Six Surprising Truths About Partner Compensation

By Blane Prescott

Partner compensation is not a subject typically taught in law schools, so it isn't surprising that law firms struggle with the issue. And it should not be surprising then that in their search for a better compensation system law firm leaders invent new metrics, adopt compensation models from other firms, or even occasionally throw up their hands under the rationalization that "*there is no perfect system*."

Compensation systems are often assumed to be self-evident because supposedly people will do what you pay them to do. But the truth is that human motivation (including lawyer motivation) is a much more complicated topic than most people want to believe, and many common assumptions about how to motivate and incentivize behaviors are wrong, according to both experience and scientific study.

The following are six of the most common misconceptions that create ongoing problems for law firms. But the good news is that law firms are often pleasantly surprised to find that changing a few key aspects of their compensation process has an extraordinary impact on both the success of the firm, and just as importantly, the happiness of the partners.

> ***Incentives don't create skills; they just act as a filter revealing who has those skills and who does not.***

1. **You Can't Incent People to Get a Personality.** One of the most pervasive misconceptions about human motivation is that you can motivate almost anyone to do anything with enough economic incentives. And yet there is more than fifty years of research and experience that soundly disproves this idea. Yes, it is possible to get people to increase their production on simplistic mechanical tasks through money. But the moment activities involve cognitive skills such as practicing law, the use of money as an incentive produces *worse* results. But how can that be? Isn't the whole US economy based on capitalistic incentives that create behaviors, that in turn earn rewards?

   The science and experience on this topic are very clear: Incentives don't create skills; they just act as a filter revealing who has those skills and who does not. Consider that almost every law firm incentivizes partners to generate significant, high quality clients, and yet only a handful of partners will ever do so successfully and consistently. Occasionally

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someone who never demonstrated those skills before will discover them, but the incentives do not create those skills, they merely reveal them.

Perhaps the easiest way to understand this lesson is to listen to something that is often repeated by senior leaders after a lifetime of trying to manage and motivate people: Despite all your cajoling, and money, and effort, **people don't change that much**. You can present opportunities to people, and you can help guide them, but it is largely up to them if they will step up and act.

The real lesson for leaders is to learn the unique skills and qualities of each partner, and then use your compensation plan to deploy those skills in ways that create the greatest value for the firm. Don't waste years trying to transform people or lecturing them about what they don't do well. **Having partners spend more time doing the things they do best creates extraordinary levels of happiness, high morale, and higher profits**. Unfortunately for a lot of Type A personalities who enjoyed success all their lives in learning and applying *information* (which is different than learning and applying *personal behaviors*), they falsely assume they can learn and exercise any behavior.

2. **Too Much Data Tends to Create Confusion and Unhappiness.** With the introduction of new technology there is more data available now than at any time in the history of law firms. Every activity can be measured, correlated, graphed, and presented almost instantly. And with the advent of more data most firms are constantly looking for new/secret financial measures, typically in the hope that will make compensation easier to set. But as has been demonstrated repeatedly, more data does not make for easier compensation decisions, better motivation, happiness, or better understanding of your decisions. It tends to do the opposite, especially with people who are highly intelligent, skeptical, and somewhat ego driven. Why is that? It turns out that human beings overwhelmingly tend to search for, favor and remember only that data which supports one's preexisting beliefs. And as a group lawyers suffer from this tendency more than most other professionals.

   It is not surprising then that many of the firms that have the most success with compensation, who have the happiest and most team-oriented partners, and enjoy the highest profits, also have the least data. Don't misunderstand the point – data by itself isn't bad, but data in a vacuum, especially overwhelming amounts of data, tends to create unhappy partners who never understand or believe in the justification for any compensation decision.

3. **Profits Are Not the Same as Compensation.** Like the last point, law firms can increasingly analyze the profitability of every functioning group in their firm – offices, departments, practice groups, lawyers, clients, matters, etc. And since profits are generally a good thing and create the firm's ability to pay its partners, many firms have succumbed to the temptation that if they can just calculate the profitability of each lawyer, they will know

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how much to pay them. So, for more than thirty years law firms have been experimenting with systems that calculate how much profit each person generates and then just pays each partner that amount, thereby dispensing with the need for compensation committees, communication, leadership, management, humans, etc.

