

# The *Seventh* in a Series of Partner Compensation Structure Articles

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This is the Appendix A mentioned in the previous articles in this series discussing structures that law firms commonly adopt for partner compensation.

## APPENDIX A Sample Partnership Agreement Provisions Respecting Compensation

Selected Provisions Of  
Agreement of Limited Liability Partnership  
Of  
A & B, L.L.P.

***[not intended as a complete partnership agreement]***

This AGREEMENT OF LIMITED LIABILITY PARTNERSHIP of A & B, L.L.P. is entered into to be effective as of the \_\_\_ day of \_\_\_, 20\_\_ by and among A ("A") and B ("B") (collectively, the "Partners") pursuant to the provisions of the [State] [Partnership Law], and according to the terms and conditions set forth herein.

NOW, THEREFORE, THE PARTIES AGREE AS FOLLOWS:

### Section I THE PARTNERSHIP

1.A *Statutory Compliance.* \* The Partnership shall qualify as a registered limited liability partnership in all applicable jurisdictions.

1.B *Noncompetition.* \* ["In term" competition is forbidden]

1.C *Definitions.* Capitalized words and phrases used in this Agreement have the following meanings:

(a) "Bonus Distribution" has the meaning set forth in Section 3.A hereof.

(b) "Draw" has the meaning set forth in Section 3.A herein.

(c) "Equity Partner" means a Partner admitted as an Equity Partner pursuant to this Agreement and holding a Capital Account.

(d) "Management Committee" means the committee described on Schedule 4.A.

(e) "Normal Retirement" has the meaning set forth in Section 7.A.

(f) "Partnership Level" has the meaning set forth in Section 9.1 herein.

(g) "Points" means the basis upon which the Management Committee allocates Partnership Profits and Losses pursuant to Section 2.A and distributes liquid funds pursuant to Section 3.A.

(h) "Buy-Back Price" has the meaning set forth in Section 12.2.

(i) "Responsible Collections" means, for any Retiring Equity Partner, any amounts received by the Partnership following such Partner's Retirement that, immediately prior to the Retirement Event of such Partner, shall be reflected as "work-in-process" or accounts receivable of the Partnership and for which the Retiring Equity Partner shall be the designated responsible attorney according to the books and records of the Partnership.

(j) "Working Collections" means, for any Retiring Equity Partner, any amounts received by the Partnership following such Partner's Retirement attributable to the hourly billings of the Retiring Equity Partner prior to such Retirement.

## Section 2 ALLOCATIONS

*2.A Profits and Losses.* [\*]% of the Profits and Losses for any Fiscal Year shall be allocated among the Equity Partners in proportion to the number of Points each Equity Partner holds as of the first day of the Fiscal Year and [\*]% of the Profits and Losses shall be allocated among the Equity Partners as determined by a simple majority of the Management Committee.

*2.B No Allocation to Partners Other than Equity Partners.* No profits or losses shall be allocated to Partners other than Equity Partners.

## Section 3 DISTRIBUTIONS

*3.A Monthly Distributions.* Except as provided in Section 13.2 hereof, on or before the fifth day of each month, the Equity Partners shall receive draws equal to the amount specified on Schedule 3.A ("Draws"). Cash distributions in excess of the Draws ("Bonus Distributions") shall be paid on a periodic basis as determined by a simple majority of the Management Committee and shall not exceed the amount by which the liquid funds of the Partnership as of the last day of the preceding month exceed the Reserve Amount. Prior to December 31, [20\_\_], the "Reserve Amount" at any particular time shall be a dollar amount equal to the average of the twelve previous months' Partnership operating expenses including Equity Partners' Draws (but excluding distributions to Equity Partners in excess of Draws). Beginning January 1, 20[\_\_\_], and continuing through December 31, 20[\_\_\_], the "Reserve Amount" shall equal 200% of the average of the twelve previous months' Partnership operating expenses. Beginning

January 1, 20[ ] and continuing thereafter through the term, the "Reserve Amount" shall equal 300% of the average of the twelve previous months' Partnership operating expenses. Notwithstanding the foregoing, a simple majority of the Management Committee may, from time to time in its discretion, specify any such other amount as the "Reserve Amount." [\*]% of Bonus Distributions to the Equity Partners pursuant to this Section 3.A shall be divided among them such that the aggregate of the Draws and such [\*]% of Bonus Distributions shall be allocated in proportion to the number of Points held by each as of the first day of the month during which the distribution occurs. Except as may be otherwise determined by unanimous decision of the Management Committee, the remaining [\*]% of Bonus Distributions shall be distributed among the Equity Partners (including members of the Management Committee) as determined by a simple majority of the Management Committee in its sole discretion.

