

Succession Planning: Weathering the Perfect Storm

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One of the most frequent questions practitioners ask with regard to succession planning is the basic premise of "when should I start? My answer to them is simple: Succession planning ideally begins the day the firm opens its doors for business. But seldom, if ever, is that proactive strategy deployed.

While you can never begin proper succession planning too soon, a harsher reality within the profession is that many firm owners begin too late and have sadly procrastinated to the point where they're faced with unfavorable transition options: among them, a hastily arranged merger, or, in a worst-case scenario, simply turning out the lights and locking the doors.



Augment that backdrop with sobering demographics from the American Institute of CPAs' 2012 PCPS Succession Survey which found that 61 percent of current firm partners are over the age of 50 and 67 percent of the firms polled expected at least one partner to retire within five years. And more than half of the nearly 1,000 single and multi-partner firms who responded to the quadrennial report, indicated that more than one partner would exit within that five-year frame.

The concern over succession planning and its eventual effect on firms won't ebb anytime soon however, as 80 percent of the firms in the Institute poll expect succession planning to remain front and center as one of the most significant issues impacting both their business and valuation over the next decade.

To further underscore just how far the profession is lagging behind in the succession planning arena consider the following:

- Less than half of multi-owner firms in the PCPS poll said they have a formal succession plan in place, and for firms with 15 full-time employees or less, more than 70 percent do not.
- For sole practitioners, the news is no more encouraging as less than 6 percent have a practice continuation agreement in place in case of death or disability.

Getting Started

Whether you're a large or small practice, every owner shares a common concern with regard to succession: What will my firm look like when the current partners are no longer actively involved in the practice?

While it's never early to begin mapping out a formal plan, as a partner or owner your ultimate objective should be to successfully transition your current client relationships and monetize the books of business - either to an internal successor, or to an outside firm via the merger route.

If your goal is to create an internal succession strategy, step one will require you to complete a thorough evaluation of your in-house talent.

Do you have adequate "bench strength," or high-performing potentials who you and the current owners feel can be nurtured and eventually assume the mantle of partner?

If you do, then crafting a formal succession plan will be somewhat less challenging but it would require creating achievable benchmarks and time frames. When looking at internal candidates, it's critical to do a deep drill down on their past performance. Did they learn your systems quickly? Have they demonstrated an ability to develop new clients? Many firms may first decide to place them in a stepping stone-type post to see how they perform, and that means often placing them in a non-equity or income partner role at first.

But never consider promoting a long-tenured employee to full partner just because he/she has been with the firm for a long time. Longevity should never be a component to a succession formula. And always replace the role, not just the body. If an audit partner is leaving for example, don't elevate a senior tax manager to assume the departing owner.

Remember, it traditionally takes a minimum of two years to transition a client from one partner/owner to the next generation of firm leaders. If your clients are "partner loyal" (clients who are more loyal to a particular partner than to the firm) as opposed to "brand loyal," it may take even longer.

So as an owner, you must first ask yourself how many more years you want to work full-time (not retiring) before gradually putting the brakes on your workload. Most firm owners don't make the leap from full-time to retirement in one step, so partners need to think in terms of how long before you want to reduce their time commitment as opposed to when they want to exit out completely.

If, say, you decide you want to slow down in three years, for most firms, by and large that's a total of just three in-person client visits as roughly 85 percent of CPA firms report that most of the annual tax and business clients are seen in their offices just once a year.

Technology – and specifically cloud applications – have penetrated the accounting space to the point where a majority of clients are often sending their sensitive data through encrypted portals and thereby curtailing the frequency of in-person office visits.

If after your assessment you're still uncertain as to whether the firm's internal bench is strong enough to lead the firm into the next generation of growth, chances are, you will have to look externally to locate your successor, via the M&A route.

As a succession planning solution, M&A has emerged as one of the predominant trends within the profession as scores of major unions have been announced over the past several years with hundreds more that have happened under the radar. Just two years ago more than half of the top 100 firms in the U.S. executed at least one merger.

Choosing the Right Firm

So how do you locate your successor? We always advise our clients to concentrate on potential suitors who demonstrate the Four Cs – culture, chemistry continuity and capacity. Let's examine each facet in more detail.

Chemistry: Our company often recites a simple caveat to our clients: if you don't want to have lunch with someone, don't do a deal with them. If your partners are uncomfortable with a potential successor, why would you think your clients would be?

Culture: This can range from a basic, what's it like to work here? To more in-depth queries of what's it like to be a

client or partner here.

Continuity: Most firms have their clients because the clients feel comfortable with their people and services and have grown accustomed to a certain degree of handholding. In a merger, the successor firm must frame the union as not the loss of the old firm but rather highlight the synergy of the newly combined firm.

Capacity: Determine how many chargeable hours the retiring partner(s) currently log – can some of that that be replaced by lower-level professionals in the successor firm? Smaller firms in particular need to be cognizant of the time an owner spends handholding clients and determine whether that can be transition to a staff member of the successor firm or does it have to remain under the purview of an owner or partner?

Firms considering an external sale should also be wary and avoid locking themselves into a long-term lease. Potential successor firms that already have a presence in your market will not want the headaches associated with assuming a multi-year lease or trying to find a sublet.

Summary

But whether your succession solution lies within your firm or with an external suitor, the time to begin succession planning is now. Firms that continue to postpone this critical strategy face the very real prospect of watching the value of their practices and years of sweat equity diminish as the number of firms seeking M&A as a succession planning solution begins to soar leaving an uneven playing field with regard to supply and demand.

The firms that are not proactive will more than likely create real estate opportunities down the road for those that are.



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Bill Carlino joined Transition Advisors as Managing Director of National Consulting Services in 2012 after serving for nearly 12 years as editor-in-chief and editorial director of Accounting Today and AccountingToday.com, where he was responsible for all content both in print and online. During his tenure as editor, Accounting Today won a number of financial journalism awards including Excellence in Financial Journalism from the New York State Society of CPAs and was a two-time finalist for the Jesse R. Neal Award, the premier publishing accolade among business-to-business publications. In his new role as managing director of consulting, he helps match Transition Advisors' array of services such as succession readiness evaluations, new partner admissions, partner retirement and exit support, partner retreats and owner agreement evaluations and design, to the strategic transition and succession needs of CPA firms across the country. He has been a frequent industry speaker, presenter and panel moderator and has appeared as an expert commentator on such business channels as CNBC, Reuters, Bloomberg, CNN as well as National Public Radio.