



Senior Partner Compensation as a Management Tool

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Design a process that will help you assess whether your current system encourages or discourages desired behaviours.

By Arthur G. Greene

Partner compensation challenges law firms with the difficult issue of determining how profits are to be shared among partners. The goal is to make sure that the process of rewarding each partner's contribution is carried out in a manner that is considered open, fair and credible.

The primary goal of a partner compensation system is to fairly allocate the profits of the firm among the partners. Who would not agree? The goal seems simple enough, but measuring the contribution of each partner can become hopeless if there is no consensus among the partners as to the relative importance of different types of contribution. And beyond the issue of intrinsic fairness, there looms the issue of perceived fairness. Openness, fairness and a credible process are the best methods of overcoming what can be a difficult process.



Rewarding desired behaviours

In recent years, lawyers charged with governing their firms have begun to realize that partner compensation systems can be a powerful management tool. From that perspective, the compensation system should reward the behaviours the firm wants to encourage and penalize the behaviours the firm needs to discourage. Using the compensation system as a management tool can not only lead to greater firm-wide success, but it can also promote a more open and more credible process.

Think about the factors that are important to the success of your law firm. Do they include:

- Originating new clients?
- Work profitability?
(as opposed to dollars in the door)
- Delegating work to others?
- Leveraging associates and paralegals?
- Training and mentoring associates?
- Managing the firm?
- Proving leadership?

The importance of evaluating the use of law firm resources

Law firms in which financial reports tend to drive behaviours have an additional problem. If a partner writes off an associate's time, it negatively affects the associate's numbers and does not affect the partner's numbers.

While an argument can be made that perhaps the write-off reflects the deficient nature of the associate's work, the better approach is to hold the partner responsible for not having managed the associate effectively.

Further, the write-off could be because the client does not pay, which is an intake issue, not an associate issue. Firms need to evaluate the partner's use of firm resources, which can only be accomplished if the financial reports sort by the responsible lawyer, in which the partner is accountable for the effective use of all resources, including associates and paralegals.

Create a list of what your firm needs to become more successful and ask yourself whether your current system encourages the desired behaviours. If the answer is no, then the partner compensation system needs to be re-evaluated.

Compensation systems can be formula based, subjective, or some combination. If the system is formula based, then the formula needs to address, or reward, the desired behaviours. If the system is subjective, the factors to be applied must articulate the desired behaviours. The scope of this article does not cover an examination of the advantages and disadvantages of the different partner compensation systems, but it is important to note that surveys report that firms that have endured from the first to second generation tend to have evolved to subjective systems.

The significance of financial reports

The practical application of any partner compensation system is tied to the data that is published in the firm's financial reports. Partners pay attention to what is reported and cannot help making decisions in their practices based on what looks good in the reports.

For many firms, the financial reports tend to drive behaviours that are inconsistent with the goals of the firm: Typically, in small firms, the financial reports reflect the billable hours worked and the dollars received from those hours, sorted by individual, whether partner, associate or paralegal. Firms that report this way do not encourage delegation and leverage, an important concept for growing successful law firms. In fact, this type of record-keeping encourages partners to hoard work for themselves, so the numbers in their column will look better.

The financial reports available for review in connection with partner compensation should be sorted by the responsible lawyer and include, at a minimum, billings, billing realization, cash received, collection realization, aged work-in-process, and aged receivables. The larger point, however, goes back to the initial premise: to determine the desired behaviours that you want to reward in the compensation system and then be sure your financial reports are consistent with reporting on those behaviours.

Lawyer annual plans

Lawyer annual plans are an important management tool to use in connection with the firm's partner compensation system. Annual plans provide firm management with a way to work with each partner (and associate) in order to coordinate individual efforts in the context of firm goals. For example, the individual annual plans would include intended efforts to:

- Enhance their skills
- Expand their practice
- Improve their productivity
- Assist others in improving their practice
- Advance the goals of the firm
- Participate in civic and professional matters

The annual plan would also set out expectations as to their billable hours, the revenue produced from files they manage, the realization rate for the files they manage, and the dollar value of originations. The first draft of the annual plan is normally prepared by the individual lawyer and then is finalized in a session with the managing partner, whose role is to focus on insuring everyone's plan covers what is needed from the firm standpoint.

Let's go back to the original goal. As a management tool, the partner compensation system needs to reward desired behaviours. The annual plan is an excellent means of communicating what is required from the firm's perspective and the role each lawyer needs to play in order to achieve the firm goals. Integrate the annual plans with the compensation system and the whole process becomes open, fair and credible.

Conclusion

Treating the partner compensation system as a management tool is not inconsistent with the goal of fairly compensating each individual for their contribution to the success of the firm. In fact, it enhances that goal by making the whole process more understandable and more predictable.

The required ingredients include (i) identifying the goals of the firm, (ii) understanding the partner behaviours required to achieve the goals, (iii) developing financial reports that reflect data relevant to those goals (iv) creating a partner compensation system that rewards those goals, and (v) developing individual lawyer annual plans that articulate specific individual contributions.

Using the partner compensation system as a management tool does not make the issue of partner compensation more complicated and difficult. On the contrary, if properly structured and implemented, it will improve the partner compensation process, reduce tensions and benefit the firm's success.

Arthur G. Greene is a principal of Boyer Greene, LLC, a law firm consulting organization with locations in Michigan, New Hampshire and Nevada. Following a successful career as a practicing lawyer, during which he served as managing partner of firm that grew to 70 lawyers, he turned his professional focus to management consulting with law firms. In recent years, his consulting practice has included profitability studies, revenue enhancement, firm audits, strategic planning, governance, succession planning, compensation plans, alternative billing methods, and other aspects of maintaining a healthy firm. Arthur Greene is a Fellow of the College of Law Practice Management.

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