3.B *Annual Distributions.* Except as provided in Section 13.2 hereof, within seventy-five (75) days after the end of each Fiscal Year, a simple majority of the Management Committee shall recommend to the Equity Partners for their approval the amount of capital contribution required for the operation of the Partnership (the "Required Capital") for the next Fiscal Year, which shall be \$X each Equity Partner until, acting at the recommendation of a simple majority of the Management Committee, the Equity Partners determine that a different amount is appropriate.

3.C *No Distributions to Partners Other than Equity Partners.* No distributions shall be made to Partners other than Equity Partners; rather, such other Partners shall be compensated by salary by mutual agreement of each Partner in question and a simple majority of the Management Committee.

#### Section 4 MANAGEMENT

4.A *General.* The day-to-day management of the Partnership shall be conducted by the Management Committee described on Schedule 4.A. The Management Committee shall have the power to adopt and enforce policies and concerning the management of the Partnership.

4.B *Equity Partner's Obligation to Pay Claims.* To the extent that the Partnership's policy or policies of insurance covering errors, omissions or legal malpractice of the Partners and those under the control of a Partner provide for a deductible per claim or occurrence, the Partnership shall pay such deductible if the Partnership is named as a defendant in a suit based upon a claim covered by such insurance, but if a claim is made solely against a Partner, then such Partner shall pay the deductible.

4.C *Loans to Partnership.* Any Person may, with the consent of the Management Committee, acting unanimously, lend or advance money to the Partnership. If any Partner shall make any loan or loans to the Partnership or advance money on its behalf, the amount of any such loan or advance shall not be treated as a Capital Contribution

but shall be a debt due from the Partnership. The amount of any such loan or advance by a lending Partner or such Partner's Affiliate shall be repayable out of the Partnership's cash and shall bear interest at such rate as the Management Committee and the lending Partner or such Partner's Affiliate shall agree but not in excess of the maximum rate permitted by law. With respect to any loan to the Partnership from a Partner or any Partner's Affiliate, the rate of interest shall be determined by the Management Committee taking into consideration, without limitation, prevailing interest rates and the interest rates the lender is required to pay in the event such lender has itself borrowed funds to loan or advance to the Partnership, and the terms and conditions of any such loan, including the rate of interest, shall be no less favorable to the Partnership than if the lender had been an independent third party. None of the Partners or their Affiliates shall be obligated to make any loans or advances to the Partnership, except as may otherwise be agreed in writing and signed by the Partnership, the affected Partner(s) and any applicable Affiliates of the Partner(s).

## Section 5 NEW PARTNERS

*5.A Admission of Partners Other Than Equity Partners.* An affirmative vote of a simple majority of the members of the Management Committee and of at least two thirds of the Partners (voting in number and not by Points) is required to admit a new Partner who is not being admitted as an Equity Partner, upon such terms as shall be established by the Management Committee.

*5.B Admission of New Equity Partners; Capital Contributions.* The Management Committee shall determine the number of Points to be awarded to such new Equity Partner, the initial Capital Contribution to be made by such new Equity Partner, and the terms and conditions of such payment. The Management Committee shall recommend such new Equity Partner to the Equity Partners. An affirmative vote of two-thirds of the members of the Management Committee and of at least two thirds of the Equity Partners (voting by Points and not in number) is required to admit a new Equity Partner under the recommended terms and conditions.

## Section 6 DISTRIBUTION LEVELS

*6.A Partnership Levels.* The Equity Partners shall be classified by the Management Committee among seven (7) partnership levels ("Partnership Levels") and awarded Points based on such Partnership Levels, as more specifically set forth on Schedule 6.A.

