

Emerging Partnership Models; Lessons for the Legal Profession in Nigeria

November 2014

Discussion paper at the 2014 NBA
Annual Conference of Section on Legal
Practice

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Different perceptions of Partnership

Different perceptions of Partnership

- A contractual relationship between two or more persons carrying on a joint business venture with a view to profit, each incurring liability for losses and the right to share profits.
- A legal contract entered into by two or more persons in which each agrees to furnish a part of the capital and labor for a business enterprise, and by which each shares a fixed proportion of profits and losses
- A partnership is a **tailored business relationship** based on mutual trust, openness, shared risk and shared rewards that results in business performance greater than would be achieved by the two firms working together in the absence of partnership.

It could be argued that most legal practitioners in Nigeria see partnership on the basis of the first two definitions.

The Partnership Model

Types of Partnerships

- **Traditional/General Partnership:** Every partner is jointly liable for all debts and obligations of the firm sustained while the person is partner. As such, the hazards each partner faces as a result of the acts of the other partners and employees are quite significant.
- **Limited Liability Partnership (LLP):** Is a hybrid of the general partnership in which partners maintain the same economic relationship as in a general partnership, but partners are not jointly liable for the debts and liabilities of the partnership
- **Equity Partnership:** Partners here are part-owner of the business, and are entitled to a proportion of the distributable profits/loss of the partnership in proportion to their ownership percentages.
- **Non Equity Partnership:** Partners are employed and given the title of partner, but have no financial interest in the firm. They earn salaries or share in total profit based on their performance and contribution to the firm.

Other Partnership Types

- **Multidisciplinary Practice:** is a partnership of professionals of a practice with professionals outside of that core practice who support or compliment the core practice. For example, a partnership of Accountants and non-Accountants (say lawyers) that provide clients with a wider range of services by one firm.
- **Virtual Firms:** In this digital age, some people have advocated for virtual partnerships. The idea is to pull together professionals from anywhere in the world to form a ‘dream team’ of sorts who work by logging into a server from their locations. A case in point is American virtual firm Axiom Legal (www.axiomlegal.com).
- **Corporate Structure:** Professional service firms have been under pressure for a while now to become more corporate or business-like in their structures .This corporate model is at best a hybrid of the typical Partnership model and a corporate governance model.
 - The interests of partners as shareholders is separated from the management and operational decisions of the organization
 - There is an Executive Board
 - Managing partner role is more executive and decisions are less consensus driven

Basic principles of Partnership

Basic principles

Partnership: What it means

- 1. Every partner is a part owner of our business** –Every partner is a part-owner of all of our businesses no matter how configured or the entities through which we trade & generate the assets. This means collective ownership of our different client portfolios and assets – current client portfolios, goodwill , etc, and all of our capacity to generate future revenues. Partners have an **undivided interest** in the business.
- 2. Partners are the managers of our business** and therefore accountable for our **Performance** and ultimately our **Results**. Accordingly, we must hold each other accountable to one another, and **to the firm**. Despite the impact of brand, synergy and leadership roles on our results, we may largely be able disaggregate our results and map to individual partners.
- 3. Performance and Results** - Our results are primarily our financial performance - (i) portfolio growth from new work, new clients, etc, generated, (ii) top line revenues from delivered work, (iii) cost contained, managed &/or optimized, and (iv) bottom line results. It also includes our performance on Strategic management, R&Q management, People management, Market positioning and other measures of performance. For each key metric we have a partner who is responsible, and who can be held accountable. To hold a partner accountable there needs to be clarity about the performance target(s). Such metrics/targets will be quantitative, qualitative and simple to determine (actual performance), and controllable by the partner

Basic principles

Partnership: What it means

- 4. Partners have different capabilities and roles**, and over time, all partners will have contributed in one form or the other to the creation of the current client portfolios and staff capacity in varying degrees. For clarity, every partner will have **generated work** – new clients or new work, **over time**. In addition, every partner will have **delivered** client work **over time**. All other things being equal, the longer one has spent as a partner, the more it is expected that he/she is likely to have contributed to the creation of the current client portfolio and other assets owned by the businesses. Thus, contribution may be loosely correlated to time spent as a partner. It is clear from our experience that contribution to the commonwealth of client portfolios is not necessarily directly related to time spent as partner. But time spent as a partner is the simplest measure of this relative accretive contribution.
- 5. Leadership :** The **Client Service Partner (CSP)** role is one of our key leadership roles as our business is impacted significantly by success or failure in this role – be it risk management, client management, staff management, engagement economics management etc. The CSP role is the front line role of how we deliver the firm to clients and to all of our people. It is therefore a very significant role.

