
Money Matters: Starting Your Own Firm

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When Stephanie L. Friese graduated from law school in 1999, she didn't join an established firm. Instead, she took the entrepreneurial route and hung out her own shingle.

With guidance, support and a few clients from her father, who's also an attorney, she launched a commercial real estate firm. For a year, she worked alone. "I remember being so lonely going to work," she says.

Friese says the firm started making money after about a year. Her father's clients helped, as did a line of credit. "Cash flow is the hardest thing, and the line of credit helps tremendously with that," she says.

Five years later, she says, Friese & Price Law Firm is successful. She now practices with her husband, Alon H. Price, and the firm has four attorneys -- one of whom works part-time -- a full-time office manager and three part-time support staffers. Also, the firm is certified as a woman-owned business, a status that has opened doors for attracting clients and other opportunities.

Though Friese's firm is financially successful, she knows firsthand about the money-related stresses a start-up can face. Most people who launch their own businesses have specific expertise, she points out, rather than the broad business background that promotes fiscal success.

In order to succeed, Friese says, "I had to seek out other people who had done this and not be afraid to open my books to them and ask them for advice."

Like Friese, many lawyers dream of launching their own firms, and wonder how they'll make ends meet -- much less make a profit. Any would-be legal entrepreneur faces a host of questions: How much money do you need to launch a firm? How do you keep business and personal expenses separate? How do you take advantage of tax deductions -- without triggering an audit? How will you ever retire, and what specific retirement vehicles do self-employed people have?

To get answers to these and other questions, the *Daily Report* asked Friese and two other attorneys who've started their own firms, as well as three financial planners, to share their secrets for small-business success.

KEEP CASH FLOWING

As Bryan A. Vroon, who along with partner John W. Crongeyer left Alston & Bird to start Vroon & Crongeyer in May 2004, puts it, "It's very challenging, but it can be very rewarding -- that sense of ownership and self-direction. Making your work more personal and putting more of your soul into what you do is important."

As important as soul is, it's cash that's crucial. "Start-up expenses for infrastructure are expensive and the outflow of cash is significant, and the inflow is minimal," says Vroon, whose litigation firm handles public health, medical and science issues.

He adds that lawyers should plan on a year of money struggles. "Starting your own firm is very exciting and having a cash crunch is the one thing that could take away from that excitement," he says.

For Friese, the line of credit was the answer. She advises others just starting out to "get as much as you can get because you don't have to draw on it all or pay interest on it if you don't need it -- it's just a great management tool."

Donald W. Patrick, managing director of Integrated Financial Group in Atlanta, says, "Having enough capital to get through the start-up phase is number one. That's why most businesses fail."

His rule of thumb: Cut projected revenues by 25 percent. Then increase projected expenses by 25 percent. "That's pretty much the way it happens," he explains, adding that before start-up, at least six months of working capital should be set aside. "If it's a scratch practice with no clientele, in an ideal world, you'd want to see more than that."

How do you know how much cash you'll need? Research, says financial adviser Michael Tankersley, of Investment Management Advisors Inc. at the Perimeter. "Talk to someone already in that business doing what you want to do," he advises. Estimate start-up costs -- such as office space rental, stationery and marketing -- billing rates and the number of billable hours you want to have, as well as how many -- if any -- employees you want.

"There's lot of uncertainty when starting your own business," Tankersley says. "So keeping expenses low in start-up should be considered. If you run out and rent the most expensive space and buy the most expensive furniture, you could be setting yourself up for cash-flow problems down the road if things don't work out."

Criminal defense lawyer Brenda J. Bernstein, who started The Bernstein Firm last year after being a solo practitioner for eight years, had a creative way to keep cash flowing.

"When I decided to go out on my own, I knew I needed some basis for business, so I contacted several criminal defense lawyers for advice and to see if they had office space to share with overflow work," she writes in an e-mail during a trip to New Zealand. "I then borrowed about \$10,000 for the basics -- computer, furniture, letterhead, online research materials -- and shared space with [an established attorney], who allowed me to work for my office space rental. That way, I was able to pay the bills."

A loan is another way to ensure you have cash for your business. "If you own a home, before you go down the road starting to look at various debt options, I highly recommend securing a home equity line of credit," says Don Whalen of Versailles Financial in Alpharetta, GA. "I don't like to see people use their equity in their home to finance something as risky as starting a business, but it's a good cushion to have if ever that's needed."

A business loan, however, may be more expensive, he says. "It's not a traditional mass-marketed instrument as is a home equity loan, but you'd be able to deduct that interest as business expense as well."

