The meaning of the position "Partner" in consultancies - Employee or entrepreneur?

by Hermann Simon, Chairman, Simon-Kucher & Partners Strategy & Marketing Consultants

The short answer to the question in the title is that the term "partner" in itself has no meaning. It is not trademarked, so anyone can call him or herself a partner. Being known as a partner can signify anything from being in regular employment to real entrepreneurship. These differences are fundamental. One of my most astonishing findings from many discussions with applicants and even experienced consultants is that they are unaware that these differences exist, let alone do they know about any of the partnership models in detail.

1. Consulting departments within large organisations

Consultants within large organisations are usually grouped into consulting departments rather than into separate companies. Occasionally these departments are run as limited companies, which are wholly owned by the parent corporation. The managers are often called partners. However, these partners are normal employees, not co-owners, and they do not hold shares in the consulting department or company.

2. Consultancies owned by corporations

This category contains formally independent consultancies, which are owned by large corporations. Some of the most well-known consulting firms belong to this category. The "partners" are employees of the consultancy, but hold no ownership within. As a rule, part of their remuneration is performance-based, and the parent corporation often offers them a share option.

3. Consultancies owned by individuals or families

In this category, the "partners" are also employed by the consultancy and hold no ownership within it. One difference is that the sole owner or the family reserves a very small percentage of shares for the partners.

4. Consultancies owned by the partners, but without realising shareholder value

Consultancies within this category are owned by the partners. Shares are transferred not at market prices, but either for free or for a nominal price which is far below the real value of the company. Most of the large management consultancies belong to this category. To understand this model you have to go back to its roots. Founders of consultancies tend to hold on to as many shares as they can for as long as possible, until they have reached an advanced age. However, if the company is successful, it then becomes too expensive for the younger partners to buy shares at the market price. In this case there are only two solutions: Firstly, and most commonly, the founders can sell the company. This is why most new consultancies are split and lose their identity one generation after they were founded. The only alternative is for the founders to give away shares to younger partners or to sell them at a nominal price. This is the typical approach of large consultancies that have retained their autonomy. However, it also means that shares will continue to be given away or sold at a nominal price in the future. After all, the partners that have been given shares for free cannot cash in from the following generation. In these companies there is no true entrepreneurship in the sense of full co-ownership, investment, risk assumption and so on.

5. Consultancies owned by the partners that realise shareholder value

Only this category is marked by full entrepreneurial partnership. Strangely enough, only a few consultancies employ this model. The reason lies with the founders: The full partnership model cannot be implemented within a successful business unless its founding partners pass on a considerable number of shares at an early stage. I can give you a precise explanation since this is the approach taken by Simon-Kucher & Partners. Each new partner obtains the right to purchase shares in the holding company and to decide how many he or she would like to buy. The price is set by an internal market rather than a formula. This model is highly effective in terms of transferring shares within our company. The three founding partners, whose average age is 56, hold only a quarter of the company shares today. The shares are widely spread among 37 partners, 21 of whom hold two or more percent. Initially, a large investment is necessary, but this is offset by the chance of significant capital growth over the following decades – provided that the company posts healthy growth. I firmly believe that this model of true entrepreneurship is the basis for over-proportional and sustainable growth.

Each consultancy must choose its own set-up. Applicants and experienced consultants may prefer a different model and this cannot be judged. However, an applicant should know what the term “partner” means, be aware of the differences between the partnership models, and decide which model best meets his/her requirements.