

# California Law Business

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Closing Argument Sandford A. Lechtick

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## Pay Raze

**The wild disparity in partner compensation at the various California law firms is having unintended consequences.**

I was shocked upon learning that the partner I was sipping café latte with, I'll call him "Frank", who had consistently been generating between \$1.5 million and \$2 million the last few years, whose practice was clearly on an upward trajectory, who had been averaging close to 3,000 hours per year (billable and administrative), who was a leader in that office, was earning not much more than \$150,000.

In fact, despite his revenue generation strength and strong collections, he had never earned significantly more than \$150,000. This book vs. compensation disparity was even more magnified when the very next day I met a partner for lunch, I'll call him "Bill" who not only picked the most expensive restaurant in town (and ordered a big steak), but whose collections the last five years hovered no more than \$500,000. And he was earning \$300,000.

While I spent a significant amount of time evaluating partners' books, commensurate compensation levels and career growth potential, the gap between those two partners got me thinking about the gulf, and sometimes huge gulf, that separates many partners - not just those at different firms but sometimes those at the same firm. The disparity of bucks at the partner level is, in a word, startling.

Consider: Some lawyers who consistently exceed \$1 million in collections sometimes makes less money than others at the same firm who originate less revenue, bill fewer hours and play more golf.

Consider: Lawyers at some firms earn twice as much money as those with the same book of business at comparable firms.

While one would think there is a strong link between contribution and compensation, at many firms, especially "lock-step" firms, this is not the case. In fact, in some cases, a partner's hours, collections and originations are almost irrelevant to what he or she gets - especially if they're outside the "in-crowd".

While one can argue the case, I believe many partners have left Pillsbury Madison & Sutro the last couple of years because of a compensation system that didn't fully reward its producers and over-rewarded many non-producers. Orrick, Herrington & Sutcliffe, a major recipient of Pillsbury talent, has been more successful at rewarding revenue-

producers, cutting costs and generating new business. Orrick's partner profits are at least \$200,000 more than Pillsbury.

Certainly firms with lock-step compensation systems pay senior partners - even those without much of their own business - more money. In these environments, up and comers, such as the fellow I had coffee with, often do not receive a proportionate share of the profits. If the firm is going through tough financial times, the differential is usually greater. Using logic that gives heartburn, in these situations those generating most of the revenue take the biggest hits. It doesn't take a PhD. To figure out that significantly underpaid rainmakers will leave - which is a shame since they are the firm's future leaders. It is no surprise that Café Latte Frank, an incredibly loyal partner, one who found it very tough to leave, just moved to another firm.

As a rule of thumb, those at large firms earn more than those at small firms. The exceptions will be elaborated on shortly. The average compensation for partners at well-run business firms under 50 lawyers is roughly \$200,000 to \$225,000; at mid-sized firms numbering between 50 to 150 lawyers, \$250,000 and at firms of 150 attorneys or more, roughly \$300,000. While California firms such as Latham & Watkins; Brobeck, Phleger & Harrison; Gibson, Dunn & Crutcher; O'Melveny & Myers; Paul, Hastings, Janofsky & Walker and Orrick, Herrington exceed \$500K in partner profits, the next rung is \$250,000 to \$350,000.

While the overhead of small firms is lower, larger firms generally have higher rate clients, a larger stable of clients, greater depth/breadth to exploit business opportunities and attorneys who consistently bill more hours. Larger firms are generally better managed, run more like a business, implement marketing strategies and are usually not dominated by one benevolent dictator who runs the firm as his personal fiefdom. Plus, larger firms generally have a much easier time attracting revenue-producing partners and the brightest, best-trained associates.

I know partners who earn \$600,000 to \$800,000 at firms where average partner profits are \$350,000 and partners at some firms earning \$250,000 where partner profits are \$500,000 and more. In addition, with almost all firms resembling a pyramid, some have steeper inclines than others - where a few at the top earn the big bucks and the others significantly less. At Christensen, Miller for instance, four or five partners earn, to the best of my knowledge, \$1 million, but there is a steep drop off after that. If those earning the highest compensation at their firms are generating \$2 million to \$3 million or more and others generating \$700,000, that's one thing. But some firms have partners earning a disproportionate compensation based on their contribution, which may be influenced more on whether they helped stitch the firm's fabric 30 years ago. Unfortunately, some of those threads are rather frayed.

In addition, there is the issue of non-equity or income/contract partner vs. equity/capital partner. At some firms the distinction is huge, at others the distinction is blurred. In fact at some firms, non-equity partners are in reality, glorified associates. And in some instances, income partners actually earn less money than senior associates. While it is

true that some law firms reward personal billable hours over everything else, and other firms reward revenue originations plus billables, it is also true that the “in-crowd” often make a lot more money at lock-step firms than they would at a merit-oriented firm. And with some irony, it is often the overly compensated partners who accuse the hard changing “ingrate” of disloyalty when he or she leaves. While there are some exceptions, I have found that those unhappy with the change of lock-step systems to merit systems are usually those who both dislike and are not good at hustling business, schmoozing and selling a product - themselves.

Partners who are evaluating how they stack up on the compensation ladder or are considering moving to another firm, should consider a few questions that may put the situation in proper context:

- What is the specific mechanism for determining partner compensation?
- What do you have to achieve in billable hours, collections and total revenue generation to achieve various compensation levels?
- What is the mechanism to move from income or contract partner to equity partner?
- What are the specifics of equity vs. income partner? (In some situations, the income partner can get most of the advantages of equity - without liability of ownership or buy-in).
- What is the buy-in?
- How does the benefit package compare with your present package? What other perks are thrown in? (e.g. car, marketing/business budget, paid seminars, etc.)
- Does the firm put its money where its mouth is and truly support business development activities?
- How are laterals compensated vs. homegrown partners? (In some cases, laterals do much better - especially if they have a highly desirable area of expertise or client base.) During the courtship phase when they're turning on the charm, make sure you also spend some time with lateral partners concerning these topics. Those evaluating firms must pay particular attention to the firm's historical dynamics for attaining various compensation levels, partnership, etc. Finally, laterals must learn beforehand, what are the firm's expectations of them; what is the time period for achievement; what support will they get; and finally what is the situation if they fall short?

Today, many firms are moving in the direction of merit compensation systems. I think those lawyers who bust their butts, who get out and hustle, who are constantly striving to deepen and broaden their roots in the community, who are their firm's top revenue producers, and up and comers, should make more money. And those “partners” who think and act like employees rather than owners, should be paid accordingly. On the other hand, firms should not focus just on books of business but reward those who lead by example, who share clients, who focus on making the firm stronger, who walk their talk and are partners in the true sense, in deed - not just word. Those who mentor associates, attract and help retain talent are the real fabric of the firm and should be rewarded. These people can be worth their weight in gold. Quite frankly, some of the

top rainmakers are terrible managers and somewhat idiosyncratic in their behavior. The way I see it, successful law firms must balance merit compensation systems with systems for rewarding those who strengthen the firm as well as the bottom line.

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