Table manners: rewarding performance without 'eat what you kill'

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1. Carrots and sticks

Compensation is a traditional 'carrot' in the 'carrot and stick' approach that many law firms use to motivate their partners' financial performance. Increasingly, law firms are discovering that an 'eat what you kill' compensation plan, in which a partner's remuneration is determined entirely or predominantly by his own fee production, is no more motivating than a cup of espresso coffee. It creates a buzz that lasts a little while and then quickly wears off.

This short-lived caffeinated effect arises from the fact that one cannot 'motivate' professional people to perform, not even with exhortations, threats, promises or money. People motivate themselves. All that a business organisation can do, if it wants to achieve lasting results, is to create and maintain the conditions that are part of a 'business case' that each individual considers when deciding the nature and extent of the performance that he is willing and able to produce.

This is why the traditional 'carrot and stick' approach seldom produces long-term results in law firms. Some partners are not especially attracted by the taste of the carrot and most of them learned long ago not to fear the stick.

This chapter presents alternative structures and methods that contribute to better long-term results, in terms of individual and group business performance, than does 'eat what you kill'. They focus on a full spectrum of activities, including fee production, by which partners contribute lasting value to their firm. Equally importantly, each of these alternatives avoids the genteel savagery that 'eat what you kill' compensation frequently produces in law firm partnerships. In extreme cases, the internal competition, suspicion, and raw selfishness that 'eat what you kill' can foster among partners can completely wipe out its benefits.

2. 'Eat what you kill' is not all bad

'Eat what you kill' does have some good points. It forces partners to focus on fee production. A partner who is content to drift along without working hard may do so, provided that he is literally willing to pay the price in the form of lower compensation, and provided further that the other partners are willing to permit the underperforming partner to continue consuming operating overheads indefinitely.

Because 'eat what you kill' focuses on fee production, it has a direct positive impact on the management of working capital. Partners in these systems usually pay very close attention to timely and accurate billing of work in progress and energetic

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collection of accounts receivable. They know that they will not get paid until the clients pay.

'Eat what you kill' can also have indirect positive impacts on marketing and business development. There is not much opportunity in an 'eat what you kill' system for the 'service partner' who relies primarily on other partners to provide his work. The easiest – and usually the only – way in which a partner can earn more money is to originate more work. This positive effect is negated, to some extent, by the fact that in many 'eat what you kill' systems the financial incentives tend to reward only work that the partner personally performs or supervises, which discourages cross-marketing. Some law firms modify their 'eat what you kill' systems to allow a commission on the fees that a partner originated; as discussed later in this chapter, however, these commission-based systems often require more work to administer accurately and equitably than they are worth.

Other forms of performance-based compensation, discussed below, can produce all of these benefits. Because they emphasise individual performance, however, 'eat what you kill' systems frequently work well in law firms that are essentially expense-sharing arrangements among partners with largely autonomous practices. The benefits that alternative forms of performance-based compensation can promote, such as internal synergies and the building of a long-term brand for the firm, as distinguished from its individual partners, are usually not priorities for the partners of these firms or even relevant to the business models by which they structure their practices.

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3. The costs of 'eat what you kill'

One of the biggest risks of 'eat what you kill' is that, after the partners have 'eaten' there may not be enough of the 'kill' left to feed sustainable long-term growth of the firm as a business institution. Some law firms operate under a short-term concept of their mission: that is, for each of the partners to make as much money as they possibly can, have a professional life that is reasonably satisfying, and then close the practice.

This vision, coupled with a compensation system that rewards only short-term results, usually means that the firm will not survive the founding generation of partners. The client base of the firm will slowly shrink, both in size and quality, as partners retire; and the last partner will turn out the lights and close the door. This is a perfectly acceptable long-term strategy (or, arguably, lack of strategy) for some firms.

'Eat what you kill' emphasises individual partner performance but does little to support the development of a competitive brand identity for the firm. In 'eat what you kill' firms, one is more likely to hear partners say "my client" rather than "our client". To the extent that the firm has any cohesive, consistent marketing strategy, it usually is based on the premise, often repeated by the partners, that "our clients hire the lawyer and not the firm". This concept may still be true for clients of retail law firms, which are smaller firms, usually local, that deliver relatively basic legal services to individuals and small businesses. It is becoming increasingly irrelevant to the engagement decisions of sophisticated consumers of legal services, who expect

both a good lawyer and a law firm that has the internal capabilities to back up the partner and ensure client service of the highest quality. In other words, sophisticated clients today are more likely to say, “Lawyer or law firm? We hire both.”

The fear of losing credit for a fee is a major motivation for partners to erect practice ‘silos’ and to hoard work during slow times. There is a strong correlation between the presence of practice silos and hoarding and an ‘eat what you kill’ compensation system. By creating disincentives for partners to recruit colleagues from other practice areas to participate in multidisciplinary practice teams, ‘eat what you kill’ systems can deny a law firm the opportunity of creating a more attractive offering of legal expertise that is more likely to satisfy all of a client’s needs in a complex matter. This suggests a subtle structural explanation for why firms that cannot offer a credible multidisciplinary team approach often have great difficulty winning larger, high-value projects, even when they may have all of the needed expertise dispersed around them.

