The Partnership Track: A Blind Race

This is the last in our series of four articles on the importance of partner compensation schemes and delivering improved "value" in legal services to clients. Previously we had Jeff Carr's perspective on the benefits of a more corporate oriented compensation model, Patrick Lamb's perspective on improved collaboration through "banding" of compensation levels, and Patrick McKenna's perspective on motivating "right" behaviors though identifying, measuring and rewarding them.

At the beginning of one's career, one sets upon a course of being a "good soldier," doing what the system asks of you in the profession's self-described "tournament" style search for excellence. You must perform better than others so that you may advance within the organization. A large measure of blind faith is involved in doing this (which is amazing considering the cynical nature of most lawyers) because the standards of what it takes to be successful as defined by each firm are not usually communicated clearly or applied evenly - perhaps because they may be neither particularly well-defined nor politically correct in the first place. For the participants, the perception, and all too often the reality, is not so much that they are participating in a rigorously monitored and graded competition, but running a race in a fog with no lanes, no finish lines, no judges and no spectators.

LAST IN A FOUR PART SERIES

Co-authored by a Fortune 500 General Counsel, a Managing Partner, a Consultant, and a leading practitioner in alternative fee arrangements.

Given industry average attrition rates for associates of about 20 percent per year and eight to 10 year track to partnership, the probability of attaining partnership is poor for those enlisting in the competition. This system renders the cost of advancing the few who survive the ordeal prohibitive. How does a system work at all, let alone efficiently, by hiring the best and brightest talent available from the most prestigious law schools, paying premier salary and benefits packages, and then going through them like tissues in flu season? The cost to the organization is multiples greater than the returns possible from the few that succeed. This cannot be the real purpose - so what is the real story? Maybe the system isn't about a reward for being the "best of the best" after all. Maybe its portrayal as a tournament, should be revised as a game that has few winners, and which clients subsidize with unnecessarily high fees and costs. A game that drives many of the best and brightest out of the profession by consuming them on a treadmill of relatively meaningless work, and severely limited prospects of advancement. The soylent green wafers the system consumes for nutrition aren't made from plankton after all.

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Few partners are made relative to the numbers hired from law school, and fewer still are home grown. In many firms the number of lateral partners admitted over the past 10 years significantly exceeds the "home grown" partners. Furthermore, those who make partner still tend to be net "givers" to the profit pool for many years after they make partner. A net "giver" is a person who contributes more in personal service and client book dollars to the firm than they are paid, after costs. In most law firms, that is a significant majority of the equity partners, all of the income partners and of counsel, and most of the associates that actually do generate a profit. And it is a component of why life for many partners, especially those in the lower two thirds of the partnership ranks, and all associates, has become increasingly pressured and perceived as out of balance with a life style that is worth living. Leaderships demand of them ever increasing billable hours quotas and higher billing rates to be pushed upon their clients. Political fear and oppression of contrary views of how firms should be run or their client relationships serviced becomes commonplace. "Get with the program or get out" is the message. There is not much ambiguity there. Nor are there many alternative choices to move to other firms in which the mantra is any different.

A not uncommon phenomenon is the partner who trains and works his protégés up to the level of finally becoming a potential success as a stand-alone partner - and therefore, a competitor for the mentor. So, in this Hobbesian world, the protégé is counseled out before they have a meaningful relationship directly with any client of the partner, during a career in which they have been actively discouraged from developing their own independent client base. Senior partner "mentors" become sovereigns who "eat their young." Why do they do it? Because more equity partners potentially take away from the profit pie, creating competition in the area that the senior partner is most expert. Better to toss the juniors out and bring up another youngster until they reach the same level, repeating the cycle over and over.

This process repeats itself because it generates more money for the senior partners, and consumes and eliminates potential competition. Hundreds of thousands of dollars of sunk costs for recruitment, training and mentoring is lost with every associate and junior partner so terminated. (A firm with 300 associates that loses sixty of them in any given year, loses $15 to $18 million dollars of otherwise net distributable income, perhaps as much as 10 percent of the amount of total net income to the firm. That translates to roughly $80,000 to $120,000 per year per partner). Those are dollars that come from clients, and internally from the lower tiers of partners from income allocations. No other profession consumes its own people with such a voracious and wasteful appetite. A firm that refocuses its approach upon delivering value, through hiring a select number of people, and making every effort it can to invest in and retain as many of those people as it can, both in terms of skill development, and compensation sharing that supports collaboration and fair value to all of the members of the team, and to the stability of the business enterprise, will have an enormous competitive cost advantage over the present leveraged model that prevails. This advantage will not only be through the reduced turnover cost highlighted above, but in reduced operations expenses for rent, computers, lower recruiting costs and smaller classes of more selective hires.

Mention has been made recently of the jettisoning of the lockstep compensation model for associates as a positive move to bring "reality" to the cost structure of firms. This ignores the fact that merit based compensation and promotion was the model before lockstep was adopted by big law firms. The problem was that partners did not put the time and effort into merit evaluation to make it meaningful, and exercise of power by partners did more to assure that "favorites" were promoted over more capable and deserving candidates. Returning to a system that firms couldn't make work before is not necessarily cause for rejoicing, nor any assurance that it will in fact reduce costs to clients. The bigger problem with the model is the cost of the rollover of so many attorneys at such great cost.

What about the model of the big law firm? There is nothing inherently superior about the model of the big firm, though it could be inherently more profitable if it leveraged experience and prior work product instead of hours. As the current recession has shown, the big firm model is not more profitable: the global firms have had a harder time maintaining profitability. While the big firm model could be inherently more stable if it focused on talent development and succession planning, it does not; multiple failures of NLJ 250 firms over the past year belie this suspicion. While it could foster inherently better quality work or "seamless" delivery of legal service through robust quality control and processes; it has not as virtually any client will attest. Bigger is just that...bigger - not better. Its advantage to clients may be incidental, as contrasted to its real benefit of size, and leverage to some of the partners, which delivers more profit in good times. In bad times it is reflected by the termination of those least responsible for the compression on profits, the associates, junior partners, and staff personnel. None of which would seem to be addressed to providing better quality work at lower prices for clients.

Do we need big law firms? Absolutely, and there will be a large and robust practice arena for them into the forseeable future. Do we need "those types" of law firms, of any size, that derive substantial amounts of their distributable partner income from inefficiently consuming their own human resources? It is hard to believe that it is necessary or desirable. The new model has to change its compensation structure to incent behaviors significantly lacking in most large firms today.

That compensation model should focus on the long term strengthening of the institution of the firm over the short-term remuneration to the partners. Reduce use of short term debt for working capital as by at least 50 percent compared to recent years, increase partner capital requirements to 100 percent of annual compensation, maintain larger balances of cash for operating reserves (60 days would be a good start), restrict payouts of departing or retiring partner capital to an intermediate term of five to seven years, such that there is a major incentive to be a part of a firm that has strong prospects of long term survival, require limits to compensation and service terms of leaders and managers, include attorneys from the first year of associate status in profit sharing at a minimum scheduled level of 20 percent of compensation based on budget, and hold practice group leaders and other senior managing partners financially accountable for failure to meet budgets by having the first 20 percent of their income applied to results below initial budget before their partners bear the outcome. With authority should come accountability. With results should come benefits, and burdens. The rest will work itself out.

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