*6.B Annual Adjustment.* Within thirty (30) days prior to the beginning of each Fiscal Year of the Partnership, the Management Committee shall meet for the purpose of reviewing the performance and contribution to the Partnership of each Equity Partner relative to the Partnership Level of each Equity Partner. At each such meeting, the

Management Committee may elect by a two-thirds majority to raise, lower or not change the Partnership Level of any Equity Partner. Upon any change of Partnership Level, the Points for any affected Equity Partner will be changed to reflect the Points for the resulting Partnership Level.

## Section 7 EXITING THE PARTNERSHIP

*7.A Equity Partner's Buy-Back Price.* Subject to the terms of Section 7.B, the Buy-Back Price of a Retiring Equity Partner's Partnership interest shall be equal to the Interest Value of the Retiring Equity Partner's interest as of [A DATE], less any Partnership distributions to, or payments on behalf of, the Retiring Equity Partner after such day.

*7.B Closing Date; Payment of the Buy-Back Price.* The closing of the redemption of the Retiring Equity Partner's interest shall occur on a date and time mutually convenient to the Partnership and the Retiring Equity Partner; provided that the closing date shall occur no later than the sixtieth day following [A DATE].

The Buy-Back Price for the Retiring Equity Partner's interest shall be paid in installments without interest ("Buy-Back Payments") as follows -

(A) The Buy-Back Price attributable to the Capital Account of the Retiring Equity Partner shall be paid in 24 equal consecutive monthly Buy-Back Payments beginning on the closing date; and

(B) The remainder of the Buy-Back Price shall be paid Buy-Back Payments each month following such Partner's Retirement in amounts equal to 15% of the Responsible Collections and 35% of the Working Collections for such Retiring Equity Partner collected by the Partnership during each then immediately preceding month.

Notwithstanding any other provision of this Agreement to the contrary, in no event shall aggregate Buy-Back Payments made to a Retiring Equity Partner exceed his or her Buy-Back Price.

Any credits determined under Section 7.F shall be applied to the next succeeding payments otherwise due pursuant to the terms of this Section.

*7.C Retirement.* A Partner shall be permitted to retire under this Section 12 on the December 31 next following his or her [ ] birthday by giving written notice of his or her intention to retire as a Partner at least sixty (60) days before the day of such retirement, which notice shall state the date upon which such retirement is to occur. A Partner may retire at any other time with the affirmative approval of Partners holding more than two-thirds (2/3) of the total number of Points then held by all Partners (other

than such Partner). A Partner shall retire on the December 31 next following his or her [ ] birthday, unless he or she is permitted to continue to be a partner by the affirmative vote of Partners holding more than one-half of the total number of Points then held by all Partners (other than such Partner). The day designated hereunder for the retirement of a Partner pursuant to this Section 7.C shall be the day of such Partner's "Normal Retirement."

#### *7.D Expulsion.*

(a) *For Cause.* (i) Any Partner who is not an Equity Partner may be expelled immediately for cause upon the affirmative vote of two thirds of the Partners (voting in number and not by Points) at a duly constituted meeting of the Partners specifically noticed for such purpose, and (ii) any Equity Partner may be expelled immediately for cause upon the affirmative vote of two thirds of the Equity Partners (voting by Points and not in number) at a duly constituted meeting of the Equity Partners specifically noticed for such purpose, that any of the following reasons for expulsion exist: \_\_\_\_.

(b) *Without Cause.* A Partner who is not an Equity Partner may be expelled immediately and without determination of cause upon the affirmative vote of three fourths of the Partners (voting in number and not by Points) at a duly constituted meeting of the Partners specifically noticed for this purpose. An Equity Partner may be expelled immediately and without determination of cause upon the affirmative vote of three fourths of the Equity Partners (voting by Points and not in number) at a duly constituted meeting of the Equity Partners specifically noticed for this purpose. This method of expulsion may be employed notwithstanding the fact that grounds may exist for expulsion for cause.

*7.E Withdrawal.* A Partner may withdraw voluntarily from the Partnership as of any December 31 by giving written notice of his or her intention to withdraw at least sixty (60) days before the day of such withdrawal, which notice shall state the date upon which such withdrawal is to occur.