Partnership Options

Partnership Options

There are very many profit-sharing options for partnerships, ranging from the simple to the really sophisticated. The sophisticated models require record keeping and measurement of many variables in order to create 'fairness' using algorithms that reflect many assumptions of performance and contribution for/from the different roles assumed to operate in the partnership.

A partnership operates largely on the basis of mutual respect and trust between partners. Any option to be considered should therefore seek to promote those attributes, while capturing the facts that (i) there needs to be minimal resentment amongst partners about how the model operates in profit-sharing (ii) the partners need to be rewarded broadly in line with their contributions (however defined), and (iii) partners feel committed to the firm and feel that the model will encourage potential partners to want to join the partnership if offered, i.e. a belief that the model encourages sustainability and continuity of the firm.

Four common options are; Equal Partnership option, Lock-Step option, Modified Hale and Dorr system and Team Building system.

It is safe to say that there are very good examples of strong legal firms in Nigeria, some of whom have adopted these options or a cocktail of the options.

The Equal Partnership system

In this system, all partners share in profits equally or within defined groups of partners. For example, in a firm with eight partners that are divided into four senior partners and four junior partners, the senior partners equally share 60 percent of the firm's total profits (15 percent each), while junior partners equally share 40 percent of the firm's total profits (10 percent each).

This system presupposes that each partner contributes equally to the overall firm performance, albeit in different ways – billable or non-billable. Individual performance is much less important than how well the firm does as a whole. As long as the firm does well, then the individual partners will do well. This allows for individuals to have performance swings – up years and down years – as long as overall the firm does well.

Strengths

The paramount financial concern is firm profitability. The bigger the pie, the bigger a partner's share of profits so emphasis is on the firm's performance.

Partners focus their competitive instincts externally rather than internally i.e. they collaborate to outperform other firms.

Partners work well together. They do not hoard either clients or files - their goal is to increase the total profit pie.

Partners have a certain sense of security as to what their income will be at any given time.

Weaknesses

Lack of incentives: There is no perceived or real value in working harder. There is no individual financial difference between the partner who works long hours and the one who doesn't.

Lack of incentives can lead to resentment of partners who are perceived as lazy or underachieving.

The impact of the most profitable partners leaving an equality firm can be devastating. Eventually only the poorer performing partners remain, profitability declines and the partnership dissolves because there is no point staying together as a firm.

The Lock-step system

In the lock-step system the basic concept is that each partner is rewarded an ever-increasing share of the firm's profits, based solely on seniority. The longer a partner remains with a firm, the more money the partner will make.

In a lock-step, income can be divided exactly along seniority lines or divided into levels. For example, the divisions might be senior partners (more than 15 years as a partner), middle partners (5 to 15 years as a partner) and junior partners (1 to 5 years as a partner).

Strengths

Offers high financial rewards for the longest serving partners, providing a great deal of stability. Few partners, once committed to the system, would leave before they had risen to the top of the compensation ladder.

Partners have a sense of security from knowing that their share of the profit pie is pre-set. The only variable then becomes how big the pie will be. This security can help to create a more collegial atmosphere among the partners.

Encourages external rather than internal competition among partners because the only way to increase individual income is by making the overall pie bigger.

There is no financial advantage to file/client hoarding among the partners so they tend to work well together, again contributing to the collegial atmosphere

Weaknesses

Lock-step does not directly reward individual contributions and initiatives. As a result, some partners will not put in extra effort when they know that all they need do is contribute at a normal rate to keep progressing along the compensation path.

This lack of financial incentives can have a great impact on a firm's profitability because, in some cases, it is actually a de-motivator.

The younger partners may feel resentment toward the senior partners.

