

WITHOUT A STRATEGY, YOUR COMPENSATION SCHEME IS YOUR STRATEGIC PLAN

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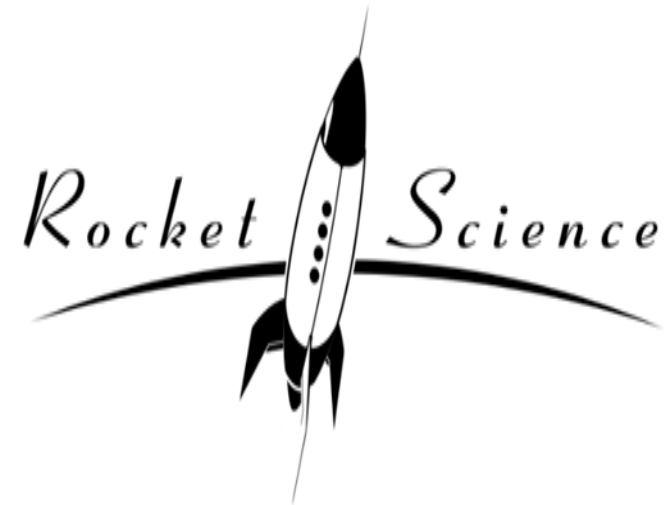
A dirt road winding through a forest with tall grasses and trees. The road is the central focus, leading the eye into the distance. The trees are mostly bare, suggesting autumn or winter. The lighting is soft and natural.

Genius is making complex ideas simple, not making simple ideas complex.

Albert Einstein

LEGAL DISCLAIMER

Steve



CHANGE IS A HAPPENING WITH OR WITHOUT YOUR PARTICIPATION

Some Hard Truths

- The advantage you have yesterday, will be replaced by the trends of tomorrow. You don't have to do anything wrong, as long as your competitors catch the wave and do it RIGHT, you can lose out and fail.
- To change and improve yourself is giving yourself a second chance. To be forced by others to change, is like being discarded.
- Those who refuse to learn and improve, will one day become redundant and not relevant to the industry. They will learn the lesson in a hard and expensive way (e.g. Minden Gross).

