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Six Steps to Selling Your Practice

By Joel Sinkin

You worked long and hard. Finally, it's over. Another tax season is behind you. Like many of your colleagues, you're probably wondering what comes next. Maybe you promised your spouse this would be the last season. Perhaps you set a goal for yourself and would like to make a career change. Maybe you love the business, but you're just tired of the challenges of being self-employed.

Every year at this time, NATP is flooded with requests for information on how to sell a practice. Clearly there are many factors involved in the process. Some practices are unique and have certain issues that must be specifically addressed; however, the following steps to selling your business should apply to almost all practices and hopefully supply you with more than just a starting point.

1. Determine When to Start the Selling Process

Many practitioners wonder when they should initiate the process of selling their practice. My first question to them is, "How many more tax seasons do you wish to work full time?" Most professionals have a significant number of clients whom they only deal with during tax season. It may seem like an eternity to you, but if you give your clients a three-year notice, from their viewpoint, it may only be three visits! To conduct a proper transition, you should build in some time that clients see, or at least perceive, you and the buyer working together. This will create a higher level of comfort for your clients. We'll discuss this further in Step 5. If your practice consists mostly of business clients whom you work with on a monthly basis, less time may be required to conduct a proper transition. But, if a high percentage of your clients are annual, you may need additional time to establish your successor. In an ideal world, sellers would affiliate with their ultimate successor for at least two tax seasons before they reduce their role.

Lease, Equipment, and Staff Considerations. In the event a practice is not dependent on the buyer retaining the exact same location, the date your lease expires may have an impact on the timing of the sale. By signing a lease, you may either eliminate the buyers who may be interested in bringing your practice into their pre-existing location, or put them in the position of reducing their offer by the cost of running a second office location. If your lease is coming up shortly, perhaps now is the time to look into affiliating with your ultimate successor in advance of committing to another extended period of time. If, on the other hand, you have a superb office location, having the option to retain the location may be critical to its ultimate sale.

Equipment has similar concerns for the timing of starting the selling process. You need office equipment, but why purchase new equipment if you are seeking to sell? Maybe this is a good time to affiliate with a successor who has the equipment you need, conduct a gradual transition, and then quit while you're ahead.

Suppose you need to hire some help. Why hire and train new staff if you are so close to selling your

business? Instead, an affiliation with your successor, who has the capacity to pick up the work, makes more sense. Now you have help, plus you've simultaneously started the transition process.

2. Make a List of What You are Selling

Any serious buyer will quickly seek information about the seller's practice. Prior to meeting with potential buyers, you should prepare a summary sheet of what you have to sell. This description of your practice should not have any names of actual clients or businesses, but list the types of clients you have, the industries they are in, services you provide, frequency of service, fees generated, staffing, billing rate information, and specialties, if any.

By sharing this information with a potential buyer, you will be presenting a clearer picture of what the practice entails. This will assist both parties in determining whether there is a mutual interest in the sale.

3. Identify the Parameters of Your Successor

When deciding who should take over your practice, consider chemistry and continuity. Change is hard for any client, so you must seek a situation that limits change as much as possible. Find a successor you feel comfortable with. If you like the buyer, chances are your clients will too. Then, consider the following:

Size. If your clients are used to dealing directly with you, perhaps you shouldn't sell the practice to a firm that intends to have a large staff handle their accounts. Bigger is not always better. On the flip side, clients who are accustomed to dealing with larger firms with multiple specialties almost demand a successor firm who can offer these things too. Typically, different size firms have different billing rates and service philosophies, so review these areas to ensure your clients will receive the same service for a similar fee.

Availability. Above all, remember your ultimate goal of selling your practice. You must determine if a buyer has the excess capacity to ultimately replace you and any non-returning staff members. I recall someone once saying that since he was a sole practitioner doing approximately \$200,000 annually, he would seek to sell his firm to another professional similar in size and focus. To this, I asked him how much excess capacity he currently enjoyed in running his practice. He laughingly suggested that he barely remembered what his wife looked like! Then I asked him how much available time the buyer he defined would have to replace him? Just something to think about.

Specialties. If you provide financial services to your clients and expect to sell that aspect of the business, your buyer will need certain licenses. And, if your practice includes providing business valuations or IRS representation, you must be sure the successor is licensed and capable in these specialty areas as well.

Background. In a world where many people are properly attempting to be "politically correct," you must maintain candor and reality in selling your practice. If your practice has a lot of clients who require someone who speaks a different language, how can you consider selling it to anyone who does not? There are practices that not only have language concerns but perhaps cultural or ethnic realities that would impact long term retention of clients. These areas need to be addressed and dealt with appropriately.

Location. The real world also dictates whether the buyer must retain your exact location, must be in the immediate area, or has a lot of flexibility geographically. Most practices do require some level of geographic consistency in the buyer, but don't always demand the exact office location. If you prepare a great number of individual 1040 returns, office location will be a factor in client retention.

To determine how portable your practice is, consider the following scenario. Imagine you are planning to continue operating your practice. Your lease is about to expire, but you cannot extend it for some reason. How far could you relocate your office and still retain your clients? If the transition is done properly, this is the same distance your buyer can relocate to.

4. Value Your Practice

There are five main variables to consider when preparing a valuation of your practice. These variables will provide you with a very basic understanding of the initial process.

Cash Up front. Very rarely is an accounting or tax practice acquired with 100% of the purchase price paid at the closing. Most deals have from zero to 33% of the anticipated purchase price paid at closing. Many items can impact the down payment, such as the accounts receivable a seller has and the time of year the buyer is acquiring. For example, if a buyer is acquiring a tax practice in May and is 9-10 months away from collections, the down payment will suffer.

