

Case Study Number 2: A Four Partner Firm with Dissimilar Retirement and Career Goals

The Seller

The seller was a four partner firm generating \$3,500,000 in annual fees. The firm had quality staff members but none were on a partner track and therefore the firm did not have a viable internal succession solution. The most senior partner, who was seeking to work part time as soon as possible on his way to full retirement, handled much of the administration and performed the least amount of billable hours. The other three partners averaged 1,500+ billable hours annually. All the partners handled similar sized books of business and were equal in equity in ownership. Two were young partners not seeking succession. They were interested in becoming part of a firm that would allow them to grow professionally and financially. The other senior partner was seeking to work several more years and then be bought out.

The Buyer

The buyer was a ten partner firm generating \$9,500,000 in annual revenues prior to the transaction. The firm offers a full range of traditional services and also offers various specialized consulting services to its clients including operational improvement, specialized services for health care providers, and business valuations. The firm had the ability to acquire additional office space in its existing facility and was confident it could provide additional staff necessary to deal with both the needs of the seller firm and new growth. The buyer firm had a proven track record of growth. The partners' goal was to more fully utilize the capacity they believed they had to manage a larger firm, add more clients and grow the top line all while adding talent to the firm. The firm also had two managers that were on a partner track and this merger would put the firm into the position to accelerate their development.

Negotiation Process

After initially meeting a few firms of varying sizes ranging from \$5,000,000 to \$50,000,000, the seller narrowed the field to the firm we introduced and is described above. We assisted in drafting a proposal and a verbal agreement was reached. We prepared a non-binding letter of intent and due diligence lists (provided by us to the parties) were exchanged. The parties conducted field reviews. We provided first drafts of contracts and transition plan. The time from introduction to having the terms resolved was approximately 13 weeks.

Deal Terms

Because each of the partners of the selling firm had such different career goals, the advisors at Accounting Transition Advisors recommended that in essence three different deals be created for each situation the partners of the selling firm faced. The deal was structured as a combination of the following three approaches:

- An Outright Sale: The senior partner seeking an immediate transition was bought out based on a 1X multiple (of his firms' total fees) times his equity interest in the firm with an 8 year payout and structured so as to provide a current deduction for the successor firm. There was a two year adjustment period wherein if the fees in the overall seller

- firm dropped by more than 5% during that period, the buy out price would adjusted pro rata. Otherwise the price was fixed at closing. The selling partner was given a new business incentive program that rewarded him with 15% of gross collections for three years on any new clients he developed and introduced to the successor firm and a 33% of what he bills out for any work the firm and he mutually agree for him to handle on a part time basis.
- The partner seeking to work three to five more years before retiring from full time was going to be kept whole in income during those years provided the fees on his managed book of business and time commitment remained steady. His compensation was tied to the collections from his book of business that replicated what he was making at the time of the merger. If he reduced his time below a mutually agreed upon level or at the end of the fifth year, whichever occurred first, his buyout would commence based on the same terms as the partner who was bought out day one. He was not given equity in the successor firm but held out as a Principal in the firm and given essentially all the rights and privileges of an equity partner other than the compensation and retirement formulas used in the partnership agreement.
 - The other two partners were admitted as equity partners in the merged firm wherein they exchanged equity in their old firm for equity in the new firm. Their equity was calculated based on a fraction wherein the numerator was their firm's trailing twelve months revenues times their equity percent and the denominator was the combined firm's revenues less the revenues attributed to the ownership by the two senior partners. There were no large unusual projects that needed to be removed from the calculation for this to be a fair representation of value. This approach was used because the two younger partners' compensation was at risk with the other equity partners for the senior partner buyouts. There was a one year look back period wherein if either firm lost more than 5% of their revenues, there would be a pro rata adjustment in equity.

Benefits to Both Parties

The successor firm added two equity partners, staff and additional clients (and the attendant revenue). There was an expectation by both firms that the selling firm's fees would be increased significantly due to the availability of more services to their clients. Furthermore, the selling firms' referral network was expected to produce a lot more referrals due to the increased capabilities of the combined firm. The two partner track managers in the successor firm were positioned to become the successor to some of the retiring firm's clients which accelerated their development. The transition was extremely smooth. The firm became known as a stronger regional firm in their area. The selling firm was able to obtain an affiliation that provided each partner a method of accomplishing their personal, financial, and professional goals.

Certain facts and descriptions have been altered to protect the confidentiality of the parties involved in the above transaction.