YOUR TWO REAL CHOICES



STRATEGIC ISSUE THINKING IS IN – STRATEGIC PLANNING IS OUT

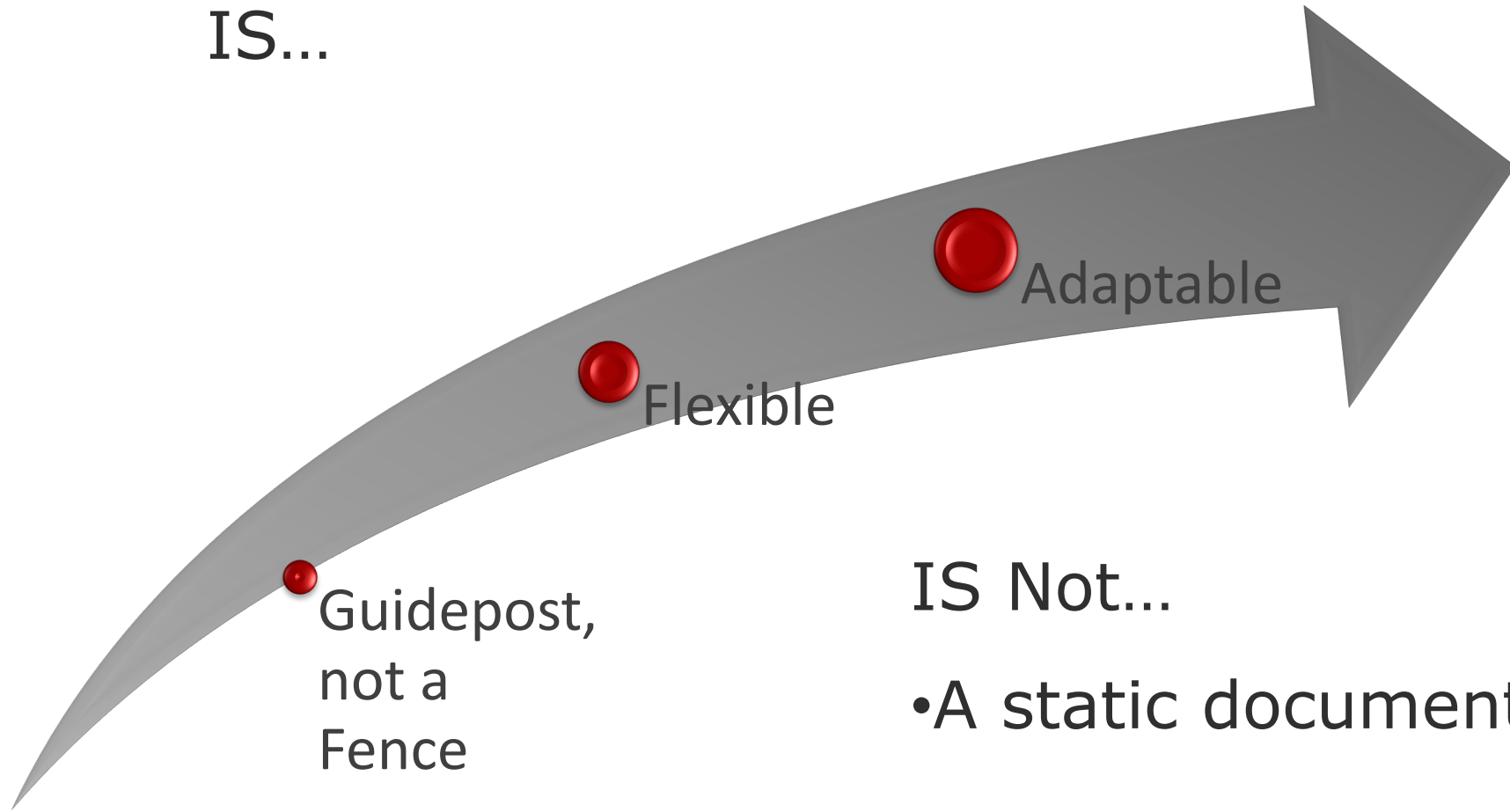
Dealing with Strategy Should Fit the Organization not Vice Versa



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WHAT STRATEGIC PLANNING IS AND IS NOT!

IS...



IS Not...

- A static document

NATURE OF STRATEGY DEVELOPMENT FIRMS SHOULD UNDERTAKE

Small plans typically involve shorter-term, more manageable goals that can be accomplished relatively quickly. They may involve everyday tasks, personal projects, or short-term objectives that contribute to a bigger picture. These plans are often SMART, more easily attainable and can provide a sense of immediate accomplishment.

<u>Specific</u>	<ul style="list-style-type: none">• Try and make your goal as precise and defined as possible
<u>Measurable</u>	<ul style="list-style-type: none">• Establish a criteria to measure your progress• How will you know when you are on your way?
<u>Accountable</u>	<ul style="list-style-type: none">• Determine a person who will help you and keep you responsible for your goals
<u>Reachable</u>	<ul style="list-style-type: none">• Set reachable goals that you will be able to attain (high expectations are good)• Set small goals toward bigger goals
<u>Time specific</u>	<ul style="list-style-type: none">• Create a timeline• Having an end time will help you stay accountable to your goals

TRADITIONAL STRATEGIC PLANNING (BIG PLANS) FOR LAW FIRMS IS DYING OR INEFFECTIVE FOR SEVERAL REASONS:

1. Rapid Changes - The legal landscape is evolving faster than ever due to technological advancements, regulatory shifts, and changing client demands. This pace of change means that long-term plans become obsolete before they can be fully implemented.

2. Emphasis on Agility - There is an increasingly high value given to the ability to pivot and adapt quickly. Traditional strategic planning can sometimes be rigid and slow to change.