In lock-step firms where senior partners are perceived to be taking more than their appropriate share of profits, there will eventually be an exodus of the younger, hard working partners. They will move to firms that are prepared to recognize and reward their efforts. The result for the firm is lower profits at best, and at worst, disintegration.

Modified Hale and Dorr System

This is considered as the first incentive-based compensation system. There are three categories in which a partner could earn income: Finder (originator of the client), Minder (responsible for the client) and Grinder (the partner actually doing the work), there is also a small portion of profits set aside to be distributed at the discretion of the partners. The clear assumption is that if everyone is motivated by the compensation system, the firm as a whole will perform well. In this system, the weight given to the various categories depends on the firm's vision and goals and also the current strategy.

Strengths

As the system places more value on individual contributions, Partners know exactly what is required if they wish to increase their income. The system allows them to become the masters of their own financial destiny, either higher or lower depending on personal goals.

There is less bitterness toward a partner who is perceived to be contributing less to firm profitability because when they contribute less, they receive less. Of course a partner who performs well below normal expectations will still have problems.

Seniority has no direct value in compensation, though a more senior partner would probably bill at a higher rate and therefore command a larger percentage of the grinder share of the profits when doing the same amount of work as a younger partner.

Weaknesses

Given the choice, partners will always opt for the billable work ahead of the non-billable unless rewards are built in for non-billable time – firm management, coaching, recruiting – which are necessary for running a profitable firm. Partners become so concerned with personal numbers and income, little time or effort gets expended on the type of activities that build teams.

Also, partners who are paid only for their production may make the mistake of hoarding clients and work. This can lead to resentment, and impact on quality when partners perform work in areas in which they are not proficient. It is demoralizing as well to the juniors who are not getting enough work or enough quality work.

Team-Building System

This is the ultimate team system of compensation. Individual contributions are given little consideration while firm profitability and practice group or department performances are paramount.

The formula for the team-building system bases 50 percent of a partner's compensation solely on how well the firm does financially. Another 40 percent is based on a practice group or department's financial performance, and the remaining 10 percent is based on the individual partner's performance. These percentages can be varied to suit a particular firm's vision areas as the weighting would be driven by the firm's vision and goals and its current strategy.

Strengths

The system is totally objective and it downplays the role of the individual. All partners in a group or department will sink or swim based on collective efforts.

It promotes firm goals. When everyone pulls together the firm succeeds to the highest levels and the competitive focus is external rather than internal.

There is cooperation and collegiality at the group and firm levels: Partners have faith in one another to always do what is best for the team – to willingly waive individualistic tendencies when they conflict with the goals of the team.

Weaknesses

Some partners may feel that there is a lack of recognition for seniority and experience. Unless there are levels of partners within the system, all partners would earn about the same amount.

Partners may not make enough of an effort because they don't see the direct rewards and don't feel they need to perform at a level above others. The individual large contributor may well leave in search of a firm that will reward individual efforts more highly.

Global Trends in Legal Practice Partnership

Global Trends in Legal practice Partnerships

- More law firms are revising their partnership arrangements in ways that bring them closer to their counterparts in other parts of the world.
- The trend follows challenges faced by law firms in ensuring their partnership models remained profitable during the economic downturn of late 2008 and 2009.
- But it has also been driven by a new generation of lawyers who are more concerned with lifestyle than investing capital and putting in the long hours to achieve traditional partnership status.
- In Canada for example, the primary change in partnership structure has been the introduction of ‘non-equity partners’

The ‘non-equity partner’ lengthens the track to equity partnership to give young lawyers more time to develop their skills and enables the established partners to postpone their decision on who can join them, while preserving the profits for those who’d invested capital in the firm years earlier.

Global Trends in Legal practice Partnerships

In the UK two trends have characterized the market in recent years;

1. A movement away from large tiers of salaried partners towards an ‘all equity’ or more specifically ‘full equity’ plus ‘fixed-share equity’ arrangement.

Motivated by HM Revenue & Customs recognition of FSE Partners as Partners rather than employees, making it instantly favourable for firm and individual, from a tax/NI perspective, to switch from salaried to FSE status. But it has also been driven by a new generation of lawyers who are more concerned with lifestyle than investing capital and putting in the long hours to achieve traditional partnership status.

