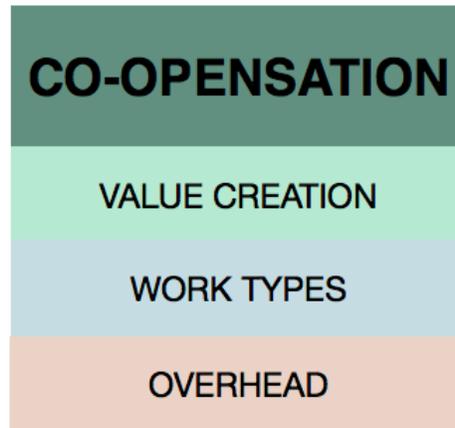
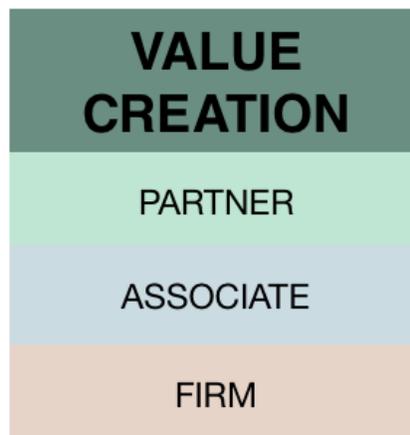


Coopensation 1.0

Worker-Owned Incentive System



Fairness is expensive. That is to say the more fair you want to be, the more expensive your fairness system will be to implement. At one extreme the easy and most simple implementation of fairness is **'keep what you kill'**. This allows a firm to start working quickly but does not give incentives for contributing to marketing for the brand. At the other extreme, there are **point systems** that give rewards for skill, effort, and long term brand building exercises like marketing. Somewhere in the middle are the traditional systems of hierarchy, where people at the top of the organization decide what the member bonuses for the lower part of the organization will be. In this paper we explore the most fair¹ system type, in terms of merit and overall long term contribution, being used in consultancies.



¹ As discussed in 'On Fairness': <https://s3-us-west-2.amazonaws.com/vulk-blog/OnFairness.pdf>

Economic Value of Individual Partners

The **market value of a partner²** is the value a partner would receive on the open market. At first glance it seems that an individual's market value would be hard or impossible to gauge. While not impossible, a calculation for giving a fair idea of partner market value is complex. This calculation is biased towards work performed and does not account for seniority in any way (other than the fact that clients might pay more for senior experience). This calculation of value **can be used in compensation schemes in order to incentivise behaviors such as brand building and management.**

The **economic value of a partner is a non-trivial calculation and carries with it the burden of maintaining records** of types of hours spent by each partner. General knowledge of the calculation requires familiarity with the seven components of value documented here.

Partners

Partners are the legal owners of the firm. They each have influence, established by law, on the direction of the firm.

Partner Responsible Hours

Every project requires some amount of soft skills in order to acquire the project, whether individual partner name recognition or the application of sales skills. The partner responsible hours show how much a partner is responsible for during the acquiring, managing and billing of a project from a client. **One half of partner responsible hours comes from the hours billed for account management and acquiring the project. The other half comes from origination.**

Origination

Origination is the **percentage of the total revenue from a project that is given to the partner responsible for obtaining that project.** This percentage of revenue is

² "Years of consideration of this issue have led Altman Weil to the conclusion that the fundamental formula is: $P = Ma(Cr - Cw) + Rp(Cw + Vf) - O$ where: P = Individual partner's economic value Ma = Margin on associates Cr = Responsible-[partner] credits of the individual partner Cw = Working-[partner] credits of the individual partner Rp = Firmwide realization on partner revenues Vf = Value of individual partner time expended in firm-authorized efforts at standard rates O = Per-[partner] overhead", Cotterman, James D. Compensation Plans for Law Firms. Chicago, IL: American Bar Association, Law Practice Management Division, 2015. 50. Print.

credited to the partner regardless of whether he or she works on the project or not. It is also ½ of the value of partner responsible hours.

Partner Working Hours

The **hours a partner directly bills to a client are called partner working hours**. The actual number is calculated using the amount the firm actually collects from the client and not merely the amount billed.

Associates

What is an associate?

An **associate is any non-partner used for billable work on projects**. Associates are by their very nature more ephemeral and tend to align more with the short term goals instead of the long term goals of the firm. Contractors should be treated as associates and calculated as such within this model. The wise **use of associates is a skill that is also rewarded within this compensation model**.

Margin on Associates

The **margin on associates³ is the profit made during the use of those associates on billed work**. This margin is calculated on the amount the firm actually collects and not merely the amount billed.

