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The flaw in the partner model: Partners

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Allan Koltin was listening recently to a Top 100 Firm's board discussing whether to sell to a private equity firm — and they were hopelessly divided.

"Two or three want to do it. They're upset they haven't done it already," recalled Koltin, the CEO of Koltin Consulting Group and a leading advisor on M&A, firm structure, and more to firms across the country. "For two or three, it's beyond their grade. They just don't understand change; they just want to go and back to do billable work. And two or three think it's the coming of the next plague, and you're selling out your people."

Koltin's concern wasn't whether the firm would bring in PE, however; his concern was whether the firm would be able to make a choice at all, given the restrictions of the partnership model.

"So as long as these models continue to exist, firms won't be able to make the tough decisions they need to make," he said. "They're in essence crippled strategically in what they do."

The partnership model is both an ownership structure and a management/governance structure, where the owners are also the managers, responsible for decisions on both day-to-day operations and long-term strategic direction. For smaller firms, that generally presents no problems — but as firms grow, the dilution of authority and responsibility can be a serious impediment.

(Firms are exploring a wide range of ownership and management models these days; see our feature story *for more, and our* glossary of the many options *available.)*

David Wurtzbacher, the founder and CEO of Ascend, a PE-backed platform that acquires independent, entrepreneurial CPA firms, recalled a lesson he learned from firm management expert Gary Shamis: Growing firms hit a rough patch between $20 million and $40 million revenue where the limitations of the partnership begin to cause serious problems.

"One of the reasons he says it's difficult is that up to $20 million of revenue, your partner group is pretty small," Wurtzbacher recalled. "So it's pretty easy to get around a table quickly and make decisions and you kind of move on. $40 million is totally different. Now, you're talking about 20 partners or maybe more. You can't do consensus-based decision-making anymore. And so it forces governance change. And some firms never make it out of that because they just can't convince the partners to move to closed compensation. They can't convince the partners to move to a corporate model. And so they just get stuck."

"That governance is one of the most important issues in the industry right now because good governance allows for good decision-making at speed, and the world is just moving fast right now in a lot of different ways," he continued. "And if you're not built for speed, I think competing in this industry in the future will be difficult."

Too many partners can be a recipe for paralysis, agreed Phil Whitman, CEO and president of Whitman Transition Advisors, who regularly works with firms on ownership and succession plans: "For the smaller firm that is still, 'All right, we got eight partners and every partner has a seat at the table and is involved in every decision that the firm.' I would say to them, 'A committee at 20 will deliberate plenty; a committee of 10 does things now and then, and a committee of one gets things done.' It's time for you guys to let one guy be the managing partner; have an executive committee and not have all your partners involved in everything."

Too many cooks

Just as major strategic decision-making shouldn't be held hostage by an overly consensus-driven model, at some size, a firm's daily operations need a new form of governance.

"Firms get to a certain size and we encourage them to form an executive committee and begin to have the executive committee handle more strategic and sensitive matters than the partner group, and then empower that CEO or managing partner or whatever title you want to give that person to be the manager of the partners," explained said Jennifer Wilson, partner and co-founder of consulting firm ConvergenceCoaching. "And in a large firm you can't have one manager of all the partners, so then you empower service line leaders to manage partners and you begin to have a true corporate structure."

That corporate structure enables firms to ensure uniform standards and procedures both within and across all practice lines, and to hold individual partners accountable for both their established goals and for the responsibilities in carrying out the strategic and tactical goals set by the MP or executive group.

Wilson doesn't wait for that $20 million threshold to start implementing that kind of governance, either.

"When we're consulting with firms from $7 to $10 million, we make sure that they have a managing partner with a clear written position description, measures of success, accountabilities and empowerment definition," she said. "At that stage, you need to start having accountabilities in place; by $7 to $10 million, you have to have people running service lines, even if it's part time, and be clear who's accountable to them and how they're going to manage quality and consistency -- just in the service delivery process, you have to have people start saying, 'Hey, here's how we do it at this place.'"

She continued, "There's a course to organize as you grow so that you just keep sort of elevating smaller groups of leaders to run the thing, instead of the traditional partner model, where all partners run everything, which means hardly anything's being managed because they're very busy serving clients, and running engagements and teams."

Setting up leadership and management structures — and then identifying who among the partner group is suited to run them – is critical to firms' ability to grow, which is one reason more and more are doing just that.

"I think traditional shops are realizing, 'Hey, maybe we're really not that great at running this business,'" said Kristen Rampe, managing partner of consulting firm Rosenberg Associates. "There's many of them that are just actually really good at accounting, either technically or client service, … but the ability to have strategic and organizational vision and leadership and hold other people accountable -- that's a different skill set that comes from a different bag of tricks, and I don't believe that all people who when they were 18 and decided to major in accounting came by that naturally. … I think firms are realizing there are other ways to run a business and that, in fact, it can be really murky and awful to have people who aren't really great at running a business running a business together."

None of this, experts were quick to say, is to suggest the partnership model can or should disappear. For small firms, it actually has many advantages, and even for very large firms it can still work — provided certain adjustments are made.

"It's not to say the partnership model is bad," Koltin said. "It's just finding that there's other models out there that might be better."=