Interest rates are a factor in deciding which type of loan to go for, says Integrated Financial Group's Patrick. "If you can get a small business loan -- and that's an if with a new firm -- it's typically going to be a fixed rate. If you take a home equity [loan], it's a variable rate so you're subject to interest rates rising if they go up."

BEWARE THE IRS

Being self-employed raises a red flag with the Internal Revenue Service, says Patrick. "You're at a high risk for auditing, so you want to make things as clean as possible," he adds. There are specific rules with the IRS code regarding personal and professional usage of, for example, cell phones, computers and cars. "You literally have to track it manually."

Log the time spent on business calls as well as car mileage, Patrick advises: You can either jot down mileage to and from work appointments (not including commuting to and from the office) or use a Dictaphone to record mileage and hand the tape to your accountant at tax time.

It's critical to keep separate personal and professional bank accounts and credit cards, however, he says. "The IRS does not like commingling of those things, and it's not the cleanest way to run any business."

He and other financial advisers recommend QuickBooks or Microsoft Money to keep track of business expenses.

Investment Management's Tankersley also recommends forming a limited liability corporation or incorporating. "That will protect your personal assets from corporate liability, and most attorneys would prefer to have that protection," he says.

An LLC keeps attorneys from having to pay quarterly taxes, Patrick adds. "You'll probably be paying yourself a salary, so you'll have to do withholding in a traditional sense -- for Social Security and workers comp -- because you are technically an employee of the corporation and an officer. With this type of setup, there will typically be distributions paid out at year-end."

RETIRE IN STYLE

If you are focused so much on the day-to-day operation of a start-up law firm, how do you put money away for retirement?

The *Daily Report* created a hypothetical attorney and asked the financial planners to offer retirement advice.

The hypothetical attorney is 40 years old and started her firm last year with clients she'd brought with her after leaving an established firm. She grossed \$300,000 in her first year, and after paying support staff and other overhead, she paid herself a \$100,000 salary.

She and her 44-year-old attorney husband, who makes \$80,000 annually at a small firm, and their three children -- ages 10, 6 and 3 -- have a \$150,000 mortgage on a \$250,000 house. They have \$150,000 in 401(k)s and other retirement plans, as well as \$30,000 in money markets, stocks and bank accounts. There is \$15,000 put away for the children's college, and

law school and car debt comes to \$50,000.

Are they on track to a secure retirement? No, says Versailles Financial's Whalen. "They have to start contributing a lot more," he says, adding that her husband should be putting the maximum in his employer's 401(k) plan annually: \$13,000. "If they only have \$150,000 in their retirement fund, I have to think he's not been doing that religiously."

Whalen says the couple should have something closer to \$757,000 in their 401(k) accounts, assuming both have contributed the maximum for the past 15 years (about \$11,000 a year each on average), with an average rate of return for the period of 11 percent. That still wouldn't be enough, he says, but would put them "a lot closer" to what they need for a comfortable retirement.

Whalen is a proponent of the SEP IRA as a retirement vehicle, to which self-employed people may contribute up to \$41,000 per year. "It's easy to set up, and you've got the maximum possibilities for investments. It's hugely flexible, and most custodians won't charge you to keep that open, so there are no fees," he says.

If this hypothetical attorney wants to contribute to her employees' retirement -- which helps ensure retention -- Tankersley suggests a 401(k) profit-sharing plan. The plan allows the attorney to defer her salary for the 401(k) portion and then top it off with a profit-sharing contribution. "She's limited by her salary how much she can contribute, but if her salary is going to move up, then 401(k) profit sharing would allow her to increase her contributions," he says.

For 2004, the 401(k) deferral limit for a \$100,000 salary is \$13,000, according to Tankersley. Profit sharing allows the attorney to defer up to the maximum of 25 percent of her salary, which would be \$25,000. The \$13,000 from the 401(k) counts against that \$25,000, so she can contribute the difference -- \$12,000 -- to a profit-sharing plan, which means she would have to defer 12 percent of all employees' salaries. "If her employees want to defer any of their salary, they could, too, and that could be a benefit that employees would desire," he says.

With so many factors to consider when starting a firm, the financial planners and some attorneys who've launched their own businesses recommend meeting with experts.

But could that be a deterrent? "Looking back, sometimes I think I benefited by not knowing everything that could go right or wrong," Bernstein says. "That allowed me to just jump headfirst."

But for Vroon, the key was understanding how all-encompassing the project is. "If there was a way our bodies could reserve sleep, I would have done it," he says. "I've worked harder in the last six months than I ever have before. But I would still do it again."