The *Fifth* in a Series of **Partner Compensation Structures**
"Modified Lockstep"

by Debra L. Bruce, JD, PCC

This is the 5th article in a series of 7 discussing structures that law firms tend to adopt for partner compensation.

Modified Lock Step

Description

Many firms have modified the lock step model to allow a committee to subjectively reward or punish behavior. The modification helps the firm to encourage essential behaviors such as business development, high productivity, recruiting, training and mentoring associates, management, and client relationship maintenance. It also provides the flexibility to bring underperforming partners into line, without having to completely expel a partner.

Some of the modifications may include the ability to promote a partner to a higher level earlier than the other classmate partners or demote a partner to a lower level. There may also be a "slush fund" for allocating bonuses to reward desired behavior. Appendix A (published as the 7th article in this series) contains an example of provisions that might be included in a modified lock step compensation plan. The author extends her gratitude to Bill McDonald, a partner at Thompson & Knight LLP, whose practice includes advice on law firm formation, for the provisions included in Appendix A.

In Appendix A, the agreement provides for seven lock step levels, but permits the management committee to assign each partner to the appropriate level annually. It also provides that a certain percentage of profit distributions, say 75%, will be made in accordance with the points assigned in each level. The remaining 25% of profits are allocated to the "slush fund" that is distributed by the management committee in its discretion. Thus, there are two mechanisms for modifying the lock step profits and loss allocation: level movement and discretionary distributions.

When It Works Well

As always, whenever the partnership compensation plan involves a subjective element, successful implementation of the plan depends upon trust in the fairness of the persons who make the allocation decisions. The compensation committee must not only signal its expectations and criteria in advance, they must maintain communications with the partners throughout the year. This will allow them to be aware of star performance in valuable areas not easily measured or reflected in monthly reports. It will also help them differentiate "slackers" from solid performers temporarily experiencing a bad year due to health or other personal issues, or a downturn in the client industry served.

This system allows the compensation committee to steer the firm in the desired directions by rewarding necessary new behaviors. If the firm needs to develop new practice areas or open an office in a new market to remain competitive, or experiment with innovative client service techniques, the management has the ability to protect or even reward the lawyers who take those risks for the betterment of the whole law firm. This structure also provides some flexibility in recruiting lateral hires of partners with essential skills or a good book of business. The firm can take more risk in offering an attractive compensation package when it has the ability to make adjustments if the lateral partner doesn't meet performance expectations.

When It Works Poorly

When the compensation committee consists of a homogenous group, they may fail to appreciate the performance challenges faced by lawyers in situations different from theirs. Often the committee consists of the most powerful veteran lawyers, who may have developed their client base in an earlier era when "the rules" were different. They may not recognize the tremendous efforts exerted by women and minorities to overcome obstacles to bring in business, or the competing demands on the time of younger lawyers. Often the biggest practice groups in the firm may get more attention (and therefore more rewards) than smaller practice groups. Being human, their judgment may also be swayed by personal friendships and animosities.

Compensation committees often tend to focus on easily measured metrics like billable hours and collections. They may fail to adequately reward or punish less quantifiable behaviors that impact the sustainability of the firm. The committee should have written criteria that include associate mentoring, management and firm administration, and business development and community service on the positive side. They should also evaluate attrition of subordinates, lone wolf tactics and irascibility as factors that negatively impact the sustainability of the firm.

The modified lock step may not work well when there are widely divergent values and profitability levels among attorneys, including highly competitive "rock stars." The rock stars may insist upon compensation so far above that of other attorneys that it doesn't fit in the formula.

Often lawyers take a short-term view, expect great leaps in compensation after a good year, and resent "carrying" the practice groups on the other side of the seesaw, whose earnings have declined. This natural conflict puts a lot of pressure on the compensation committee.

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