



Too Many Non-Equity Partners?

The number of non-equity partners in law firms has expanded dramatically over the past decade. In the US it has more than tripled in the largest firms and increases of a similar nature are apparent in other jurisdictions.

Originally, non-equity partnership was created to provide a transitional step to train, develop and prepare lawyers for equity partnership. The role was intended as an interim position providing the opportunity to hone business development skills and progress towards future ownership of the firm, while allowing the partnership additional time to assess an individual's potential.

Over time, the role and purpose of non-equity partners has altered; many firms have promoted lawyers to non-equity partner positions without full consideration of the lawyer's ability to progress to equity or to generate business for the firm. In some cases, firms intentionally adopted such an approach as a retention mechanism in a competitive talent market. In other cases, these promotions were more the result of weak performance management and an inability to make difficult decisions. Regardless of the intent, the result has been the creation of large groups of non-equity partners, often at a 1:1 ratio, or even greater, to equity partners.

In the current environment the capability to generate business has become a critical requirement for achieving equity partner status. Thus, those non-equity partners lacking this ability have become marooned in terms of career progress, becoming a static and, in many firms, growing group. They present a significant challenge to the management of firms.

Opportunity Costs

Non-equity partners absorb training and development opportunities which would otherwise be available to junior lawyers. Such opportunities come in a variety of forms – substantive work (e.g. learning through doing), client contact, volume of work, etc. The result is under-experienced and dissatisfied junior lawyers/associates.

Firm structures typically support between 1 to 4 lawyers to each equity partner. As the number of non-equity partners increases, the number of junior lawyer positions available to incoming associates/new talent reduces. This can have a significant impact on the firm's ability to recruit younger generations and bring in fresh blood. While some argue that a diamond model of leverage (a large experienced group in the middle) offers strategic advantages, evidence points to the fact that clients are often not willing to pay the consequential higher billing rates.

Declining Margins

Non-equity partners tend to expect and receive annual compensation increases as their experience grows. This results in highly paid senior lawyers who, while offering substantive expertise, lack the ability to generate client work/revenue. In some cases, these individuals function as highly paid associates, with a partner title. While most firms can profitably utilize a certain number of such lawyers, there is a limit on how many senior, non-business generating partners a firm's economics can support.

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Because such partners are not able to generate significant client relationships they often suffer from an inadequate workload. Clients are also questioning the value delivered at the relatively high rates charged for non-equity partners. As a consequence, over time they tend to achieve relatively low hours with equity partners inclined to direct work towards lower billing rate lawyers – both to benefit clients and to provide development opportunities to junior lawyers.

Overall as their compensation increases and increasing levels of work are diverted towards junior lawyers, the profitability of non-equity partners' declines.

Morale/Clarity in Partnership Track

The promotion of lawyers who are not likely to make equity partner to non-equity partner roles can create confusion among junior lawyers about the firm's promotion track. Junior lawyers mistakenly assume that they too can be promoted and achieve partnership without dedicating themselves to building client relationships or becoming business generators, as they observe these role models of apparent partnership success within the firm. This, in effect, undermines the perceived importance of becoming business developers.

In addition, firms find that their scope for promoting associates is increasingly limited due to the growing pool of non-equity partners. Morale is adversely affected and associates may depart as they observe fewer opportunities for advancement with non-progressing, non-equity partners creating a blockage.

Addressing the Challenges

For a small number of firms having a relatively significant number of non-equity partners is viable. There is a clear business rationale for such non-equity partners and their level of compensation is carefully aligned to their value to the business so that they continue to be profitable. Furthermore, their role is such that it does not compromise the career development of others. Typically, such partners may be overseeing particular practices that undertake certain types of work or managing the day-to-day relationships with established 'institutional' clients.

For many firms, however, this is not the case; the bloated ranks of non-equity partners, while offering a valued pool of expertise, restrict profit potential in the short term and, in the longer term, adversely impact on the development of younger lawyers and hence compromise a firm's on-going success.

This is not to say that all such firms must embrace the more traditional law firm 'up or out' model. New business models can be developed that leverage the strengths of experienced lawyers, perhaps in non-partner roles. The successful application of these models involves defining the specific purpose of these roles, having clients and practices where these structures can be successfully applied, understanding the strategic, financial and operational benefits and challenges, and differentiating the criteria and expectations of these roles from those on the equity partnership track. We see this as being one of the key challenges facing many law firms - with the more successful in the longer term being those that most effectively address this issue.

Meanwhile those firms that retain a more traditional model will need to adopt more rigorous and sophisticated approaches to career paths. Within such firms the lawyers being promoted to non-equity status will need to demonstrate the fundamental ability and potential to progress to equity status. By clearly defining the criteria for, and expectations of, non-equity partners and seeking to promote individuals who demonstrate the ability to achieve equity partnership, firms will avoid the serious challenges associated with non-progressing, non-equity partners.

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