There also is a high correlation between ‘eat what you kill’ compensation systems and the relative lack of cross-marketing or cross-practice staffing of engagements. In the most toxic ‘eat what you kill’ environments, the author has observed law firm partners who originate a matter outside of their usual practice and fail to refer it to a more qualified partner because they do not want to lose credit for the fee. Even in partnership cultures that have stronger values of mutual good faith, cross-selling usually occurs only by chance. This is because ‘eat what you kill’ systems frequently do not provide incentives that are significant enough for partners to be alert to cross-marketing opportunities.

The subtle barriers that ‘eat what you kill’ compensation systems raise against multidisciplinary practice teams and cross-selling combine to produce yet another observable characteristic of the law firms concerned. These firms tend to have substantially lower rates of repeat client work than firms with more broadly based compensation systems. In some law firms, such as retail litigation practices, this is a normal consequence of the area in which the firm specialises. However, for firms that want to develop a stable client base, with a substantial core of long-term profitable clients, ‘eat what you kill’ can be a subtle but stubborn obstacle.

Many law firms, and especially small- and mid-sized firms that face increasingly tough competition from larger law firms and non-traditional service providers (such as accounting firms), want more. These firms are avoiding the short-term temptations of ‘eat what you kill’ systems in favour of other methods to incentivise and reward partner performance and long-term contribution to the value of the firm.

4. A better way: goal-based performance compensation

The principal defect of ‘eat what you kill’ compensation is that it devalues, or ignores altogether, the actions by which partners support the long-term business performance of a law firm. Fees are convenient measurements of the level of business activity, but they are only short-term results. In some cases, reliance only on fee production can distort an evaluation of a partner’s performance. It is not unusual in some firms for the biggest fee producers also to be among the least profitable partners.

Determining partner compensation entirely or primarily as a percentage of fees

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collected is not the most accurate or reliable way for most law firms to define, promote, evaluate and reward individual partner performance. The trend among law firms that want a more comprehensive view of partner performance is to incorporate individual performance goals into the partner compensation system, with goal achievement producing a defined financial reward. With significant variations to fit each firm's business model, strategic objectives, and partnership culture, three basic structures are most frequently observed in law firms that want to clarify and, to some extent, quantify the nature and relative value of individual partner performance as a factor in compensation.

4.1 Performance-driven modified locksteps

This structure works especially well with firms that already use a lockstep structure. In a traditional lockstep system, partners 'move up' in the partnership, earning larger shares of the profits, principally by seniority. As a very simple example, each year a partner earns 10 profit points or shares, and his profit distribution is determined by the overall percentage of points or shares that he holds at the end of the fiscal year.

The most common form of a modified lockstep introduces other factors that can result in the award of additional profit points. These may include, for example, extraordinary performance in areas such as fee production, origination of a major new client, or completing a major project, such as opening a new branch office. To carry forward the example from the previous paragraph, a partner may earn 10 points for seniority plus another two points for exceptional performance.

In a performance-driven modified lockstep, the principal driver of upward movement is performance, not seniority. Although seniority may still be a factor, significantly more points are awarded for performance, often as high as a 5:1 or 6:1 ratio. In such a system, a partner with superior performance moves up the lockstep, and receives a larger profit distribution, faster than does a partner who earns only points for seniority. In some performance-driven lockstep compensation systems, a partner's upward movement is determined entirely by his performance points, with no points being awarded for completing another year as a partner.

Some firms allow a partner to retain and accumulate all of his annual performance points from year to year. Other firms carry forward only a percentage of the performance points earned each year. Either method creates a new concept of 'seniority', which is determined primarily, if not exclusively, by long-term performance, not longevity.

This system also works very well for associates and non-equity partners in determining the thresholds for eligibility for promotion. For example, when an associate achieves 300 points – however long or short a period of time that may take – he becomes eligible for consideration for promotion to non-equity partner.[1] Linking sustained achievement of performance goals, especially those relating to developing and demonstrating business and professional skills, will help assure that when a

1 This does not mean, however, that the lawyer actually will be promoted. Most firms apply other criteria, especially for election to the partnership. Achieving the minimum number of points means only that a lawyer has become eligible.

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lawyer is considered for promotion, he will have the skills and successful professional experience necessary to meet his responsibilities in the next highest level. By linking upward movement in the professional structure of the firm to performance, and not just to longevity, lawyers who demonstrate superior performance can advance more quickly than their contemporaries. This opportunity can help a firm retain its most productive lawyers, both at the associate and non-equity partner levels.

This is an extract from the chapter 'Table manners: rewarding performance without 'eat what you kill' by Norman Clark in Partner Remuneration in Law Firms: A Guide to Reward Structures, Performance Management and Decision-Making*, published by Globe Law and Business.*

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