

Getting Your Succession Planning on Track



ABOUT PCPS

The Private Companies Practice Section (PCPS) is a voluntary add-on firm membership section of the AICPA that brings together CPAs interested in the business of practice management. PCPS partners with more than 6,400 CPA firms of all sizes nationwide and provides targeted and customizable practice management tools in the areas of technical resources, business development, human resources, benchmarking and succession planning.

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Tips for Getting Your Succession Planning on Track

When you enter retirement, will you be able to reap the rewards of decades of hard work? Is your firm positioned for a profitable sale, merger or a successful transition to new leadership? Those are critical questions for all practitioners. A significant number of CPA firm owners will retire in the coming decade, and firm leaders will need to determine the best ways to navigate this important change.

The results of the 2016 PCPS CPA Firm Succession Survey, a joint project between PCPS and Succession Institute LLC, show how CPAs in firms like yours are addressing succession planning. It highlights some barriers but also provides insights to overcoming those barriers. To learn more, find the full results at aicpa.org/pcps/succession.

This brochure is packed with tips specific for sole proprietors and multi-owner firms, including best practices to consider and resources to assist with the implementation of your own plans. **A successful succession is possible, and these tips can help make it happen.**

Addressing succession planning highlights some barriers but also provides insight to overcoming those barriers.

Tips for Sole Proprietors

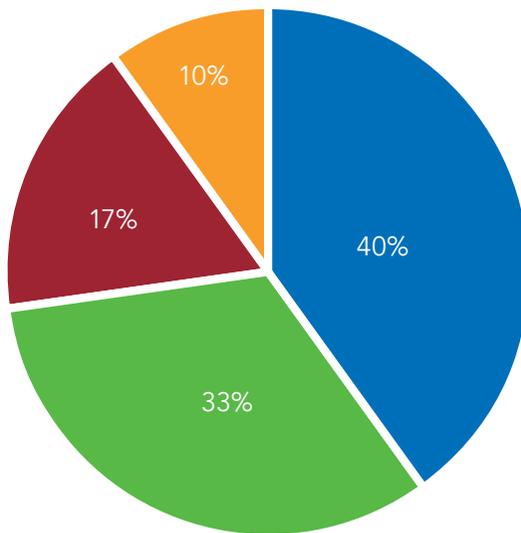
1. Prepare for the unexpected. A **practice continuation agreement (PCA)**, which sets forth who will run or take over your firm in the case of your disability or death, can protect your firm's future. The 2016 survey found that only 7% of sole proprietors had one, however. There are a number of compelling reasons to get started now:
 - a. First and foremost, a PCA can safeguard the business you have built, providing for your clients, staff and loved ones.
 - b. Planning ahead gives you the opportunity to consider the many issues that a PCA should cover so all goes smoothly if the unexpected occurs.
 - c. Putting together a PCA can be a valuable strategic planning exercise. You'll address questions about the potential worth of your practice and who would best run it in your absence. These considerations can inspire ideas on ways to enhance value and identify potential future M&A partners.

PCPS Resources: Among CPAs who didn't have a PCA, **42% didn't know how to get started**. Find PCA templates, topical podcasts and other tools at the PCPS Succession Planning Resource Center: aicpa.org/pcps/succession.

2. The more thorough the PCA, the better. The **PCA provisions** that survey respondents considered most important were:
 - 73%: The conditions that trigger the agreement are clearly identified.
 - 70%: There's a clear formula to calculate the firm sales price.
 - 66%: Upon notice of a triggering event, the agreement clarifies how quickly the responsible party is required to take over the firm.
 - 66%: Payment period and terms.
 - 60%: The party responsible for buying your firm is clearly identified.

3. Be prepared for a **buyer's market** and competition to find ideal merger partners or buyers. A total of 40% of sole proprietors reported that they are planning to fully retire or exit their practices within the next five years, and another 33% plan to transition within 10 years. Nearly half of sole proprietors said their first choice of exit strategy was to merge with another firm.

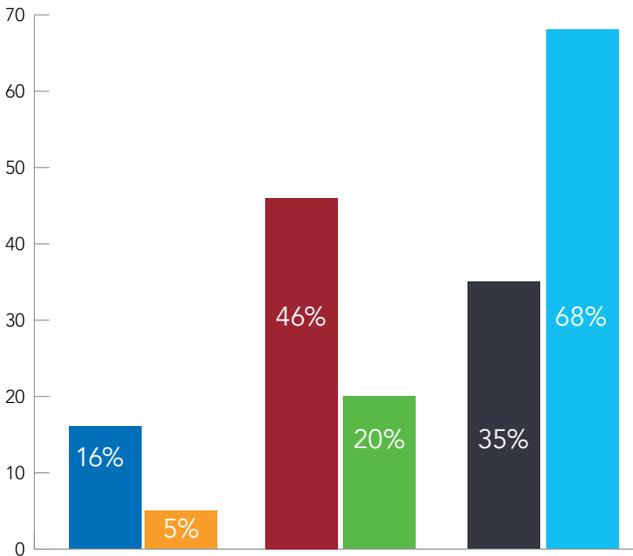
Exhibit 1: I'm planning to retire or exit my practice:



- Within five years
- In 11 to 15 years
- In six to 10 years
- In more than 15 years

4. Determine whether **the deal** you're expecting is realistic. There is a considerable gap between what sole proprietors expect to receive for their practices, as well as the terms of the deal, compared with current market realities. Some of these seller expectations may become even more difficult to achieve as a significant group of baby boomers retire and sell their practices in the coming years.

