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Compensation Hikes: Free Money or Lack of Freedom?

Considering the landscape of news, gossip, and reviews that has influenced the world of associates and partners in 2006-2007, one thing remains certain: the ongoing salary war undertaken by law firms throughout the U.S. has changed the playing field (and future) of attorneys in this country. Perhaps more so, it has ushered in changes in business models and visions for a number of area law firms.

On a regular basis lately, I am confronted with phone calls from attorneys looking to laterally move for *one* reason only: more money. This would not be surprising to me if it weren't for the fact that these attorneys are currently employed by firms where they are happy, fulfilled, and on clean tracks to partnership (if not already there).

Fielding calls from practitioners who are happy but are incentivized to move solely for the cash has been a source of confusion for me. At the very least, many of these attorneys are looking at short-term gains. At the very most, they are asking me to assist them with changing their lives—literally changing their very existences—without asking me about the downside of the compensation wars.

In fact, it is safe to say that 85% of the attorneys who solicit my help for lateral moves which have been prompted "solely because of the salary war" fail to inquire about the fallout from this war. And there is always fallout from battle.

At first blush, one can confirm that the compensation hikes over the past two years (and rumors attendant to more hikes at the end of 2007) are a natural result of a strong market during 2006 and early 2007. In New York City, such hikes are also the expected result of investment banks and, more so, hedge funds stealing away top talent at the big firms by offering them notions of more dynamic work and lucrative pay increases ($300,000 to the mid-$400,000s), as well as bonuses, travel, and the kind of excitement one can only find at the O.K. Corral.

Law firms see this, and while they cannot change their environments to be more cowboy-like, they can change their pay structures as an incentive to encourage associates to stay. Thus, compensation hikes aren't a surprise; we can usually plan on their arrival if we watch the market.

What we often cannot plan on, however, is the actual dollar figure of the bump-up. The "magic number" for first years used to be $160,000; however, rumors abound that, by December 2007, $180,000 will be the new first-year benchmark. We also cannot plan on the dark side of such pay hikes, which, I have come to find, nobody seems to want to think about.

More Than Meets the Eye

In April of 2006, *The Wall Street Journal* featured an article by Cameron Stracher ("Rule of Law") entitled "Cut My Salary, Please!" Presenting a very realistic look at what happens to associates and partners when base compensation is on the rise, Mr. Stracher noted a number of doomsday residuals: an increase in billable minimums; increased difficulty hitting the hours figure attendant to end-of-year bonuses; a dramatic loss of a personal life; and over-handed lawyering, to name a few.

Mr. Stracher was entirely correct when he noted in summary that "[a]s long as there are law firms willing to pay them to have no lives, [associates] will take the money." Moving beyond *The Wall Street Journal*'s predictions, however, are a host of outcomes which affect not only associates but also partners and the very souls of law firms themselves.

As a legal recruiter, I sit at the center of a voyeuristic world where associates, partners, and law firms come to play, share secrets, make choices, and change the face of law. To that end, one thing I have seen most clearly over the course of 2006-2007 is law firms struggling to redefine their own images in light of these salary wars. Where once a mid-sized New York firm—or top-ranked New Jersey firm—felt at the top of its game, inching slowly toward the upper echelon, it now must come to terms with the fact that its partnership can't afford (or doesn't want to afford) to play with the big boys. As such, we see a host of firms undertaking image overhauls.

We see firms redefining themselves as "comfortably mid-sized" and "seeking practitioners who want a work/life balance" and not a 24/7 regime.1 Is this how they truly feel? Probably not. However, this is what they can afford. It's somewhat akin to quarterback Frank Reich realizing he will never be Jim Kelly (sorry—I'm a Buffalo Bills fan). That's not necessarily a bad thing, mind you. Frank Reich played a vital role in the Bills' football history. It simply was a coming to terms of a sort.

Likewise, a shift of sorts is occurring with national law firms where the lines of demarcation between "big firm" and "not" are growing thicker and more defined. For some associates, this can be a disturbing realization—namely, that their firm may never become a "big firm," and perhaps they made the wrong choice when accepting their post-law school offers. For partners, this can be a disturbing realization because, very often, splits are becoming more evident along partnership lines—with one side wanting to give up more of their pot to associates in order to stay in the race and one side wanting to stop the money bleed and keep their resources in their own wallets.

In short, fractures are occurring in area mid-sized firms' business models, requiring a decision to be made to either crack open the model and re-create or plaster over the fracture and carry on as planned.

Big Law is also redefining its business models in a way that has to do with hiring and tolerance. On the hiring side, firms are expecting more for their money. If they are looking for a second year at $170,000, they truly want a second year...with the knowledge base of a third year. They want a first year...with the knowledge base of a second year. Similarly, ever mindful of how costly senior associates are right now, if a mid- or senior-level is sought, they frequently are asking some candidates to take a step back in class, depending on their knowledge base, so they "fit better into their new firm environment and are better situated for partnership in line with their class." While a true motivation, one can't help but wonder if the salary wars (and high cost of a mid-level/senior associate) are also causing this class-year pushback for some firms.