Unfortunately, most firms quickly discover that short term profitability is not the sole measure of someone's contribution. Plus, year-over-year variations in profit (and to the surprise of most law firms, some partners actually lose money periodically) lead to wild fluctuations in compensation that most human beings find intolerable. Interestingly, most firms using pure profit-based compensation find that it actually reduces profitability, because it drives down collaboration and teamwork, and ultimately gets tossed out as a functioning system.

4. **What's More Important – The Process or The Results?** One of the most surprising facts about human motivation and compensation is that even if you get a compensation number right, you still won't necessarily make people happy. Many firms have lived through the experience of setting compensation and paying everyone consistent with the market for firms of their profitability, yet still have partners rioting about the process or results. Sometimes it is concern about origination, about unfairness, about the "black box" nature of setting compensation. Oddly enough, studies repeatedly show that people are far happier and better motivated when they believe the process is fair, than when they think just the results are fair. So, getting the compensation number right is only half the battle - the other half is effective communication and creating a pervading sense of trust and fairness in the process.

5. **Pre-Compensation Versus Post-Compensation Interviews.** While there are many firms that make the mistake of never talking to partners about compensation, successful firms often have a procedure that involves talking to partners either before they set their compensation, or after. And if polled, most people will say that a logical sequence is to set someone's compensation and then meet with them to explain it. After all, that's how most employees in corporate America are managed.

   Here again both experience and studies dispute the common wisdom: Part of the reason is that post-compensation interviews are primarily focused on rationalizing decisions that have already been made. In many post-compensation interviews the interviewee feels judged, and judged by someone who is generally defensive about their process and results. So, it is not unusual to find that firms engaging in post-compensation interviews tend to have higher levels of unhappiness about compensation, more dissatisfaction with the process, and seem to do the worst job in terms of modifying partner performance.

   In firms utilizing pre-compensation interviews, where the focus is on guiding the individual partner, (or more importantly, talking to partners about their performance and trying to

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help guide them in ways that utilize their strengths), interviewees feel helped, which is why they have remarkably higher success and satisfaction rates.

And just in case anyone is thinking that "our partners are all professionals, and they don't need coaching or help…they know what to do," I suggest you consider two facts: If everyone knows what to do, why aren't they doing it? And second, guidance and coaching are proven to be most effective for those with the highest intellects.

6. **Transparency is a logical, appealing, politically correct theory, but it pales in comparison to predictability and proven trust.** One of the common complaints from partners is that they want more transparency in their compensation process. Unfortunately, this is typically a red flag denoting deeper trust and process issues, and so partners reach out for a logical but often damaging cure.

   In its simplest form, transparency either means that every partner should have access to every piece of information that was used in the compensation process, and/or, it should be readily apparent to everyone why each partner is paid exactly what he/she is paid.

   Transparency is often requested when a firm is surprising too many partners with its compensation results (in violation of one of the most basic rules of great leadership – **Manage Expectations**, no matter how difficult that may be, because almost no one likes to be surprised with bad news).

   Unfortunately, real transparency is almost impossible to achieve unless a firm uses a pure mathematical formula to set partner compensation (Note: There is a reason why the use of pure formula compensation systems has virtually disappeared among the AmLaw 100 firms over the last quarter century). Or alternatively, unless every partner is privy to every piece of data/information/input/fact/secret that the Compensation Committee has access to, AND then treats all of that information in a completely objective, unbiased manner (see item 2 above).

   Here again the lesson is that many of the most successful, team oriented, profitable firms with the happiest partners do not feel the need to disgorge every fact – what those firms focus on is managing expectations, having honest conversations, provide a heavy emphasis on helping partners to succeed, a focus on competing outside the firm rather than inside, and engendering high levels of trust through strong and consistent communication.

Compensation is one of the more difficult challenges in running a law firm. That is primarily because most organizations succumb to two common problems:

- First, they tend to ignore most of the science and experience about human motivation because it inconveniently contradicts many preexisting notions.

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- And two (particularly in law firms), many leaders avoid face-to-face conversations about performance and want to believe that partners are so smart they never need any help or guidance.

But honesty and genuine help go a long way to creating happiness and success, even though doing both items well tends to be highly time consuming.

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