

Putting Business Into Practice

Partner compensation: all for one or one for all?



The problems associated with partner compensation

In the first of a number of briefings aimed at law firms we consider some of the challenges facing today's legal practice. In this issue we tackle the difficult subject of partners' profit sharing arrangements.

As law firms seek to improve their profitability, individual partner compensation is increasingly becoming a bone of contention amongst partners.

Tackling partner reward and performance management is no mean task. The traditional lockstep system as a stand alone criterion is in many cases no longer an adequate method for rewarding partners. How do firms move on to a more progressive system of individual recognition without creating an environment of damaging internal rivalry?

There has to be a "middle ground". Consideration needs to be given on how to incentivise partners yet ensure that the firm is still operating as a cohesive unit.

The key questions must be asked; how do we attract high calibre people? How do we retain the most successful people? If a traditional lockstep system is sufficient then maybe there is little to be done but in most circumstances this will not be the case.

Implementing a new structure requires a great deal of thought and consultation. There isn't a generic structure that fits all firms and to add further complexity there may be a need to overhaul the structure as the business climate changes or as the needs of the practice alter.

Is lockstep still valid?

It is not difficult to see the attraction of a traditional lockstep profit-sharing arrangement for professional partnerships. The earnings of the lawyers within the firm cease to be a political issue.

Individual partners are not labelled with how well they have performed or by how they compare to their peers. Rivalry tends to shift from within the firm and is focussed on the competition.

However, the environment in which lawyers operate is changing with unprecedented speed, putting tremendous pressure on traditional partnership arrangements. For those firms who wish to adapt, the challenge is how to supplement the lockstep with a structure that works for the benefit of the individual partners or prospective partners and the business as a whole.

The most common approach used is to retain the lockstep to a degree but to add a system that rewards individuals when recognition is due. Typically, this will be handled and implemented by a remuneration committee. With this approach it is essential that the partners trust those who will be making the award and are fully informed as to the reasoning behind it.

Objectives and rewards

To facilitate a successful transition to a new partner reward system it is important that you align your compensation scheme with the firm's objectives.

Does your firm encourage cross selling or is it silo driven? Is profit everything? These amongst others are considerations that must be addressed when deciding on a suitable points system.

Performance models and incentives

When considering the various criteria, the firm's objectives will need to be reflected in the weighting of points. It is likely that a system will be needed to reflect both tangible financial performance as well as intangible performance in areas such as business development, cross selling and new initiatives. The financial performance issues should be linked to the provision of up to date accurate financial information in order for partners to monitor their progress.

Such issues will no doubt include:

- I. achieving targets
- II. winning business
- III. profitability
- IV. lockup management
- V. recovery
- VI. and such other issues which are relevant to the firm's objectives.



Building compensation into the appraisal system

Using the appraisal process to measure a partner's financial and non financial contribution to the practice is now being considered and in some cases adopted by law firms. This move is a step away from the traditional structure but should only be used if the review system can be managed effectively.

With this in mind, the appraisal must be a two way process if it is to be credible as a basis to measure performance for partner compensation. It should review the previous year, set challenges for the forthcoming year and identify the resources needed for the partner to achieve his/her objectives. Reviews should have some form of scorecard method and feedback should be gained from clients, managers and colleagues to allow for a balanced assessment.

Capitalisation policy

Law firms need to also consider the impact that changes in the compensation structure will have in relation to the amount of capital invested in the business. Clearly, if the result of changes in the compensation awarded to partners means one partner earning significantly more than another then consideration must be given to differential capital investment. This is something that will need to be addressed on an individual basis.



How we can help

We would be delighted to discuss these issues with you and assist with the development of your business.

For further information about **Cowgill Holloway's Professional Practices Unit** and how we may be able to assist you, visit www.cowgills.co.uk or contact Paul Stansfield on **01204 414262**.

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