Exhibit 2: Seller Versus Buyer Expectations



- Seller:** 16% expect lump-sum payment at time of sale
- Buyer:** 5% paid lump sum

- Seller:** 46% expect sales price to be set at the time of sale and paid out over time
- Buyer:** 20% made that type of offer

- Seller:** 35% expect their payment to depend on client retention
- Buyer:** 68% retention was a payment factor

5. Take steps to **raise your firm's appeal**. The most popular approaches that surveyed sole proprietors are taking to make their firms more attractive to an outside buyer are:

Exhibit 3: How are sole proprietors enhancing their practices?	2016
Increase fees/billing rates	70%
Streamline workflow and processes	62%
Leverage technology whenever possible	61%
Improve the overall profitability of the firm	56%
Delegate — handing off lower-level work	54%

PCPS Resources: *The Succession Planning Guide, specifically Chapter 4 — Selling Your Firm, and related podcasts can enhance your efforts. Find them at aicpa.org/pcps/succession.*

6. **Train and develop staff.** While it may sound counterintuitive, the years leading up to a possible transition may be a good time to add another person. By delegating the day-to-day tasks, you give yourself the chance to focus on the business of managing — and enhancing — the practice. Forty-nine percent of sole proprietors picked training their people as one way to increase firm value. When you're ready to sell or merge, you can offer a firm with a structured, clear leadership path and well-trained staff that is ready to maintain the client relationships and services you built.

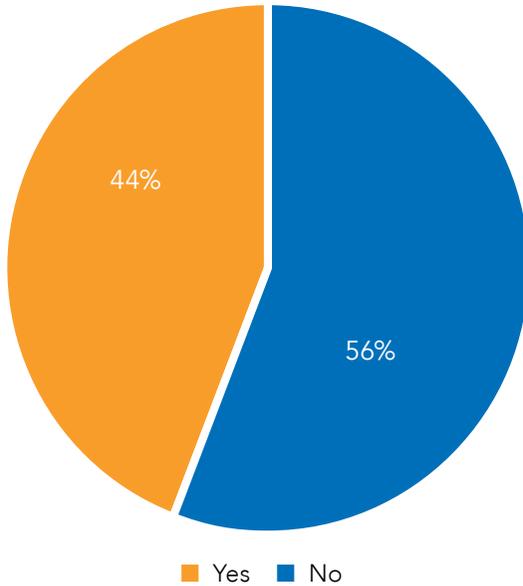
***PCPS Resources:** Using tools such as the **Staff Assessment** and **Career Development Plan** will encourage emerging leaders to develop their own journey as partner. The **Firm Competency Model (Career Ladder)** provides an example of a well-defined path. Find these and other resources at aicpa.org/PCPS.*

7. Determine your exit strategy, including a **three-year formal succession plan**. No matter the firm size, a formal plan can help focus your thinking and identify necessary steps to achieve your goals. This is advice you'd give your clients, and it holds true for your firm.

Tips for Multi-Owner Firms

1. Create a **formal succession plan** as the first step. Even though 84% of firms said they expect succession planning to be a significant issue in the next decade, the majority of firms don't have a plan. Without a blueprint, the transition that occurs when owners leave could be unnecessarily difficult.

Exhibit 4: Does the firm have a written, approved succession plan?



2. **Review partnership agreements.** They are a valuable tool that lay the groundwork for a successful succession and minimize day-to-day conflicts and misunderstandings by establishing firm-wide management policies and procedures. Unfortunately, only 63% of firms had a partner agreement. Among other things, the policies should clearly articulate the scope of and limitations on the role of retired owners.
- a. It is best to determine, and document, acceptable roles and pay for retired partners when no one is on the verge of retirement. The firm will be able to make objective choices without worrying about their impact on any one individual.
 - b. Confirm your firm's partnership agreement does not omit important considerations. Full survey results detail numerous examples of items to consider and additional issues to address in partnership agreements.

