

Partner Compensation: Formula or Subjective

Presentation for:

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**CLOTHIER
& HEAD** PC

Compensation: The Root Cause of all Evil

$$\text{\$} = \sqrt[n]{\sum_{i=1}^{\infty} e^{v_i l}}$$



***How many of you are
involved in determining
Partner Compensation?***



***How many firms use a
Formula Based System?
(>90% Formula driven)***



*How many firms use a
Compensation Committee?*

*How many people here
today do not know how
Partner Compensation is
spread within their firm?*

***Does anyone have a
Compensation System
that works extremely well?***

*Why is
Compensation
important*

Types of Law Firm Compensation

- **Equal**
- **Lockstep**
- **Formulas**
- **Committees**
- **Benevolent Dictator**
- **The Smoke Filled Room**

Cash or Accrual?

Objective Data

- **Origination (Finder)**
- **Management (Minder)**
- **Billable Dollars (Grinder)**

Subjective Data: Development

- **Developing Associates**
- **Developing New Practice Areas**
- **Developing New Products**



Subjective Data: Leadership

- Firm Leadership
- Contributing the Firm Culture



Subjective Data: Hygiene

- **Billing Hygiene**
- **Firm Hygiene**

Subjective Data: Service

- **Community Involvement**
- **Client Service**
- **Transitioning Clients to Firm Clients**



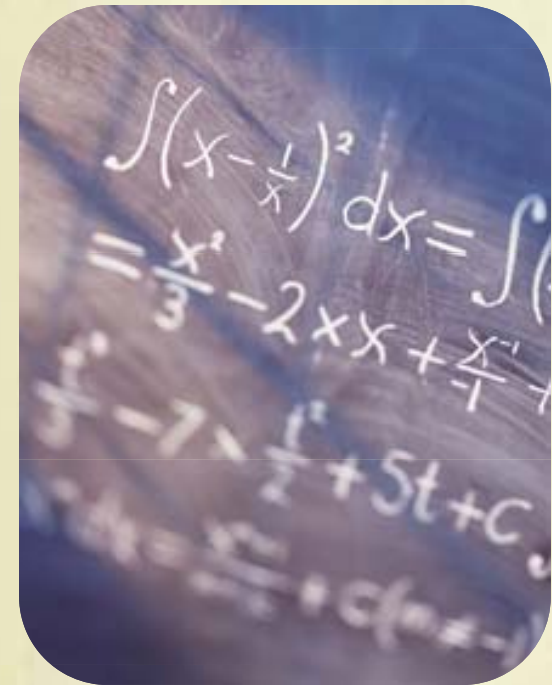
Open or Closed System?

- Does each Partner know what each other makes?



Why are Formulas Bad?

- Focus on statistics that make individual more profitable, not necessarily firm.
- Create silos
- Do not promote proper activities



Considerations

- 1. How do you migrate from a Formula System?**
- 2. How much do you reserve for bonus and discretionary distribution? (> 20%)**

Leverage: Example 1

Woods billable hours	1800
Hourly rate	\$300
	<hr/>
	\$540,000
Overhead allocation	\$150,000
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Grand Total	\$390,000

Leverage: Example 2

Woods billable hours	1000
Hourly rate	\$300
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	\$300,000
Overhead allocation	(\$150,000)
	<hr/>
Woods' Total	\$150,000

Associates billable hours (3 @ 1800 hrs)	5400
Hourly rate	\$250
	<hr/>
	\$1,350,000
Associates Cost (3 @ \$200k)	(\$600,000)
Overhead allocation (3 @ \$100k)	(\$300,000)
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Associates' Total	\$450,000
Woods' Total	\$150,000
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Grand Total	\$600,000

