8 Keys for a Proper Internal Succession Plan

By: Joel L. Sinkin and Terrence E. Putney, CPA, Transitions Advisors, LLC,
Leading CPAs Through Transition With Succession and M & A Strategies.

When you start planning for the internal succession of the partners in your accounting practice, there are many vitally important items to review. Below are 8 key things to keep in mind.

1) Assess the adequacy of the personnel that will replace partners that will be leaving

An internal succession means you have or will find the necessary talent in the firm to adequately replace partners that will be leaving. You should consider all of the duties partners are responsible for, such as client management, practice development, high level production and expertise, administrative, and leadership. You cannot replace the partner position only, but need to replace the role as well. For example, if the partner retiring was handling the administration for the practice, replacing him with a rainmaker can create a problem. Make sure the people that you are assuming will take over these duties have the excess capacity and talent to adequately perform them. If you will need to develop or recruit the necessary talent, consider to what extent you have been able to do that in the past when assessing the viability of your plan.

2) Know what your partners are planning with respect to their succession and make sure your agreement requires adequate notice

A successful plan depends on knowing what your partners' plans are for their succession. The longer your firm has to plan for what will be required to transition client relationships, replace critical responsibilities, and find the necessary talent, the better the transition will go. You should encourage frequent discussions amongst the partners about their plans. Your agreement should require notice of intent to leave that is a minimum of two years in advance of the intended date to minimize risk for the firm.

3) Determine the value of the equity in your firm in a manner that is fair to all the parties

A fair valuation of a partner's equity is one that the firm and remaining partners can afford to pay. Use a backwards approach. Start with the foregone compensation of the partner that will be leaving and with those funds allow for the buyout or retirement payments, be sure to allow for the cost of replacement talent, and leave some upside potential for the partners that are left. If the buyout is not self-funding or creates significant financial risk for the remaining partners, the retiring partners may not receive all that they expect or the partners expected to make those payments may not be willing to do so.

4) Make sure your agreement protects client and staff relationships

The basis for the value of equity is the relationships the firm has with clients and key staff. If a partner is being paid for the equity, there should be no risk that the firm will lose those relationships due to competition with that partner at least during the term of the payments.

5) Cover all types of termination in your agreement

Every kind of termination of a partner's role in the firm should be covered in the agreement including retirement, death, disability, involuntary termination, and voluntary termination for other than retirement. Each of these terminations carries different types of risks for the firm. Therefore, consider buy out terms that take into account how client relationships and other transition issues, the things that affect the value the firm, will be handled.

6) The buy-in terms for new partners need to be fair as well

Just like the buyout terms for partners leaving need to be realistic, what newly admitted partners are asked to invest needs to create a lucrative opportunity for them. The expected terms should leave a significant opportunity for increasing levels of income or cash flow net of the investment terms in order to attract and retain the level of talent you will need to have a viable internal succession.

7) Consider what your options are if your internal succession plan is not viable

The number one reason firms seek external succession, such as a sale or an upstream merger, is because they don't have a viable internal succession plan. If your firm is five or fewer years away from partners retiring or significantly slowing down, you may not have the time necessary to develop and implement an internal succession if you have not already done so. Even if you have planned ahead adequately, you may encounter unintended circumstances that make your plan no longer realistic.

There are many ways to create affiliations with other firms, such as mergers or mergers with prearranged buyouts that will accomplish all of the objectives the partners have for their succession. Planning for external succession when you are five or fewer years away will allow you enough time to find the right solution for your firm.

Find expert and experienced help

Lawyers will say, "An attorney who represents himself has a fool for a client." Accountants need to recognize the same thing. In creating a succession plan, internal or external, there are many things that need to be worked out. Valuing the practice, structuring the deal, treatment of accounts receivable, WIP, liabilities, names, roles, transition strategies, partner buyout provisions, documentation of the deal and much more. This is not only a critical business decision it can get emotional. Having a professional, who has years of experience specific to accounting practice sales and internal succession, can be the most important step in obtaining a win/win deal for everyone.

If you want to find out more about how succession planning can work for you, we will provide you a free consultation and valuation of your practice. To find out more about what your practice might be worth, how to start the succession process, or if you have any other questions or comments, please feel free to call us directly or e-mail us at jsinkin@transitionadvisors.com (Joel Sinkin) or tputney@transitionadvisors.com (Terry Putney).

Go to our website, www.transitionadvisors.com and click on articles for more free information on buying, selling and merging accounting firms.

Copyright © 2012 Transition Advisors, LLC