In keeping with the above, we are seeing a number of big firms requiring that their associates get up to speed a lot more quickly. No more hiding in the back office or floating along unnoticed. These increased hiring demands and this lower tolerance for slackers are direct results of the salary hikes. In addition, we have seen a number of big firms this year de-equitizing their partners or eliminating partners altogether, which many feel is a partial result of the salary war.2

Aside from image overhauls, changes in structure, and internal discourse (for some firms), there are those who predict that the high salaries of 2007 are going to encourage associate layoffs in 2008. As we all know, market watchers predict a serious economic downturn. Could the effects of an economic downturn, including thousands of layoffs in the subprime lending market, encourage Big Law to lay off associates?

A number of authorities expect to see layoffs in real estate and corporate finance but a corresponding upswing in bankruptcy and litigation to buffer the blow. Still, the rumors persist, and with the world watching to see whether Big Law jumps up to $180,000 in December 2007 for first-year salaries, these rumors, according to some, seem more and more likely to become fact.

One thing in particular to remember for New York lawyers is that New York firms are deeply entrenched in the financial markets. As a result, New York is very often the stage upon which market drama is realized. According to the *New York Lawyer*, "In past economic cycles in which layoffs were seen, it was the more leveraged firms with higher salaries that had to face layoffs."3

Having said this, only time will tell. It is hopefully more likely that New York firms and other Big Law firms have only agreed to join the salary war where they have adequately diversified their practices to bolster against economic downswings. In sum, it is important when considering a lateral move *solely* for money to be aware of the above residuals and predictions, otherwise known as side-cast shrapnel.

Moreover, looking forward, what can we truly expect in the final months of 2007? The final calendar quarter is traditionally seasoned by bonus news. Of course, with associate salary increases, we can expect to see slower growth in firm profits.

What effect will that have on our expectations for higher bonuses in keeping with higher salaries? Can firms possibly keep up? Well, the race has begun. September 2007 saw Sullivan & Cromwell's bonus memorandum entitled "Senior Associate Supplemental Compensation Plan" giving senior associates "incremental compensation" (in addition to base pay and bonus). When split across the board, this incremental compensation likely will not be a huge chunk, but it certainly is something.

What it may be more than anything, however, is the toe in the pond that starts the ripple to wrap up 2007. With Sullivan stepping out into the murky bonus waters, who is next?

A Reasoned Approach to More Money

The moral of this article? Nothing in this life is free—even free money. What associates and partners need to remember is that for every upside there is a downside. If you are looking to make a move prompted *solely* by more money, that is fine. However, you should know all sides of that reality and make an informed decision. If you are happy where you are, don't underestimate the value of that truth.

It's an exciting time to be an attorney, and your career moves should be prompted by (i) hard-core knowledge of your goals for the future; (ii) a realistic assessment of your current career standing at your firm; and (iii) a well-thought-out exploration of the highs and lows of the salary war. Hence, when you ring me to tell me that you wish to make a move for money, please also tell me that you've read at least some of the above-referenced articles and, as such, consider yourself a well-informed soldier in the battle for higher pay.

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[1] Atlanta-based labor and employment boutique Ford & Harrison, for example, has redefined itself by doing away with billable-hour requirements for first-year associates. Using the medical-school approach of residencies as a model, according to the *National Law Journal* (August 20, 2007), the firm is apparently hoping that first-year associates will learn more by watching (without worrying about billable hours), thereby enabling them to handle juicier issues earlier in their career trajectory. One could venture a guess that Ford & Harrison's change in business model was prompted by more than just altruistic goals. The firm is distinguishing itself from its often better-paying and larger competition with the hope that such changes will appease clients and encourage associates to stay. Likewise, Fox Rothschild recently announced that it would not raise first-year associate salaries, a move possibly prompted by subtle shifts in its business model and a desire to assuage a possible market downturn.

[2] Mayer Brown was at the forefront of such partner de-equitizing in spring 2007, when it set back a number of partners from its Chicago office, with these partners learning of their fate from the *Chicago Tribune*. Mayer Brown's goal relative to the de-equitization was said to be a desire to make it more competitive. Of course, while it is possible that the firm's actions were simply a natural weeding out, it certainly was not saved in the press and chat rooms, which believed the de-equitizations to be, more likely, a fallout from the salary war. As quoted in Chicago's Larry Bodine's *Law Marketing Blog*: "If there is one partner for every associate, management will thin the partner ranks. They won't fire those $160,000 associates, because they're money-making machines." Keep in mind, however, that Mayer Brown should not be held out alone. Whether publicized in the papers or undertaken more discreetly, shifts in partnerships (post salary-hike announcements) are regularly occurring, to the dismay of many senior practitioners.

[3] Quoting Fox Rothschild partner Mark Silow in "Are Associate Layoffs on the Horizon? Credit Crunch Could Trigger Cutbacks in Some Practices." *New York Lawyer*. August 27, 2007. http://www.nylawyer.com/.