Grumpy Partners and the Case for 'Multi-Pool' Comp Systems

HUGH A. SIMONS

Nearly 60% of equity partners want to see changes in their law firm's comp system, according to the 2018 Major, Lindsey & Africa (MLA) Partner Compensation Survey. This isn't normal. I've seen comparable numbers for physicians and consultants—for these, typically about 30% want their systems changed.

This desire for change among law firm partners is not driven by any one segment of partners, although there is some variation around the average by group. For example, the desire for change is stronger among:

- ***Women than among men:*** *65% v. 55%. This difference reflects varying perspectives on the existence of gender bias in comp.*
- ***Younger than among older partners:*** *62% for those in years 5 to 10 as a partner v. 54% for those who have been partner for more than 20 years. It's notable that, while the 20+ year cohort is the least inclined toward change, even among this conservative group, more than half want to see change.*
- ***Partners at closed system firms (i.e. firms where partners do not see what each other earn) than among partners at open system firms:*** *65% v. 56%. The difference here is especially pronounced among younger partners at closed system firms who evidence a strong desire for their firms to change to open systems.*
- ***Homegrown than among lateral partners:*** *61% v. 65%. This reflects the belief among homegrown partners that they are under-valued relative to their colleagues hired in laterally.*

SUSPICIONS OF CRONYISM

With profits at all-time highs, you'd expect lawyers to be happy with all aspects of comp. Why are they so grumpy? In brief: cronyism, or at least a suspicion of cronyism. When MLA asked about biases their firms exercise in determining compensation, 36% of equity partners identified "cronyism" as such a bias, essentially the same as the number (37%) who said their firm exercised no particular bias.

Cronyism swamps the other forms of bias that partners identified by a factor of 3 or more: bias against homegrown partners, 13%; gender bias, 12%; bias against laterals, 7%; racial bias, 4%.

Cronyism is a not a great word. My sense is that true cronyism is rare; less rare is managerial discretion that, from a distance, may look like cronyism. Managerial discretion is entirely appropriate—leaders have awareness of contributions to the firm, and exogenous factors, that bear on comp decisions but that those partners focused intently on serving clients simply don't have. This doesn't mean concern about cronyism can be ignored—feelings, too, are facts and have to be dealt with.

SUGGESTIONS FOR PROFIT POOL ALLOCATIONS

The challenge for leaders is this: How to maintain discretion while alleviating the emotionality around possible cronyism. To address this, leaders should, first, circumscribe explicitly the funds over which they exercise discretion and, second, articulate both what discretion is being used to reward and how it does so. What might this look like?

Today, most law firms think of their entire annual profit as a single pool to be divvied up and allocated to individual partners. Other professional services firms do this differently. They split the firm's annual profit into separate pools each of which is then allocated to partners on a different basis.

For example, the pools could be:

- ***Pool I, Long-term ownership:*** *15% to 30% of annual profit could be taken as owed to partners in their capacity as owners. Thus, the allocations to individual partners from this pool could follow a lockstep system or be* *in proportion, say, to cumulative years as a partner at the firm.*

- ***Pool II, In-year financial contribution:*** *50% to 60% of annual profit could be allocated to partners in proportion to, say, originations, or other measure of economic contribution to the firm that year. To avoid wild year-to-year swings, the percentage allocations could be smoothed using, for example, three-year averages.*
- ***Pool III, In-year institutional contributions:*** *20% to 40% of annual profit could be allocated to partners on the basis of how they contributed to the firm over the year in all the ways not captured in Pool II. These could include: helping fellow partners; bringing others into one's client relationships; leading business development efforts; and, attracting new marquee-value clients and matters. One could get more explicit on how awards are made from this pool—for example, having a rating system for partners wherein each rating corresponds to a particular dollar amount (within a cohort of partners) and a forced distribution of ratings to ensure the highest ratings don't all go to, say, more senior partners.*

ADVANTAGES FOR YOUNGER PARTNERS

A "multi-pool" approach like this has many advantages. First, on the issue of discretion versus cronyism, it appeases possible concerns by limiting the funds to which discretion is applied and by having an explicit articulation of what it rewards, and how, in the description shared with partners of Pool III.

A compelling aspect of a multi-pool approach to younger partners is that it enables a successful junior partner to earn more than more senior partners, i.e., a young partner with strong financial contributions and the ability to include others in her client relationships will out-earn a senior partner who services solo a moderately-sized client. The potential for such comp levels, even if rarely realized, binds younger partners to a firm thereby promoting its long-term health and dynamism.

More generally, the multi-pool approach moves comp systems in the direction they need to go. There was a time when firms could believe that if they delivered great value for clients they would prosper. Lateral movement of partners changed this. Firms must now place equal store in delivering great value for clients as in delivering compelling comp for partners. This latter requires that firms evolve their comp systems to being explicit and precise in how they reward partner contributions.

Multi-pool approaches give firm leaders the opportunity to transition from talking about what they endeavor to reward in their comp system to direct demonstration (in the form of the relative sizes of the pools) of what the system truly rewards. In the push-and-pull of retaining and attracting talent, being able to demonstrate explicitly what one's firm rewards will start out as an advantage and, over time, become table stakes. ■

Hugh A. Simons is formerly a senior partner and executive committee member at the Boston Consulting Group and chief operating officer and policy committee member at Ropes & Gray. Early-retired, he now writes about the business of law as a hobby and does some consulting for old friends. A fuller paper on this topic, The Wise and The Innocent Ways Partners View Their Firms' Compensation Systems*, is available on MLAGlobal.com or upon request from hasimons@gmail.com.*