***PCPS Resources:** Template partnership agreements and further guidance are available in Chapter 11 of the Succession Planning Guide at aicpa.org/pcps/succession.*



3. **Leverage staff effectively.** By doing this, owners can channel their energies into management issues and higher-level services. It's particularly important before a retirement in order to create capacity to take on the work of a retiring partner.
4. **Consider all aspects of prefunding retirement.** As partners get closer to retirement, they may be less likely to support substantial investments in technology, training, hiring, improved operational processes and other initiatives to ensure money stays in the bank to fund their retirement. By prefunding a portion of their retirement, partners may feel more secure in their retirement funds, providing more incentive to contribute to the firm's ongoing success.

Best Practice: *Generally, the prefunded portion of the retirement obligation should not exceed 20% in order to make the partner comfortable while keeping the partner interested in additional firm growth opportunities. Each firm's specific goals and ability should be assessed when prefunding a retirement obligation.*

5. Protect the firm's assets by **implementing penalties for outgoing partners who take staff or clients**. In addition to leaving the firm financially vulnerable, allowing partners to "own" their clients can support a silo mentality and make it tough to build a sustainable, unified practice. Firms also will face turnover costs for every employee taken when a partner leaves, and could suffer significant opportunity costs if it's a promising, key person.

Exhibit 5: Penalties or Costs for Outgoing Partners Taking Clients or Staff

- 31% of surveyed firms had no penalties or costs for taking clients
- 23% had no penalties or costs for taking staff



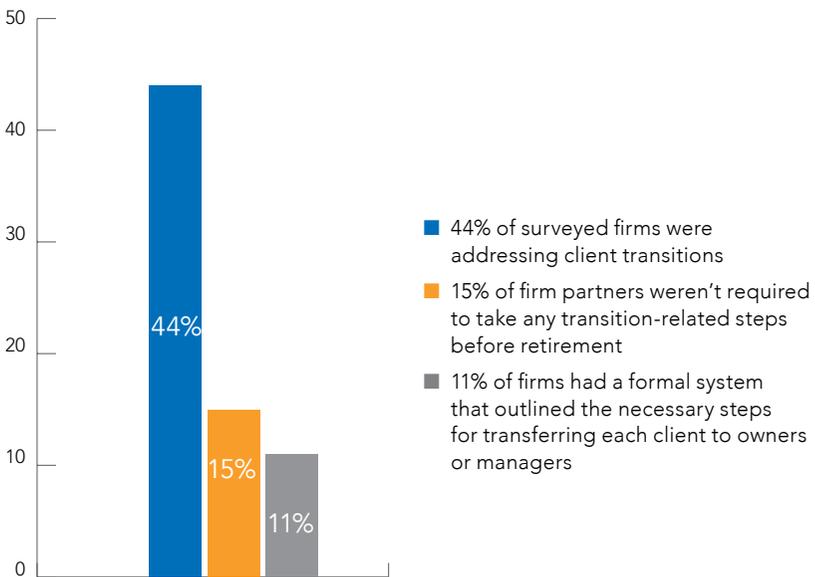
6. **Set clear expectations of the retirement age.** Partner retirement without sufficient notice can be a financial- and succession-planning burden. Strategic consideration of the retirement age can make it possible for emerging leaders to take on new roles and responsibilities but also allow the firm sufficient time to capitalize on experienced leaders' knowledge and the relationships they've built.

Best Practice: *Partners should give at least two full years' notice before leaving to receive their full retirement benefits.*



7. **Keep clients happy** by setting rules for transitions. CPAs spend years developing strong relationships with clients. When they're preparing to leave, it's important that care is taken in shifting those relationships to a new key contact.

Exhibit 6: Firm Practices for Addressing Client Transitions When Owner is Two or Three Years Out From Retirement:



Best Practice: *If you're planning on a sale, merger or internal succession, client transition is critical. Refer marginal clients to other firms that better meet their needs and give key clients personal updates on your transition plans so you can allay their concerns and show you value them.*

8. **Prepare new leaders.** Your firm’s success depends on its future leaders. Proper client transition — and ongoing management of the firm — is most successful when the practice has qualified new leaders ready to take the reins. That may be difficult for many firms to achieve, however, since 70% don’t have either formal or informal requirements for admission to partnership. Below are the top three steps firms are taking to nurture promising leaders.

Exhibit 7: What is your firm doing to develop future leaders?	2016
Identification of, and training for, specific competencies (preferably based on a competency model)	53%
Formal training or education in soft skills such as management, assertiveness, handling conflict, communication, change, etc.	36%
Formal training or education in management and delegation	34%



9. Diagnose and tackle your **firm's top barriers** to effective succession management. The survey revealed the following are among the top succession challenges firms face:
- a. Senior partners don't believe younger professionals are ready to take over leadership.
 - b. Retiring partners have no incentive to get involved in client transition — and they may not even want to retire.
 - c. Partners working in silos mean there's no shared vision of the firm's future.

PCPS Resource: *The firm inMotion e-Toolkit can guide you through the latest trends affecting the profession, including generational differences in how trends are viewed. Assess firm strategy, culture, client relationships and other topics with an eye on the future. Find the toolkit at aicpa.org/pcps/inMotion.*





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