3. Limiting Creativity and Innovation - Strategic planning is based on past data and experience, which can restrict firms from thinking outside of the box or innovating.

4. Illusion of Control - Strategies often give the illusion of having control over the future, which is unpredictable. This illusion can cause firms to overlook potential threats or opportunities.

5. One Size Doesn't Fit All - Traditional one-size-fits-all strategic plans may not work for every firm. Firms have unique needs, strengths, and weaknesses.

SO, WHAT TAKES IT PLACE?

*"Strategic planning is not strategic issue thinking. Indeed, strategic planning often spoils strategic issue thinking, **causing managers to confuse real vision with the manipulation of numbers**".*

- Henry Mintzberg

WHAT IS STRATEGIC ISSUE THINKING (“SIT”)?

We are big on using an iterative, flexible planning method that entails continuous learning and adjustment. This approach often involves setting shorter-term goals, constantly reviewing and revising plans, and adopting a more experimental mindset.

This forward vision includes anticipating changes in the legal landscape, shifts in client demands, or broader societal changes that could affect their services.

HIGHLIGHTS OF THOMSON REUTERS INSTITUTE 2024 STATE OF THE CANADIAN LAW FIRM MARKET

Released earlier this year, the report unlike the US and England does not get into specific numbers (sigh disappointment) but does deal with law firms and the market at a strategic level and confirms some long-held concerns and planning issues facing Canadian Firms, including:

- *"Firms recognize many of the challenges they face; however, they often are not planning or taking action to address these challenges."*
- *"Just as there was an evident disconnect between how Canadian law firms define success and what they measure, there is a similar incongruity between many of the problems law firms have identified and what they have chosen to prioritize for solutions."*

HIGHLIGHTS OF THOMSON REUTERS INSTITUTE 2024 STATE OF THE CANADIAN LAW FIRM MARKET

- *"However, there are significant gaps between awareness and action as evidenced by the relatively lower number of Canadian law firms that report measuring key metrics or having actually adopted plans to address key challenges."*

Remember in the absence of a shared strategy your compensation system is your strategy!

STARTING POINT – MAKE SURE THEY ARE SHARED

The vision statement - How or why we do it

Outlines the values that drive the organization or how it accomplishes its goals; some are succinct, while others include an expanded description. **But in all cases, it must possess an illuminating quality that allows firms to move quickly and precisely.**

The mission statement - What we do

Defines a firm's purpose and measures its success. Ideally, it is precise and concise and communicates the organization's strengths, differentiators, and desired goals.

NEXT STEPS

1. **Identify the issues** you see impacting your firm;
2. **Prioritize them** – at the firm level not the individual; and
3. **Set a schedule** of meeting dates to tackle each issue.

SIT SESSIONS MUST

SIT sessions should be inclusive, holistic, candid, and strategic. They should engage all key stakeholders and should:

- **Stick** to the priority **issue at hand**.
- **Focus on driving** the firm toward **its vision and mission**.
- **Proposed strategies** should be **SMART**.
- Incorporate a **communication plan**.

REMEMBER

“Basing your actions upon what other firms are doing is like running a race with no finish line.”

The right SIT outcomes must align with your compensation, values and culture. Anything else will lead to the “d's:

- Dysfunctionality
- Dissatisfaction
- Disengagement
- Dissolution

CURRENT EVENTS REINFORCES THE NEED

Everyone has a different spin on what lead to the collapse of Minden Gross but irrespective of your perspective the lessons are clear:

- Firms without a strategic direction have a higher probability of failure
- Firms that do not stick to their chosen strategic direction have a higher probability of failure

**GREAT COMPENSATION SYSTEMS
WILL DRIVE YOUR FIRM'S DESIRED
BEHAVIORS**



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TWO CHARACTERISTICS OF COMPENSATION SYSTEMS

While the degree will vary amongst compensation systems, there are two key types of criteria that the systems will evaluate:

- Subjective
- Objective

The chart serves to provide an overall sense of direction of changes being made to the compensation system and enables partners on a macro scale to think about the direction they would like to see the Firm's compensation system migrate / evolve towards.