*7.F Value; Credit for Uncollectible Amounts and Assignment Thereof; Contingent Fee Matters.* The "Interest Value" of an Equity Partner's interest, as of any day, shall (subject to the further terms of this Agreement) equal the sum of

- (I) 100% of the Retiring Equity Partner's Capital Account as of the end of the month in which the Retirement Event occurs, plus
- (II) The sum of (A) 15% of the sum of "work-in-process" and accounts receivable of the Partnership for which the Retiring Equity Partner shall be the designated responsible attorney according to the books and records of the Partnership immediately prior to such Partner's Retirement and (B) 35% of the sum of "work-in-process" and accounts receivable of the Partnership attributable to the hourly billings of the Retiring Equity Partner

prior to such Retirement, less (C) reductions and credits as provided in the further terms of this Section 12.9.

Notwithstanding any other terms of this Agreement, the Interest Value of a Retiring Equity Partner shall be reduced, and the Partnership shall be entitled to a credit against its obligation to pay the Buy-Back Price for any Retiring Equity Partner, to the extent amounts otherwise included in Interest Value under item (II) above are not collected by the Partnership. Any "work-in-progress" or accounts receivable resulting in a credit under the preceding sentence shall be assigned to the responsible Retiring Equity Partner. If a Retiring Equity Partner shared responsibility for such "work-in-progress" or accounts receivable prior to the Retirement Event with any other Partner (Retiring or otherwise), then such items shall reduce the Partnership's obligations to Retiring Equity Partner and shall be assigned to the Retiring Equity Partner on an equitable basis as determined by the Management Committee acting in good faith.

Subject to the last sentence of this paragraph, the Interest Value of a Retiring Equity Partner's interest attributable to the Retiring Equity Partner's Capital Account shall be determined by the Management Committee based on the federal income tax returns of the Partnership for the year in which the Retirement Event occurs. The Management Committee shall forward copies of the federal income tax return and the amount of such Interest Value to the Partnership and each of the Equity Partners by written notice. For purposes of this Section 12.9, billed, unbilled or billable attorneys' fees and unreimbursed advances relating to contingent fee work undertaken by the Partnership shall not be considered "work-in-progress" or accounts receivable for purposes of any Interest Value, Buy-Back Price or Buy-Back Payment calculations and shall be excluded from any such calculation.

## Section 8 MISCELLANEOUS

8.A *Arbitration.* If a dispute arises with respect to any term of this Agreement, any party to the dispute may request arbitration to resolve the dispute by notifying the other parties to the dispute in writing that arbitration is desired. In such event, the dispute shall be submitted to binding arbitration in City2, [State2] in accordance with the commercial arbitration rules of the American Arbitration Association and the further terms of this section on or before the expiration of 60 days following such notice before a single arbitrator. Judgment on any award resulting from such arbitration may be entered by any court having jurisdiction over the dispute. The arbitrator shall not limit, expand or modify the terms of this Agreement and shall not award damages in excess of compensatory damages, and each Partner waives any claim to any damages in excess of compensatory damages. The content and result of the arbitration shall be held in confidence by all participants and Partners.

### Schedule 4.A

## Management Committee

The Management Committee shall be initially constituted of A and B. Membership and operation of the Management Committee shall be determined in the manner set forth in policies set forth by the Management Committee from time to time. The Management Committee shall select a member to chair and preside over its meetings, which member shall serve in such capacity for a term ending on the next succeeding December 31. The Management Committee shall have the power to delegate to Partners, employees or other representatives of the Partnership any responsibility or responsibilities which the Management Committee shall from time to time deem appropriate or necessary. The Management Committee hereby irrevocably delegates its authority to manage the day-to-day affairs of the City1 office to A and its authority to manage the City2 office to B. Such delegation shall continue until changed in accordance with Section 5.2 of the Partnership Agreement.



Schedule 6.A

Partnership Levels

<u>Level</u>	<u>Points</u>	<u>Monthly Draws</u>
1	175	\$22,000
2	135	\$18,000
3	100	\$15,000
4	70	\$13,000
5	55	\$12,000
6	45	\$10,000
7	30	\$ 9,000