2. A movement away from pure lockstep towards a more merit based system whereby advancement is determined by performance alone or by some combination of performance and length of service.

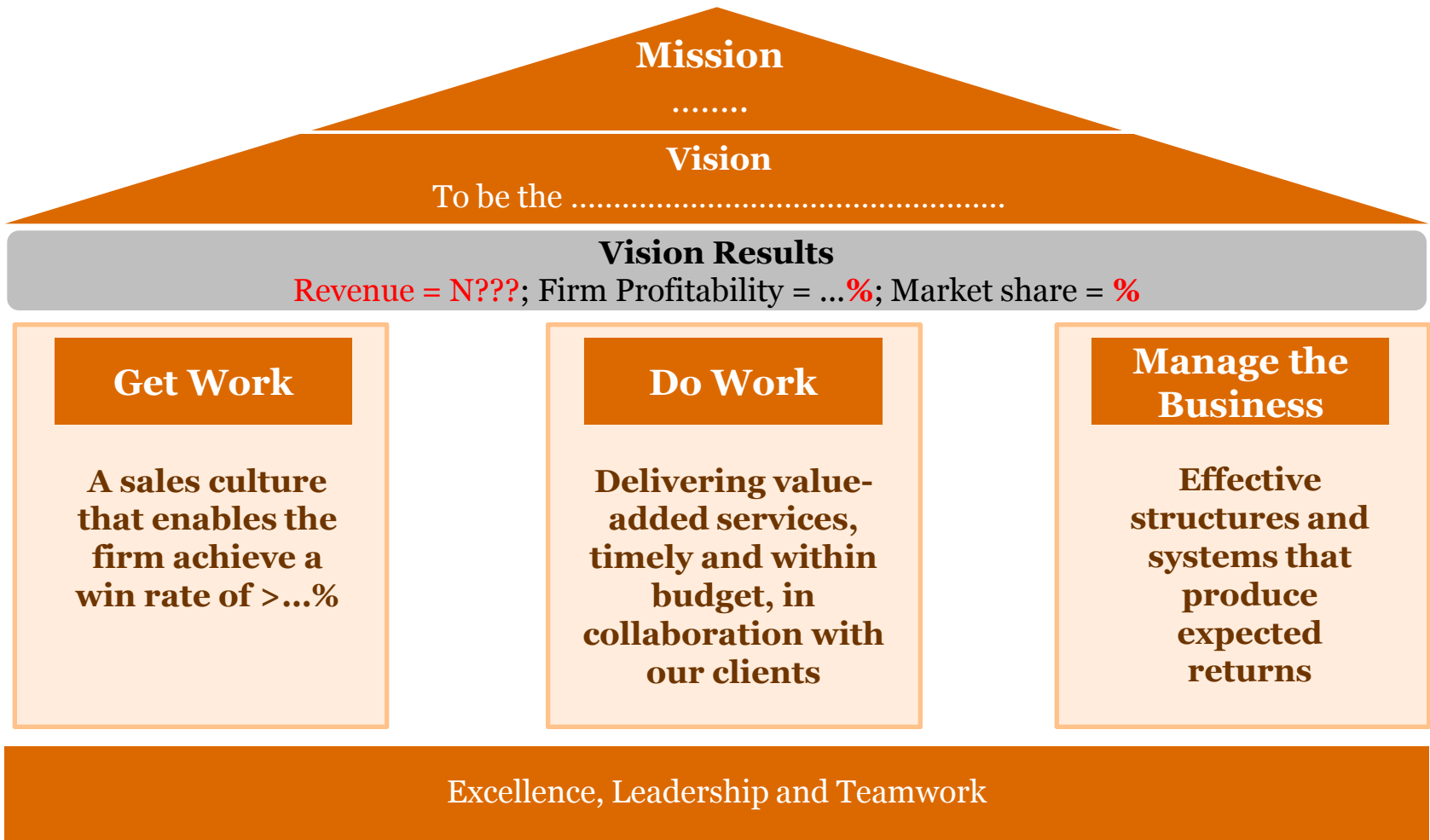
Slowly firms have begun to jettison the long-held lockstep method that rewarded Partners for their longevity of service and replaced it with more meritocratic assessments that allow the flexibility to offer high-achievers a higher share of the profit.