Adjusting Compensation

Comparative Worth	Subjective with Formula Bonus	Combination Subjective / Objective
Lockstep or Equal Division with Subjective Merit Factors	Objective Tiers with Subjective Differentiation	Formula with Subjective Bonus
Lockstep or Equal Division	Lockstep or Equal Division with Statistical Adjustments	Formula

HISTORICAL COMPENSATION SYSTEMS

The experts, of which I am not one, while recognizing that firms will have slight variations generally lump law firm partner compensation systems into seven (7) types.

While not advocating for any particular one, it is important to at least consider the perceived strengths and weaknesses of each as part of any deliberations.

THE SEVEN COMPENSATION SYSTEMS ARE

- 1. Equal Partnership** - This system is typically used only by smaller firms. Basically, all partners share in profits equally or equally within defined groups of partners.
- 2. Lock-step System** - The lock-step system is used by a fair number of firms that are organized in a traditional fashion. The basic concept is that each partner is rewarded an ever-increasing share of the firm's profits, based solely on seniority.
- 3. Modified Hale and Dorr System** - Back in the 1940s, the Boston law firm Hale and Dorr created what is regarded as the first incentive-based compensation system. The firm created 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).

THE SEVEN COMPENSATION SYSTEMS – CONT'D

- 4. Simple Unit** - The simple unit formula is designed to reward seniority, production, client generation and non-billable activities, using a relatively straightforward and totally objective calculation.
- 5. 50/50 Subjective-Objective** – This system attempts to overcome the problems associated with systems that are too objective or too subjective. It recognizes that both types of criteria are valuable to the firm as a whole. The objective part of the scheme is that 40 percent of partner income is based on actual billings or receipts, while 10 percent of income is based on actual client generation statistics. The subjective portion of the system is based on the perception of all of the partners of two other criteria. Ten percent of the subjective portion is based on the perception of a partner's client handling abilities and 40 percent is based on the perception of all other criteria.

THE SEVEN COMPENSATION SYSTEMS – CONT'D

- 6. Team Building** - 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. It is diametrically opposite any form of an eat-what-you-kill system. 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.
- 7. Eat What You Kill** – This system solely rewards individual efforts, with no recognition for anything beyond personal production. One form of this type of system charges each partner a share of firm overhead, but each partner pays the salary of his or her secretary or assistant. Also, individual marketing, continuing education, personal technology and member- ships costs are the responsibility of the individual partner. The time of juniors is “purchased” from the firm at set rates but charged out to clients at whatever billing rate the partner thinks is appropriate

FOUR CRITICAL PARAMETERS

Before you get too deep into the discussion it is helpful to put all compensation systems for partners in context. The following are four critical parameters that many working with compensation systems, particularly those for law firm partners, have observed:

- 1. There is no magic system that will satisfy all partners, meet all strategic goals and never need to be changed.** All professional service firms must realize that a compensation system is a living and breathing beast. It will need to change or adjust to meet the demands of changing times—either to satisfy partner concerns or to complement and reward compliance with ever-changing firm goals.
- 2. A fair system can only be created when all those affected openly discuss the strengths and weaknesses of any proposed scheme.** This type of brainstorming session is the only way to get the issues out and dealt with in appropriately. Remember the old axiom - They saw the consultant like a seagull flying in from afar. It circled their heads and dropped something white in their hands. They thought it was a report. Only after the seagull had disappeared from sight did they discover what it really was – its true!

FOUR CRITICAL PARAMETERS – CONT'D

- 3. K.I.S.S. (Keep It Simple Stupid).** A compensation system that leaves most partners scratching their heads over the calculation of their individual compensation is doomed to fail. You may think it is straightforward, but be sure others agree with you.
- 4. A compensation system should be related to your firm's strategic goals.** For example, if you think that the mentoring of Associates is a worthwhile pursuit, then you had better have some form of reward for it in your compensation system or the message to your partners is that it is valueless and will only be done through their altruism and sense of teamwork.

