t heard, South Florida was and is still often referred to as the fraud capital of the world.

One of my first engagements involved auditing a public company that operated a franchise business. During the audit, we discovered fraudulent sales invoices – a covert effort by the client to overstate sales and earnings, and thus, increase the stock price. The audit firm acted credibly by hiring outside legal counsel and bringing in additional talent from the New York office to limit negative exposure to the firm. In the end, the client became insolvent and the firm ended up with a large unpaid bill.
Many years later, I was faced with a similar experience as managing partner in a small local practice of fifteen professionals. The additional costs of hiring lawyers and another prominent CPA firm to “double check” my conclusions became prohibitive and overwhelming. The fact that the SEC was involved further complicated the situation. Conclusion – the resources that small and medium sized firms possess to properly deal with situations of this type are significantly limited when compared to a larger firm.

A substantial up front retainer might have mitigated this result, followed with frequent progress billing – but the extensive additional work would still have resulted in a substantial loss to the firm. It was years later that I realized a better solution.

Regardless of the controls we put in place, there is always a temptation to compromise principle for money. In our case, principles prevailed and the public interest was served at the expense of prosperity. Might this have been avoided if the entire audit fee, plus a contingency fund was escrowed with an independent third party before the work began?

Shouldn’t the honesty, integrity, independence and talent required of the auditor be worth protecting? It seems outrageous that auditing firms, through the competitive process, submit low bids for work that should cost as least as much as high quality tax work, and then wait for collection of these fees. How can this practice protect the auditor’s independence and be in the best interests of the public good?

There is no good reason why an auditor should be pressured with the additional possibly of non-collection. The exposure the auditor faces by failing to find fraud, or encountering fraud or other defalcations is enough without worrying about collection issues.

At the very least, small firms auditing non-public companies must establish in the engagement letter the requirement for progress billing. The billing system should provide a means to paragraph bill progress fees and expenses without sacrificing the ability to document detail time spent in the event of a budget dispute. This, in fact, is one reason our firm created our own billing system and much later, ImagineTime software.
The invoice system should be flexible enough to separate agreed upon fees that do not require supporting detail from additional costs that may result from extra work outside the scope of the normal engagement. This extra work should have the option to be displayed as an extra paragraph or detail time slips, whichever is more appropriate. The final bill should recapitulate the total engagement cost and subtract previous progress billings, services outside the engagement scope as well as show any unpaid outstanding balances – see the example that follows. In the event of a dispute, the total engagement cost should be supported by a comprehensive detailed work in progress report.
Another way to limit exposure is to vet your client by performing a detailed background check. Nevertheless, even the most credible client on the surface can obscure a can of worms. During the 1980’s as our local firm established its’ reputation in the community, we were most fortunate to be awarded the audit engagement of a very prominent local charity. My worst nightmare ensued by catching our audit client in an indefensible misuse of restricted funds. As fate
would have it, a director misused funds for personal gain. To make matters worse, the board member involved was a prominent attorney.

After being characterized as ‘auditors in white coats’, we were discharged from the engagement with a significant loss of our engagement fee. Had we insisted on more funds being paid at the inception of the engagement, our losses would have been limited. Ideally, small firms should have a mechanism in place to arbitrate any fee disputes as part of the engagement letter and some language that covers fees in the event of engagement termination.

In our case, the client situation was brought to head when the successor auditing firm consulted with us before beginning their engagement. However, we were never fully compensated for the additional time spent on the engagement. It is my hope that you can learn from our experiences.

Value yourself, insist on fair treatment and level the playing ground with a comprehensive engagement letter that covers fees and disputes. If possible, before field work begins make arrangements to have the fee escrowed with a third party.

Is the Cloud just a bunch of Blue Sky?

Most of the accounting world by now has heard the term “cloud” and read articles about firms moving to the cloud, but is the cloud right for you and your firm? The purpose of this article is to assist small to medium sized firms (50 users or less) in answering that question. Technical specifics of cloud computing are beyond the scope of this article.

Not all firms have the luxury of crack information technology staff. For many professionals, especially sole practitioners and firms just starting out on their own, your skill set may not include IT. The cloud can be an extremely good solution for the sole practitioner or smaller firms with less than five staff. By using the cloud, you gain immediate access to the tools you need without the investment in computers and infrastructure. Nor do you need consider the
aspect of equipment failure or defective backups, etc. You pay someone else to handle that for you.

On the other hand, is the cloud a good solution for established firms or firms with the necessary resources? Maybe – maybe not. The decision criteria are somewhat analogous to the benefits of renting versus home ownership. Over time, the monthly cloud fees may seem pricier as compared to the cost of desktop applications. Do you have the capacity in servers and personnel to properly manage your local area network? More importantly, do you have sufficient redundancy to protect against equipment failure? If the answer is yes, consider maintaining your own local area network as a lower cost solution in the long run.

To empower small firms, Microsoft recently released Windows Server 2012 with Hyper-V© replication technology. This new server operating system is more user friendly to small business and has an emphasis on secured, remote connectivity. Remote users can now access applications directly through a browser, or desktop icons instead of from the server desktop. Server 2012 also allows replication to an offsite replication server (at a partner’s home, for example) that is never more than five minutes behind and has the capability to take over in the event the primary server fails. The basic server installation for Windows Server Standard 2012 with replication technology installed for a typical small firm can run less than $5,000.

The decision to go to the cloud or to a local area network using desktop applications is a business decision that you need to make. Make a T account (remember Accounting I) and create a Pro and Con list and work through the scenarios. We can’t make the decision for you but we can answer your questions that can help you make that business decision. ImagineTime has products for both the desktop and the cloud. While there has been quite a bit of interest in our Cloud offering, we continue to actively support and promote our flagship desktop product as an economical, easy to install and maintain solution that can also be accessed remotely using MS Windows Server 2003 or better, or one of the commercial remote access tools such as LogMeIn or Mikonos.
A Final Word…

In the sixteen years that have passed since the initial beginning I have had the opportunity to assist and learn from literally thousands of CPA’s and accountants. Many of our clients made valuable suggestions that greatly improved our product. It is from that experience and the two accounting firms that I managed that I developed the information for this short book about best practices for small firms.

Naturally, I didn’t cover everything about best practices, but hopefully, this information has been helpful and will be useful to you on your journey.
Imagine having more time to spend on what is most important to you.