Firm Hours

When **the firm as a group approves certain types of marketing and management hours** as worthy of some compensation, those hours are called Partner Firm Hours. The value of these hours are the most difficult to comprehend and are **based off of opportunity costs realized by the firm**.

³ "Margin on Associates (Ma) refers to profit on work done by associates, calculated on a cash receipts basis ... $Ma = \frac{[\text{Sum}] Cwa - Sa (Oa * A)}{[\text{Sum}] Cwa}$ where: [Sum] Cwa = Aggregate associate working credits Sa = Associate salaries and benefits Oa = Per-associate overhead A = Number of associates", Cotterman, James D. Compensation Plans for Law Firms. Chicago, IL: American Bar Association, Law Practice Management Division, 2015. 50. Print.



Firm-Wide Realization

Firm-wide realization⁴ is the value the firm has realized from marketing and management functions. **This value takes into account billable hours as well as the opportunity costs realized because of the partner work hours lost or gained during the execution of the aggregate firm hours.**

Non-Billable: Aggregate Firm Hours

The total **sum of firm-approved marketing and management hours** represent the **total amount of approved non-billable work** done by partners.

Mitigation: Opportunity Costs

When the firm agrees that certain types of work must be done, it approves of that work under the name of firm hours. When one partner does one hour of firm-hour work, that partner enables another partner to do a partner work hour (a billable hour). Partners with a higher billable rate have a higher opportunity cost than others when they do firm hours. **This mitigated opportunity cost is used to calculate the value of any partner doing approved firm work** in order to compensate them accordingly.

⁴ "... realization on partner revenues ... considers the fact if specific, identified partners did not, for example, manage the firm or its departments, others would have to do it , and, therefore, the economic- opportunity cost ... must be spread among all ... $R_p = \frac{[\text{Sum}] C_w}{([\text{Sum}] C_w + [\text{Sum}] V_f)}$ where $[\text{Sum}] C_w = \text{Aggregate partner working credits}$ $[\text{Sum}] V_f = \text{Aggregate authorized firm credits}$ ", Cotterman, James D. Compensation Plans for Law Firms. Chicago, IL: American Bar Association, Law Practice Management Division, 2015. 50. Print.



Overhead

What is Overhead?

Overhead is any non-billable and non-approved (not firm hours) expense. Overhead can be accrued by each partner and/or by associates. An example of overhead would be the Freshbooks billing service cost.

Overhead for Associates

An **associate's overhead is usually accrued per project** since associates are usually provisioned per project. Some associate overhead may be accrued during a relationship building phase (e.g. the Slack messaging system costs). Associates have more startup and shutdown costs since they are more ephemeral in nature.

Overhead for Partners

Partners accrue overhead over their time at the firm. This **overhead is in the form of non-billable expenses** ranging from project management tools to food and drink.

Summary

When deciding if a procedure for allocating payouts is fair, it is **useful to consider its proportionality, efficiency, envy-freeness, equitability, and manipulability in an objective manner**⁵. In this paper we have reviewed Altman Weil's algorithm which

⁵ <https://s3-us-west-2.amazonaws.com/vulk-blog/OnFairness.pdf>

considers **efficiency** (all money is distributed), **equitability** (opportunity costs for talent, quality of work, risk, etc are weighted based on contribution), and **manipulability** (even if the process and compensation is transparent, the participants don't gain an advantage in compensation). This algorithm, along with others like it, are a fair way provide compensation in service based companies.

Appendix A - Main Calculation

Quarterly Partner Compensation		Sub Calculation	Explanation
Partner	Johnny Partner 1		Full Partner in the firm
Sum of all credits worked by associates Q1	\$70,500.00	Sum Cwa	Associates are any non partners (contractors in our case) that the partners use to get work done. The associate credits are the gross billable hours value to the end customer
Associate salaries and benefits Q1	\$20,000.00	Sa	The compensation given to the associates
Per-associate overhead	12	Oa	Non billable hours and expenses related to onboarding, maintaining, and terminating associates
Number of associates	5	A	
Margin on associates	0.6780141844	Ma = [Sum Cwa - Sa - (Oa * A)] / Sum Cwa	The profit made from associates. This is the leverage the firm has when using associates. It represents how efficient the firm is when using resources to accomplish customer goals
Responsible-Partner credits of individual partner	\$25,000.00	Cr	(Origination) Amount of work a partner has brought in (sold) but didn't actually work themselves