Global Trends in Legal practice Partnerships

- More mergers and acquisitions
 - With public sector cuts and fiscal belt-tightening in all sectors, firms are looking for long-term solutions to secure their place in the market – a merger offers obvious cost saving and cross-selling potentials. Mergers are also important for **practice expansion**, **tapping new markets** and **going global**.
- For example, In the last 15 years a small group of firms – including Bingham McCutchen, DLA Piper and Baker & Mackenzie– have been trailblazers for building international networks based on mergers. DLA Piper is the result of mergers between at least five major firms (two English, two American and one Australian), while Baker Mac has used small strategic mergers to enter new markets.
- The trend for mergers is expected to continue and even accelerate. According to a 2011 *The Law Society Gazette* research; 83% of top 11-25 law firms think a merger is likely in the next two or three years. That was up from 50% in 2009.
- This trend has also extended to Nigeria with notable local mergers in recent years and the ‘perceived’ dominant sole practitioners indeed having robust partnership arrangements

Performance management system

Performance Management System



Partner Performance Management

Culture of Accountability, Sales Culture

Culture of Accountability requires

1. Transparency [how will I be held accountable?]
2. Clarity & Specificity [of objectives, strategy, process and actions]
3. Dialogue and communications
4. Sharper Focus on Results

And engenders [should engender]

1. Teamwork
2. Trust
3. Effective communications
4. Effective Execution
5. Follow-through

Partner performance management

Annual partner income should be driven by three (3) components:

- | | |
|----------|---|
| 1 | Responsibility income.
Whether each partner is playing Client service/delivery role, business development and relationships, practice management – including staff mentoring and development, thought leadership etc.
This is usually between 60 -80% of ‘expected’ income available for distribution. The higher percentage considered for more junior partners i.e. putting less of the total expected income at risk. |
| 2 | Performance income.
How well has each partner performed against set expectation as determined by the agreed responsibility.
Essential that each partner has a duly agreed personal plan
This is usually between 10 -20% of ‘expected income. The lower percentage considered for more junior partners. |
| 3 | Equity income
Component based on partners relative contribution to the business over the years.
Also a reflection of capital contributed to the business
As with performance income, this is usually between 10-20%. |

A case for change

A case for change

- Building strong partnerships would enhance the value of legal practitioners
- Fierce competition from within and outside the profession.
- Need to build competencies and areas of expertise
- Increased scrutiny on the profession by regulatory authorities and other stakeholders
- Need for differentiation: Re-articulating and focusing on a sufficiently distinctive offering
- Follow the Accountants: Indeed the Institute of Chartered Accountants of Nigeria (ICAN) has developed a robust Guide to Practice which details how members can establish thriving practices based on partnerships.
- Other benefits:
 - Expected Economies of scale
 - Broadening the experience and skill base of the firm & service offered to the market
 - Cost saving arising from reduction in duplication of resources
 - Broadening of knowledge pool from which firm can draw internally
 - Larger pool of resources from which firm can pay out exiting partner

Matters for consideration

Matters for consideration

- Valuation of the firm should be conducted on a regular basis
- The equity contributions of each partner should be clearly determined
- Equity partners should be paid an agreed interest on the capital contributed
- New partners should be assisted to obtain facilities for equity contribution
- There should be a transparent partnership income scheme
- Proper financial reporting systems should be put in place.
- Partner annual plans aligned to the firms business objectives
- Policies that clearly show the career paths of practitioners should be put in place
- Separate 'private' business from firm's business.

Conclusion

- Partnerships continue to provide the most successful platform for profitable governance of professional service firms world over.
- A number of new models of partnerships are emerging in response to global trends and events which offers even more options for professionals who wish to go into partnership
- Regardless of the Partnerships model, it is important that all parties see the relationship as a business relationship which can only be successfully nurtured with trust, openness and shared commitment.
- The legal profession in Nigeria can benefit immensely as has the Accountants in forging robust partnerships which will assist them in expanding, tapping into new markets and creating jobs for new lawyers.
- Taking the next step may not be easy. ***If in doubt consult the Accountant in practice.***

Thank You

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