

Financial Due Diligence Checklist

A comprehensive financial review framework for law firms — covering trust compliance, billing, payroll, taxes, and internal controls.

01 General Financial Records

Chart of Accounts

Verify it follows legal industry standards (IOLTA separate, trust vs. operating)

General Ledger

Review for completeness, accuracy, and proper categorization of all transactions

Bank Statements

Collect last 12–24 months for all operating and trust accounts

Credit Card Statements

Review all firm-related card statements for unauthorized or personal charges

Petty Cash Records

Confirm petty cash log matches receipts and balances

Check Register

Review check issuances for dual authorization compliance

02 Trust & IOLTA Account Compliance

IOLTA Account Ledgers

Ensure individual client ledgers are maintained for every trust matter

Three-Way Reconciliation

Confirm bank balance = book balance = sum of client ledgers monthly

Client Trust Balances

Verify no client account shows a negative balance at any point

Trust Disbursement Records

All disbursements must be authorized and properly documented

Commingling Review

Check for any mixing of firm operating funds with client trust funds

State Bar Compliance

Confirm records meet jurisdiction-specific bar association requirements

03 Accounts Receivable & Billing

Outstanding Invoices

Review aging report — flag anything 90+ days overdue

Billing Rate Schedule

Confirm current rates are applied consistently across all client matters

Write-Offs & Adjustments

Review all billing adjustments for authorization and documentation

Retainer Balances

Verify all retainer deposits are recorded and applied correctly

Collection Procedures

Confirm a documented process exists for following up on overdue balances

Unbilled Time & Expenses

Review WIP (work-in-progress) for billable items not yet invoiced

04 Accounts Payable & Expenses

Vendor Invoices

Confirm all payables are recorded and supported by invoices

Expense Categorization

Review that expenses are properly categorized (client costs vs. firm overhead)

Outstanding Liabilities

List all unpaid vendor balances and upcoming obligations

Recurring Subscriptions

Audit software, memberships, and services for active use and necessity

Employee Reimbursements

Confirm reimbursements are documented and approved before payment

Client Cost Advances

Verify all advances paid on behalf of clients are tracked and billed back

05 Payroll & Compensation

Payroll Records

Review payroll registers for the past 12–24 months

Payroll Tax Filings

Confirm 941, 940, state payroll tax filings are current and reconciled

W-2 & 1099 Issuance

Verify all employees and contractors received correct year-end forms

Contractor Classification

Confirm 1099 workers are properly classified vs. employees (IRS rules)

Benefits & Deductions

Audit health insurance, retirement, and other deduction accuracy

Overtime Compliance

Check overtime hours and pay rates comply with federal and state law

06 Tax & Regulatory Compliance

Federal & State Tax Returns

Collect last 3 years of filed returns (1120S, 1065, Schedule C, etc.)

Estimated Tax Payments

Verify quarterly payments are made on time and amounts are accurate

Sales Tax Obligations

Confirm applicability and compliance in all operating jurisdictions

IRS Correspondence

Review any notices, audits, or open issues with the IRS or state agencies

Business Licenses

Confirm all required licenses and registrations are current

Prior-Year Adjustments

Note any audit findings or amended returns from prior periods

07 Financial Statements & Reporting

Profit & Loss Statement

Review monthly and YTD P&L; for revenue trends and expense anomalies

Balance Sheet

Confirm assets, liabilities, and equity balances are accurate and current

Cash Flow Statement

- Analyze operating, investing, and financing cash flows

Budget vs. Actuals

- Compare current performance against annual budget (if one exists)

KPI Dashboard

- Confirm firm tracks billable hours, realization rate, collection rate, and overhead ratio

CPA / Accountant Review

- Confirm whether financials are reviewed or audited by an external CPA

08 Internal Controls & Bookkeeping Processes

Segregation of Duties

- No single employee should handle all steps of a financial transaction

Approval Workflows

- Confirm authorization thresholds exist for payments and expenses

Bookkeeping Software

- Identify platform (QuickBooks, Xero, Clio, etc.) and access controls

Monthly Close Process

- Verify books are closed and reconciled by a set deadline each month

Document Retention Policy

- Confirm financial records are stored securely per IRS/state guidelines (7 years)

Backup & Data Security

- Verify financial data is backed up and protected from unauthorized access

How to Use This Checklist

Work through each section with your bookkeeper or financial advisor. Check off items as they are reviewed and verified. Flag any discrepancies or missing records for immediate follow-up. This checklist is designed for annual reviews, firm acquisitions, partnership changes, or onboarding a new bookkeeper.

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