A SIMPLE APPROACH WHETHER OVERHAULING OR TWEAKING YOUR COMPENSATION SYSTEM

It has been my experience that when many law firms begin a review of their approach to partners' compensation they tend to start with a system / approach that theoretically seems to fit their needs / desires and then try and squeeze their firm into the system.

This works for some but for many it just redirects the frustration / challenge they were experiencing that made them want to review their compensation approach in the first place.

COMPENSATION GAP ANALYSIS – TWO STEP PROCESS

Step One - Identify and prioritize the behaviors required to achieve your firm's strategic goals / directions. Again, there is little rocket science to identifying the types of behaviour that most plans require in order to have a chance of succeeding. The real challenge is achieving a weighted consensus as to their priority.

STEP ONE

The behaviors listed are not meant to be an exhaustive list but rather as a typical list. For greatest impact, firms should customize to their values and desired behaviors.

The behaviors are listed in no particular order and generally each partner ranks all listed behaviors as to importance e.g. scale of 1 – 10 with 1=Lowest Importance and 10=Highest Importance)

- Growing the business
- Legacy
- Firm mindedness
- Reputational excellence
- Delegation of work
- Client service
- Leadership
- Management
- Respect
- Integrity
- Teamwork
- Compassion
- Trust
- Professional growth
- Community involvement
- Innovation
- Training

COMPENSATION GAP ANALYSIS – TWO STEP PROCESS

Step Two - In this step we take the behaviors identified in **Step One** and determine where, if any place there is a gap between the desired behaviour and those driven by the current compensation system.

A word of caution when approaching this part of the exercise. It is not sufficed to say that the compensation system drives (rewards) the behavior. The partners need to be able to articulate how it drives (rewards) the desired behavior. Remember if it is not transparent to the partners the odds of it even having the desired result are reduced.

STEP TWO

Behaviours That Should Be Supported / Driven by the Firm's Compensation System	Which of these Behaviours the Current Compensation System Supports / Drives	How (specifically) Does It Support / Drive the Desired Behaviour?	Importance designated by Partners
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The fourth column not only identifies the "No" answers from the second column but also indicates the weighted priority that the partners have assigned to that behaviour from Step One.

Obviously if the behaviors in the fourth column are all "8s", "9s" or "10s" (Step One a 10 is of highest importance) then, a wholesale change out of the system is likely necessary.

However, if there are a number of "1s", "2s" and "3s" in this column the likelihood of successfully achieving the firm's strategic goals / direction are doable without wholesale changes to the firm's compensation system being implemented.

REALITY

These gaps, combined with the notoriously poor track record of execution in many law firms, will increase the risk of failure to unacceptable levels. Remedial action on the part of the firm's leadership in general and the partners specifically is imperative.

Is your compensation system worth following?

REAL MESSAGE – REALLY SIMPLE

The law firms that will survive and thrive will have courage. Courage to:

- Have challenging discussions with the Partners and others;
- Make tough decisions after having had discussions with the appropriate parties;
- Execute the decisions made.

WHO IS STEPHEN MABEY?

Stephen Mabey is a CPA, CA, and the Managing Director of Applied Strategies, Inc. His credentials include:

- Fellow of the College of Law Practice Management (one of 19 Canadians – 276 Fellows);
- Author of *Leading and Managing a Sustainable Law Firm: Tactics and Strategies for a Rapidly Changing Profession and Key Performance Indicators: An Introductory Guide* (Amazon);
- More than 25 years in a senior management role with Stewart McKelvey, a 220 lawyer, six offices Atlantic Canadian law firm;
- He has been advising law firms for over 15 years on a wide range of issues, including - strategic action planning, leadership, understudy (succession) planning, compensation - both Partner and Associate, organizational structures and partnership arrangements, business development, capitalization of partnerships, partnership agreements, lawyer & staff engagement, marketing, key performance indicators, competitive intelligence, finance, mergers, and practice transitioning.
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