Working-Partner credits of the individual partner	\$30,000.00	Cw	Amount of work a partner actually worked themselves but didn't bring in (sold)
Sum of all partner working credits	\$65,000.00	Sum Cw	Sum of all billable work the partners actually worked themselves but didn't bring in (sold)
Sum of all authorized firm credits	\$7,000.00	Sum Vf	Sum of authorized marketing/management hours worked by the partners
Firmwide realization on partner revenues	0.9027777778	$\text{Rp} = \frac{\text{Sum Cw}}{\text{Sum Cw} + \text{Sum Vf}}$	Firm-wide realization is the value the firm has realized from marketing and management functions. This value takes into account the opportunity costs realized because of the partner work hours lost or gained during the execution of the aggregate firm hours.
Value of individual partner time expended in firm authorized efforts	1000	Vf	Authorized (voted on) non-billable hours (including management and marketing) for which the partners are responsible. Takes into account partner billable rates and the fact that if some partners didn't complete these necessary firm-time tasks, others would have to (which creates an opportunity cost)
Per partner overhead	\$450	O	Non billable hours and expenses that don't fall under firm-time
Partner compensation value	\$22,340.48	$\text{P} = \text{Ma}(\text{Cr} - \text{Cw}) + \text{Rp}(\text{Cw} - \text{Vf}) - \text{O}$	This formula does not take into account seniority

Appendix B - Associate Usage

Associate Hours Billed	Johnny Assoc 1	Johnny Assoc 2	Johnny Assoc 3	Totals	Cash Totals
Q1	480	200	50	730	\$70,500.00
Q2	480	200	50	730	\$70,500.00

Q3	480	200	280	960	\$105,000.00
Q4	480	200	50	730	\$70,500.00
Totals	1920	800	430	3150	
Cash totals	\$192,000.00	\$60,000.00	\$64,500.00		\$316,500.00
Associate quarterly pay/salaries/benefits	Johnny Assoc 1	Johnny Assoc 2	Johnny Assoc 3	Totals	
Q1	\$10,000.00	\$8,000.00	\$2,000.00	\$20,000.00	
Q2	\$10,000.00	\$8,000.00	\$1,000.00	\$19,000.00	
Q3	\$10,000.00	\$8,000.00	\$5,000.00	\$23,000.00	
Q4	\$10,000.00	\$8,000.00	\$0.00	\$18,000.00	
Totals	\$40,000.00	\$32,000.00	\$8,000.00	\$80,000.00	
Q1 Hourly Usage	Johnny Assoc 1	Johnny Assoc 2	Johnny Assoc 3	Totals	
Johnny Partner 1	400	50		450	
Johnny Partner 2	80	50	25	155	
Johnny Partner 3		100	25	125	
Totals	480	200	50	730	

Appendix C - Number of Associates and Partners

Number of Associates	5
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Number of Partners	4
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Appendix D - Responsible Partner Credits

Q1 Responsible Partner Credits	Origination	Value worked but originated by others	Totals
Partner 1	5000	20,000	25000
Partner 2			0
Partner 3	10,000	5,000	15,000
Partner 4			0
Totals	15000	25,000	40000

Appendix E - Working Partner Credits

Q1 Working Partner Credits	Billed
Partner 1	\$30,000.00
Partner 2	\$25,000.00
Partner 3	
Partner 4	\$10,000.00
Totals	\$65,000.00

Appendix F - Firm Time

Value of individual partner time expended in firm authorized efforts	Hours expended	Cash Totals
Partner 1	10	1000
Partner 2		0
Partner 3	30	6000
Partner 4		0
Totals	40	7000

Appendix G - Overhead - Associates/Partners

Per Associate	Admin Hours

Q1 Overhead	
Johnny Assoc 1	10
Johnny Assoc 2	10
Johnny Assoc 3	10
Salaried Assoc 4	15
Salaried Assoc 5	15
Totals	60
Hours spent Per Associate	12
Admin hourly rate	45
Per Associate Overhead	\$540.00

Per Partner overhead	Hours	Cash Totals	
Partner 1	10	\$1,000.00	
Partner 2		\$0.00	
Partner 3	30	\$6,000.00	
Partner 4		\$0.00	
Totals	40	\$7,000.00	
Hours spent per Partner	10		
Overhead hourly cost	\$45		
Overhead Per Partner	\$450		
If rolling up associates to partners			
Per Partner overhead	Associates	Other	Totals
Partner 1	10		10
Partner 2			0
Partner 3	30		30
Partner 4			0
Totals	40	0	40

Appendix H - Rates

Hourly Rate	
Partner 1	100
Partner 2	150
Partner 3	200
Partner 4	225
Johnny Assoc 1	100
Johnny Assoc 2	75
Johnny Assoc 3	150
Johnny Assoc 4	150 ⁶