Partner Retirement – The Elephant in the Room

by

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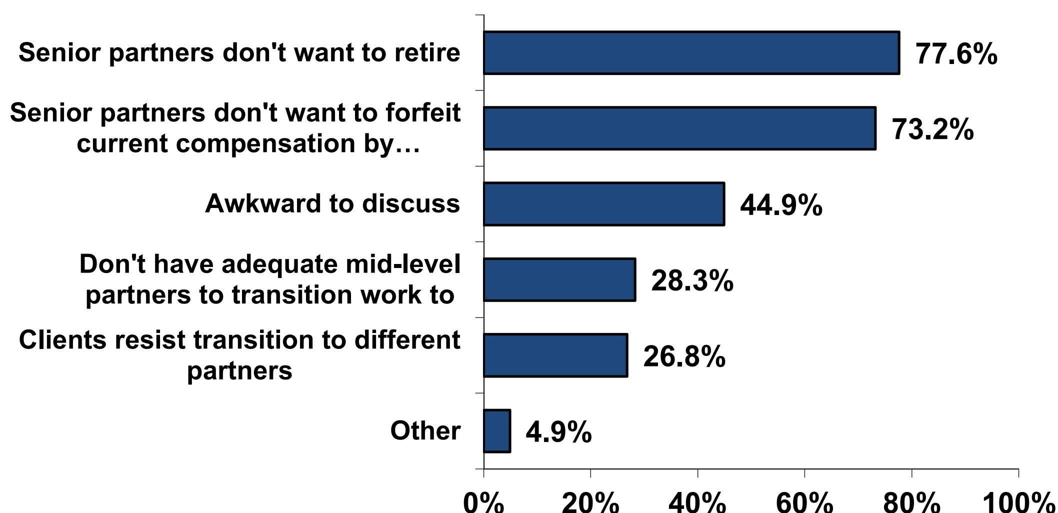
UK research in 2015 for a Jomati Report – *The Paradox of Partner Retirement* – showed that many law firms and their partners found it extremely difficult to have open and constructive discussions about a partner's retirement plans. The partners often had not thought deeply about the alternatives available to them and the law firm leadership, often inadvertently, gave the impression that the conversation was about how soon the partner would leave or at least take a smaller piece of the firm's profit. Indeed, some partners were so keen to avoid such a potentially difficult conversation that they moved to another firm, in many cases, years before they would have been expected to leave their current firm.

This lose-lose situation clearly helps no-one (expect perhaps recruiters). While some best practice is now beginning to emerge it is clear that there is ample room for improvement.

In the US, although partners tend to retire far later than in major UK based firms, similar issues appear to arise. Altman Weil's *2013 Law Firms in Transition Survey* showed the following stumbling blocks when trying to address the issue.



A review of partner photographs on many firms' websites may give the impression that lawyers have discovered the secret of eternal youth, but the reality is at some stage partners will want to start to ease up or retire. Most firms do not have a formal system of succession planning and hope that when the time comes the roles and responsibilities of the departing partner can be passed to others. The assumption that a very short handover of a key client relationship will be sufficient is a risky proposition and can alienate otherwise loyal clients.

Inevitably partner remuneration plays a key role in both sides failing to address the issue. The partner does not want his or her remuneration reduced during any transition period and the management does not want the partner to move to another firm. But, it is unlikely that this standoff will help the partner, the firm or the clients. The use of client teams especially for larger clients, rather than a sole client partner may help to mitigate the client risk and provide some continuity but the effective use of such teams is, at best, mixed.

As the "Boomer" generation enter their 60s and 70s this issue has become more acute. As a result of the recession and its negative impact on partner profits and partner promotion, we are already advising a number of firms encountering increasingly serious succession related issues. Indeed, many of the recent law firm mergers involving smaller firms were driven, at least in part, due to the succession issues the smaller firm faced.

The manner in which firms address retirement issues will vary. Some have a mandatory retirement age, often 65 or 70. Others have no formal retirement age, a position endorsed by the American Bar Association. While some firms encourage partners over a certain age to move from the equity into another status. A key issue in many firms is the, often unfunded, benefits payable to retired partners. In an era of low growth and low interest rates the actuarial cost of these can be massive (and often the ultimate poison pill in law firm merger discussions). At least if a partner works until he or she drops that liability is at least mitigated (subject to any spouse benefits).

There is not a one size fits all answer for law firms or each partner. A level of pragmatism and flexibility will be necessary together with a level of realism as to the continued ability of the partners to perform at the level they used to.

But rather than do nothing a firm's management needs first to understand the following:

1. The age profile of the partnership as a whole and in individual practices and offices. This is not just to identify those potentially approaching retirement, but also to show any gaps in the age and experience range of the partners. In particular, are there partners able and willing and with the necessary capacity to credibly assume the work and client relationships of partners retiring over the next few years? Indeed, the younger partners will not only need to transition existing client relationships but to build new ones if the firm is to have a sustainable future.

2. The extent of the firm's unfunded pension liabilities to partners (and staff), how they could be funded, at what cost to current compensation and what changes may be appropriate. These are difficult and emotional issues, outside the scope of this article,

and whether addressed or not will increasingly cause significant intergenerational tensions. Firms may think that they have solved the issue by placing a cap on the percentage of the firm's profits that can be paid out to retired partners. The acceptance of this tax on current compensation by younger partners has declined over the past two and one-half decades – yesterday's acceptable cap is now too high. Accordingly, this may cause partner's expectations as to their retirement income to be significantly reduced thereby impacting their own financial planning.

3. Is our partner age base aligned with our client age base? Although perfect alignment may not be necessary or desirable, relationships are likely to be deeper with people who consider themselves peers. As *The American Lawyer* reported in September 2015, over 30% of NASDAQ listed GCs were Generation X and almost 20% of Fortune 100 GCs were Generation X. So does the firm have the right levels of contact (whether at partner level or otherwise) across the client?

Armed with this data the management will at least be aware of the extent of the issue they face. But then they need a clear and coherent plan to address the issues. This may be difficult, but ignoring these issues can be terminal for the firm.

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