The Legal Intelligencer

The Impact of Compensation on the Lateral Market

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by Jason Mandel | February 25, 2014

Case Digest Summary

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As the economy continues to improve, firms are now beginning to take more risks, while not forgetting the recent past. This caution has shifted to partners themselves, who have in many cases re-evaluated their practices and the firm at which they currently practice. Those who chose to step outside the walls of their firms have noticed that things are changing. It's a different world, with options abound not only in the size and scope of practice that different law firms offer, but in the way they compensate partners.

There are many reasons that partners tend to leave their firms: billing rates that clients can no longer support, conflicts, lack of leadership opportunities and, of course, compensation. As many times as I hear from candidates, "It's not about the money," and while that may be partially true, my experience tells me it's always about the money. Law firms both big and small are realizing that the methods they previously used in determining compensation are becoming archaic—whether it's a compensation committee that sits behind a closed door and arbitrarily decides what their own partners are going to earn in the coming year, or a dictatorship style. Many firms traditionally have determined compensation for the upcoming year based on previous years' production. This method has many flaws, chief among them being that previous production in no way is a guaranteed predictor of the future. Partners are typically paid a larger base salary, with a small bonus if they exceed expectations.

The fundamental change we have seen over the past five years is the model of smaller firms compensating their attorneys in a measurable format based on their production for the current year. In this method, a draw is determined, and partners are usually given credit for both origination and production, as well as any other area they contributed to the firm, such as leadership roles.

Our firm recently assisted a partner who had been at a midsized regional firm for the past decade. Under his current formula as an equity partner, he was given a large draw plus a bonus that was determined by a combination of how his practice did and how the firm did as a whole. As it turned out, regardless of how good of a year he had with his own origination and production, his compensation almost always ended up being around the same from year to year.

I presented many opportunities to this candidate and none really jumped out to him as exciting. He had a lot of required criteria in the firm he was seeking, but there had to be a persuading reason for him to ultimately leave the firm he had grown comfortable at. It was not until I presented him an opportunity with another regional firm that offered a compensation system based on measurable numbers, where his compensation year to year would truly be tied to his own origination and production, that his ears perked up. In this new model we determined that while there was risk, the potential significant upside along with the opportunity to help lead and shape a department were too much to pass up.

Partners who are considering making a move first need to evaluate their own practice before they can start looking at other firms. What makes your practice successful? Are clients likely to follow you if you go from a large international firm to one that has fewer than 100 attorneys? Do you need to be at a firm that has offices in 23 different countries when all of your clients are within the region? Are your clients working with you because of your expertise or because of the name of the firm at the top of your letterhead? What type of associate and administrative support do you need for your practice to be successful? These are all questions that need to be asked.

Let’s talk for a minute about firm size. There is little question that big firms provide not only a reputable name with years of experience that can be backed up with deal after deal, but also a breadth of expertise in a diverse range of practice areas that simply can’t be matched by small firms. Partners with practices that need a wide range of support in a multitude of practice areas, such as tax, securities, employment and complex financing, often need to be at a big firm.

In contrast, a state-focused litigation practice, corporate practices representing mostly privately held businesses, and estates attorneys can excel at a small firm. Though small firms typically can’t offer the same depth and varied experience, they nonetheless are often composed of a similarly bright group of lawyers who have chosen the model that bigger isn’t always better.

There is a common misconception that partners at big firms are earning significantly more than their colleagues at small firms. While it’s true that small firms typically charge lower rates and may be billing fewer hours than large firms, these firms are often run with significantly less overhead. While traditional large firms spin their wheels looking at the partners with the elusive million-dollar practice, small firms are making deals with partners with significantly less. While a partner with a $700,000 practice at a large firm may be a small fish in a big pond, those roles are often reversed when you place him or her in a small firm. Furthermore, these partners can often earn more at a small firm.

As the economy continues to improve, firms continue to look at ways to improve their bottom line. They are getting more aggressive and taking risks on deals that a few years ago they would have been quick to pass on. I've seen several situations over the past year where partners approached us with a sense of fear that they would not be marketable. In many of these instances, we not only were able to ultimately place the candidate, but I'm happy to report they had multiple offers.

The bottom line is that it's hard to gauge one's true worth without getting out there and testing the market.

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