Length of Retention Period. The overwhelming majority of practices sold include a retention period where lost clients, as well as fee increases from clients, impact the purchase price. These retention periods can be as short as one tax season or can run the entire duration of the payout period.

Profitability of Sale. This subject is not limited to what your net profit will be. Unless the buyer is taking over your actual location and running the practice exactly the same as you did (including the staff), your net profit may have little to do with the buyer's. The buyer needs to address what his profitability will be. This includes the tax ramifications of the deal. Now that items such as goodwill, restrictive covenant, client list, etc. are all 15-year deductions, you must consider how the purchase price will be treated from a tax standpoint. Making someone take on overhead they did not need will ultimately reduce the profitability of the deal as well.

Duration of Payout Period. How long the buyer has to pay off the balance owed to the seller is another important variable. Most deals typically provide three to ten years for payout periods.

Multiple Billings. Most practices are sold as a multiple of billings. For example, if you have a practice that generates \$100,000 annually and are seeking a 1.25 multiple, your anticipated buyout is \$125,000. Of course as earlier mentioned, the retention period most likely will mean an adjustment must be made in the balance owed, but the multiple is typically the formula that ultimately establishes the purchase price prior to any adjustments. The formula: the more money up front, the shorter the retention and payout period; the less profitable the acquisition, the lower the multiple. The less money up front, the longer the retention and payout period; the more profitable the acquisition, the higher the multiple.

5. Prepare a Proper Transition

Philosophy. Very few clients have sufficient knowledge to determine the skill level of their tax professional. Because of this, clients have many choices. Why do they choose and stay with a particular practice? They may do so because of the location or the fee structure. But, perhaps the number one reason is because of the owner or people who service them. To make sure a transition goes well, you must realize that your clients enjoy a certain comfort level with you. Maintaining this comfort level is paramount in client retention. Change is unsettling; additional talent and services are welcome. Always seek to offer continuity to the clients. Where reasonable retain staff, locations, fee structures, and methods of servicing clients.

Announcing the Deal. Most deals are held out to the client base as a merger – not the loss of the people they trusted, but the addition of the new talent and firm. Larger clients are typically notified of the impending change in person or by phone. You can notify others by mailing an announcement letter or telling them during their tax appointment.

Continuity. A reoccurring theme throughout this article has been continuity. Continuity of names, location, fees, staff, and other items are the keys to long-term client retention. Make your changes slowly and let the clients get comfortable with the buyer before wholesale changes are installed. Remember, if chemistry is a key in choosing whom to sell too, offering continuity is the key to the deal's success. Most sellers stay on with their successor for months or even years in a reduced capacity to help clients through the transition.

6. Seek Professional Help

The selling of an accounting or tax practice is tremendously different than the selling of almost any other business or professional practice. This is mainly due to the fact that these deals include retention periods, are structured differently than traditional buy/sell agreements, may start off as a merger with an ultimate buyout, include exposure concerns and accounts receivable issues, plus much more. Having someone who has personally handled at least six transactions of this nature, specifically relating to the industry, is key. The benefits to the seller, and to the buyer as well, include:

The proper intermediary can exchange information without providing each other the names, can screen the buyers to ensure financial and professional requirement to close the deal, and can provide the advice that comes from experience.

When dealing directly with each other, emotions can kill many deals. Remember, the buyer wants to pay the least and the seller wants to receive the most. These are adversarial positions that can be softened by the right intermediary.

Time kills all deals for many reasons. Having a good intermediary or advisor should not only better protect both parties, but also speed the process along.

There are strong needs for expertise in the drafting of these agreements. Without experiencing multiple closings specific to this field, how could a mediator fully protect both the buyer and seller? For example, every buyer wants a contract containing representations clauses that would protect him from items that cannot always be uncovered through due diligence. A seller who is providing a retention period needs protection that ensures the buyer is properly accountable for retaining clients and servicing them within certain constraints. These are the types of things that protect both parties and create positive deals for everyone.

Conclusion

The decision to sell your practice may be difficult. But, the actual process doesn't have to be. One of the first questions a buyer may ask is why you are selling. Are you getting out for health reasons, burnout, or do you simply desire to change your specialty? Are you retiring? The answer will help you to establish the type of successor you will need. Being aware of the reasons you seek a sale will be important in many ways as you go further into the process.

Following this article a few resources available to guide you through the process of selling your practice.

With a little help, you'll soon be able to face the first few months of the year with a little less anxiety. Good luck!

*Joel Sinkin is a partner in Accounting Transition Advisors, LLC. The firm services the accounting industry exclusively, providing merger and acquisition assistance to firms seeking to merge, acquire, or otherwise affiliate accounting practices and related enterprises. To date, Mr. Sinkin has facilitated over 700 successful closings of accounting affiliations, has published numerous articles in state and national professional publications, co-authored, the "bible" of the accounting affiliation field, *Buying and Merging CPA Firms*, published by PPC, and teaches CPE courses across the country. More importantly, his firm is now handling and creating numerous affiliations in the accounting industry in response to the needs of the current marketplace. Call corporate headquarters at 866 279 8550 to receive additional information, a free valuation of your practice, or an update on the current marketplace for buying, selling, and merging practices. You can reach Mr. Sinkin directly by e-mail at jsinkin@transitionadvisors.com or through the website of www.transitionadvisors.com.*

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