Partner Compensation: What Is The Right Way To Approach A Difficult And Sensitive Subject?

Partner compensation is one of those subjects most firms don’t discuss openly, at least not until there is a problem. It can be a challenge coming to terms with compensation because there is no one-size-fits-all approach. What works for one firm may not work for another. But as attracting accountants gets more difficult and landing new business can mean the difference between survival and closing your doors, partners are asking hard questions and experimenting with new approaches. To get the latest in partner compensation strategies, IPA spoke to August Aquila, a consultant in CPA firm management. Aquila co-wrote a best-selling book, Compensation as a Strategic Asset: The New Paradigm with Coral Rice.

Q: What do you mean when you refer to compensation as a “strategic asset?” There are two levels. First, a firm’s compensation plan is an asset and can be used as a retention and recruiting tool. When firms have a good system, they can use it to attract and retain the right employees. If a firm has a great brand name or reputation, that’s also an intangible asset, they can use to attract employees.

Second, a firm’s compensation system should help drive the strategic direction and vision of the firm. It should reward behavior that will drive it toward achieving its goals. For example, a firm has a strategic goal of getting closer to its clients and developing much deeper client relationships. If the compensation system does not reward that type of activity, which can frequently pay off in the longer term, partners and staff won’t do the activities they need to deepen those relationships. They might not spend non-billable time with clients trying to understand client needs.

Q: We’ve heard consultants say, “If you have twenty partners, you should have twenty different compensation formulas.” What’s your view? There is really no one, right plan. You need to create a plan that is reflective of the firm’s culture and values. If a firm is very growth-oriented, a good part of the compensation system may be based on new business development. Partners who bring in more new business may be paid more. A compensation system should reward for character and performance. You want someone of a high character, obviously, and you want someone who is a high performer. If you look at a firm, there are A, B and C players. Maybe 15% are the stars (the As), another 15% are C players, but the majority is made up of B players, so you don’t want to put all your emphasis on A and C players.
ignore B, because B players are the glue that holds the firm together. They are the ones there, day in and day out, doing the work with the clients. A compensation program needs to ask, “How do we reward these B players fairly?”

**Q: What are the hallmark characteristics of a firm whose compensation system needs an overhaul?** There are several. Normally you see a lot of partner dissatisfaction with compensation. Partners will also feel the current compensation system is not fair. I’ve seen some firms where the majority of the compensation would be determined on equity or ownership of the firm. Say two partners in a six-partner firm owned 60% – or 30% each. And the other four, junior partners owned 40% – or 10% each. If you distribute income based on equity, two partners get three times as much as junior partners. If a junior partner brings in a new engagement, he/she only gets 10 cents on the dollar. That’s not much incentive for younger staff to bring in business. Too much focus on entitlement and not enough focus on performance breeds dissatisfaction and can lead to attrition.

**Q: What are the biggest challenges a firm leader will face when approaching the subject of changing the compensation system?** The biggest challenge is no one wants to give up what they are currently making. Compensation becomes a very emotional issue. You have to show people that under a new system the compensation pie can actually grow. Partners are going to say, “What is going to happen to my compensation? If it is going to go down, I am not going to be happy.” Leaders need to educate the partner group on how, as a group, they can make more. They need to get each partner doing what they do best. It also helps to create a philosophy of abundance rather than scarcity. If one partner makes more, it doesn’t necessarily mean another makes less.

**Times are changing.** In *Compensation as a Strategic Asset: The New Paradigm*, we outline a new compensation paradigm. With the old system, there was more of a guarantee of compensation with little risk. In the new system, much more is at risk. Compensation in general is going from an entitlement system to a performance system. A lot of the old systems that were formula-based relied heavily on production and generating dollars for today. The newer systems are rewarding people not only for current production but also for building future capacity in the firm. For example, developing a new service area may not pay off today but it has the potential to pay off tomorrow.

**Q: What are the most practical “first steps” a firm should take when it wants to review its compensation system?** Here are some things you should ask about the current system: *Is it fair? Is it fairly applied? Do the partners understand how it works? Does it create a one-firm concept or a silo concept? (A team approach versus an individual approach.) Is it tied to the firm’s strategic goals? Is there an element of subjectivity to reward for exceptional behavior? Does it encourage partners to live the firm’s values?*

When you employ basic pay-for-performance principles and apply them to accounting firms, those firms perform at a higher level. It keeps the A’s and B’s because it rewards those who perform better. Not everyone gets the same type of raise, which gives you a lower annual increase but for those who perform, they can actually make more under the new system while under-performers make less.
Q: *Any other thoughts or success stories?* We have seen evidence that firms can significantly increase net income per owner when the owners and employees are aligned with the strategic plan. People in each department know exactly what they are doing and how it fits into the larger, overall goals of the firm. Firms may start pay-for-performance at the partner level but eventually they will push it to staff level. You can’t go in and totally change the compensation system (at one time). It evolves. One option is to run the new and old systems together for one year to show people how they would have done on the new system (versus the old).

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