

LAW PARTNER COMPENSATION ALTERNATIVES

I have a small law firm with three partners (members of a PLLC actually) and four non-attorney staff. For the past couple of years we all billed roughly the same amounts and have simply divided the net income each month. So far this year one partner has been consistently billing more and one partner consistently billing less. An additional complication is that two partners handle litigation which frequently results in widely fluctuating monthly billings.

We are discussing alternative compensation arrangements, everything from a straight "eat what you kill and share expenses" arrangement to some sort of bonus or formula compensation.

I spent most of the 1990s watching very large national law firms fall apart around me over compensation issues. One of the reasons that I spent the next 10 years as a solo is that I do not like to deal with those issues. On the other hand, I really like my partners and enjoy practicing in a small firm.

Without getting too specific (since this is a public forum) what sort of arrangements have or have not worked for you? If you are willing to talk specifics, then e-mail me off list at neal@klblawfirm.com.

Thanks.

I am very interested in this as well, since a few of us are thinking of joining forces in the near future, and our billings differ by quite a bit,

and may also change over the next few years. So I would appreciate having the discussion on the list serve, or being included in any private responses.

Another related topic is how to split things when one partner brings in a lot of clients, and the others do the resulting work. I think it is customary for the "rainmaker" to get a small percentage of billings resulting from his/her referrals (in an "eat what you kill" arrangement), how do others split the pie?

Cynthia Hannah-White, Hawaii

My firm, and others like it, operate on a modified eat what you kill. Shared expenses come off the top; if you work your own files, you take home the rest of what comes in. If you work someone else's files, or they work yours, the revenue is split. I've seen splits of 60% worker 40% originator all the way up to 75% for the working attorney.

Kevin W. Grierson, Virginia

You can try Jay Foonberg's book, "How to get and keep good clients", the section entitled "Getting business from others in the office", subsection F-6 "Fee allocation formulas to encourage marketing" (kindle edition here). Here there's a discussion about different fee allocation formulas you may find helpful.

I highly recommend the book, it's nice to have around.

Andrew Kornoff, California

I have gone through a lot of variations on this over the years. My firm, which has been around for about 18 years, has been 2 partners, 3 partners, and 4 partners at various times.

Among the issues that need to be addressed are:

1. Will each partner be entitled to a minimum draw just for being there?
2. Will percentages be adjusted each year, or more or less frequently?
3. How much does the firm value origination v. production? My personal view on this is that, in a small firm, origination is king. Anyone can (should be able to) do the work. Not everyone can bring the work in the door. And, from a purely mercenary point of view, the partner with the book of business can easily go elsewhere if he/she wants; the partner who does the work cannot. But I recognize that strong arguments can be made for the importance of production, and the sense that clients should be considered "firm" clients after a certain period of time (our firm doesn't work that way)

Initially, we set %s and then forgot about it. After a number of years of not looking at percentages, we found that our percentages no longer reflected what each of us was doing, which led to several years of experimentation.

We started out with a modified eat-what-you-kill. Each partner had a monthly nut, which was an equal share of the firm's overhead. Each month a partner earned one % of the collections where he originated and produced; a different % where he just originated, and a different % where he just produced. The monthly nut was deducted from that. So compensation could vary widely. We kept a fairly complicated spreadsheet that did the calculations. PITA.

We didn't like that, so after a year we moved to a practice of setting %s at the beginning of each year. We look at origination and production (but lately each partner is doing most of his own work, so the distinction is not terribly significant). We also look at any other metrics any partner considers significant. Typically there's no problem reaching a consensus over about 95-97% of the pie. It's the last few points

that often lead to debate and discord. Generally those last few points end up being very subjective, and can include many factors, including historical value to the firm. But we've always ended up at a consensus, even if it might be somewhat grudging at times.

It has been suggested to me by some business folks that it's dumb to set this year's percentages based on last year's results. That suggests a mechanism that I think a lot of bigger firms use: each partner gets a monthly draw. At the end of the year, or each quarter, profits are divided based on some formula, usually looking at what each partner contributed for the year in question. What I don't like about that is you really don't know your % until the end of the year. And I think "discussions" over a pot of existing money are bound to be more heated than discussions over money that has yet to be earned. OTOH, I recognize that there's more certainty discussing what people actually did, instead of assuming that next year will be like last year. As another negative, , I find that, when the firm keeps a lot of money on hand, theoretically to distribute at the end of each quarter, the firm finds things to spend it on and it never gets distributed.

I have found that discussing percentages at the beginning of each year is the most distasteful part of practice. Each of my partners hates it too. But ignoring the issue almost led to the firm breaking up when people weren't being compensated fairly. So we recognize it as a necessary evil. I wouldn't want to do it more than once a year, though.

Patrick W. Begos, Connecticut

I don't have any advice for how to compensate or share revenue with members of your firm, but I've been in several office-sharing arrangements with other solos and I don't think I'll ever join a firm or use a different approach.

It is of course "eat what you kill" and we share some common expenses, like rent, phone service, internet, etc. Benefits include: you don't have to be responsible for anyone else's compensation, you don't have to depend on anyone else for managing their bookkeeping or finances, you get to keep 100% of what you earn (minus your own share of the overhead), and you still get the collegiality of being around other lawyers on a day-to-day basis.

How to share staff can always be a contentious issue, and I don't think there are any easy answers to that, whether you're in a firm or not.

In my office, we have two solo lawyers, and I have a part-time staff member that only works for me. Sometimes my assistant adds a few hours and works for the other attorney. The other attorney and I have complementary practice areas (similar clients and similar approaches), and have been known to co-counsel on a few cases. I think this arrangement works swimmingly and wouldn't trade it for anything. Before I was in this office, I was in an office of three solos, and we had a similar arrangement. It works really well, and we have always stayed out of each other's' hair.

Monica Elkinton, Alaska

A few random observations:

1. Why would you need to adjust a formula every year (or more often)? Why not apply the same formula to everybody, every year? e.g., after overhead is taken out, you get 100% of what you eat and kill yourself, 30% (or whatever) of what you bring in for others, and 70% of what you do for others. That way, rainmakers can make money off of the work they bring in, whether they do it or give it to someone else.
2. For the originator/worker split, you want to give the originator an incentive to farm the work out, and the worker enough of an incentive that they want to do work brought in by somebody else. If the numbers skew too much one way or the other, and nobody is sharing because it either doesn't make sense to share work or it doesn't pay to work on someone else's client, then you're not really a firm, just a bunch of lawyers sharing some overhead.

Kevin Grierson

The simple answer to your question is the partners have never been able to agree on a specific formula for weighting origination v. production. Some years, that percentage would make a big difference. Other years (more recently), it doesn't, because each of us is doing most of the production on our own origination. No one was willing to commit to a weighting for the indefinite future. Hence the annual review.

In any event, the reality is that any partner (in any firm) can essentially ask for a re-evaluation at any time (unless there are really onerous withdrawal penalties, which our firm doesn't have, and I expect most small firms don't have). So there's never really a formula that you can be sure will last forever.

Patrick W. Begos