Leverage



Leverage

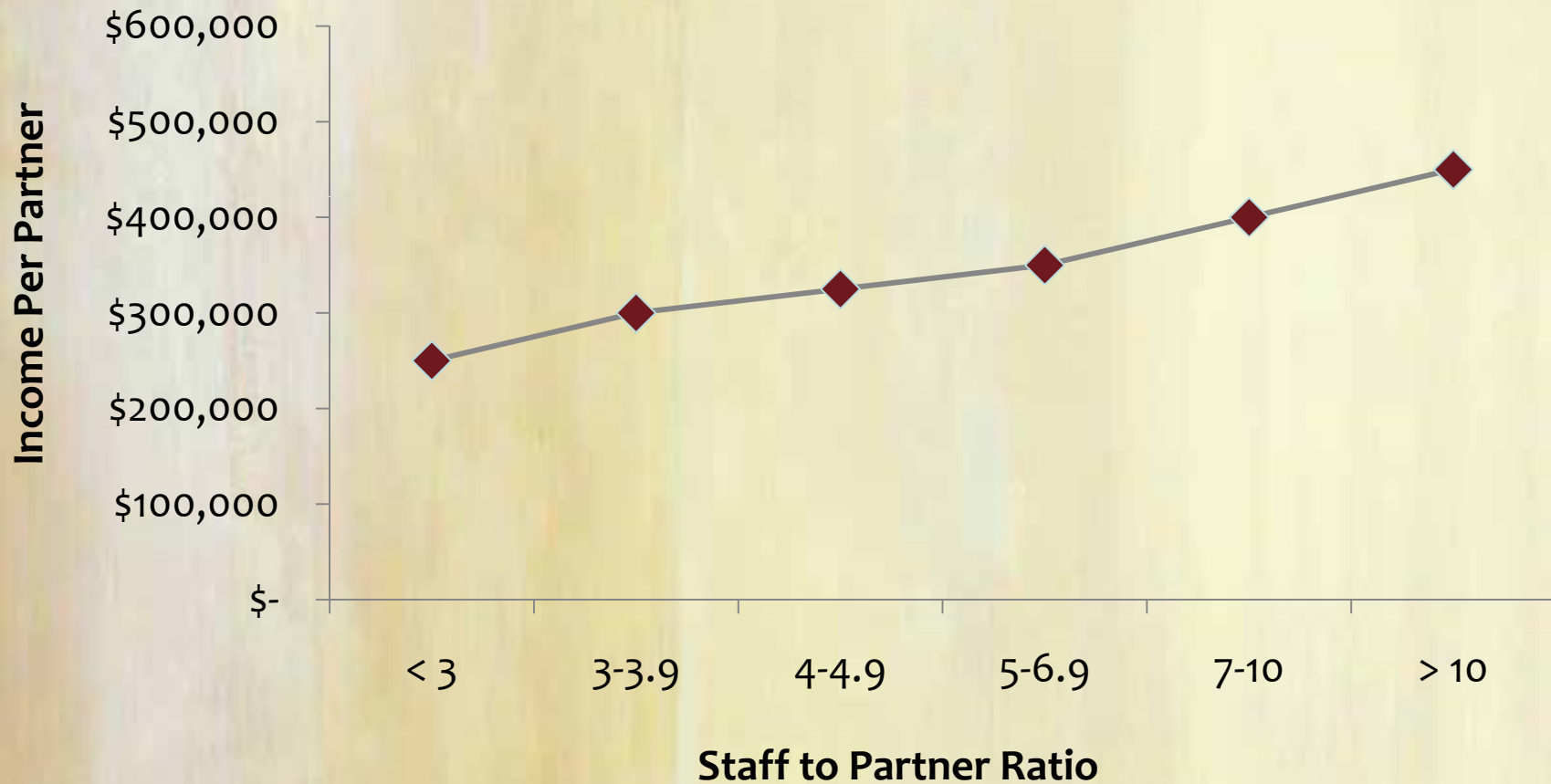
Bigger is Better



Graph source: The Rosenberg Survey, 2011

Leverage

Correlation of Staff-Partner Ratio to Profitability



Graph source: The Rosenberg Survey, 2011

How to Allocate

***What would a
Compensation Matrix
look like?***

Conclusions

- **Strict Formulas are limiting**
- **Balance between objective & subjective factors should be closer to 50/50 than 90/10**
- **Compensation should be collaborative not competitive**

Best Practice Systems Reward

- **Being profitable**
(originating, billing, collecting fees)
- **Serving clients well**
- **Transitioning clients**
- **Developing a product, process, or service area**
- **Mentoring associates**

Questions?

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