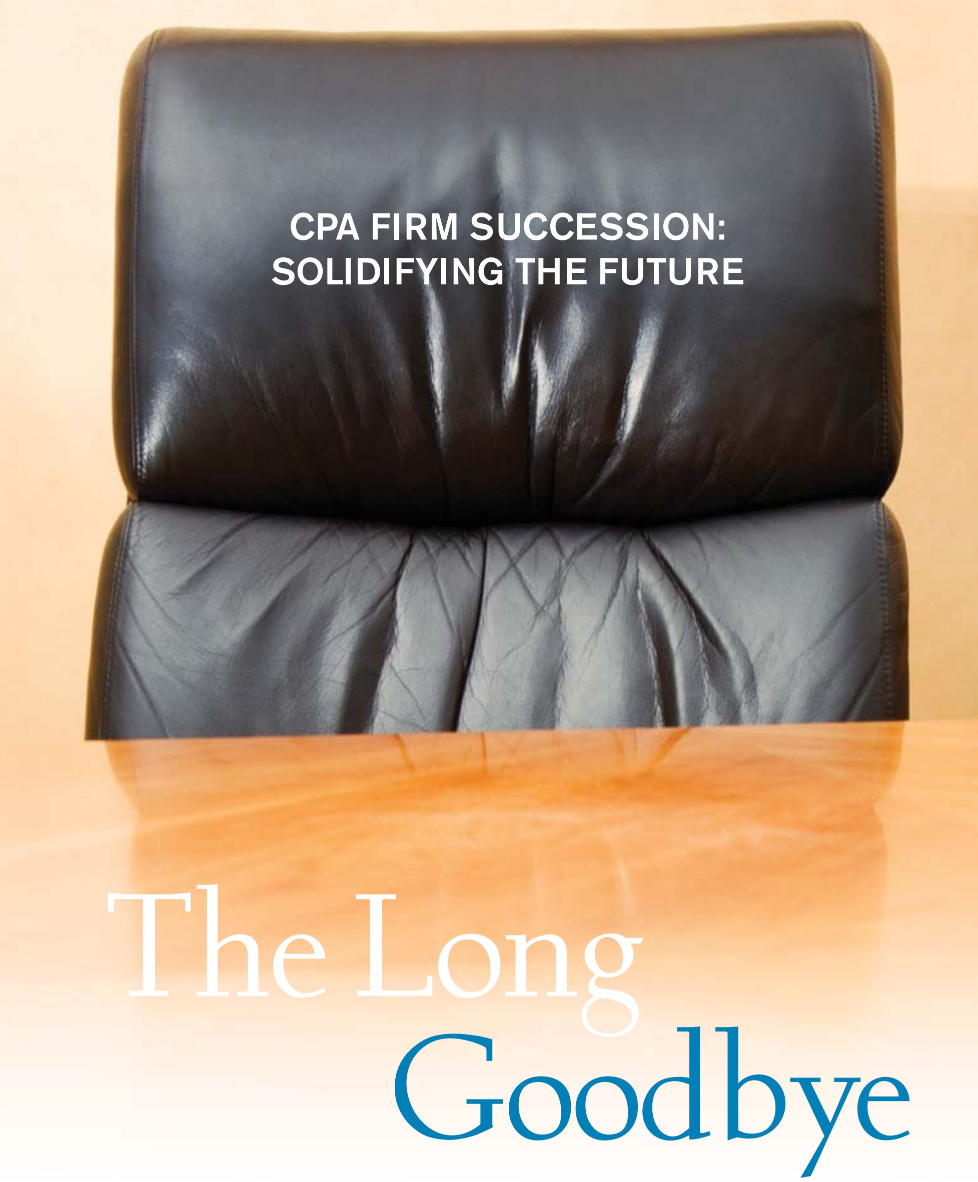

CPA FIRM SUCCESSION: SOLIDIFYING THE FUTURE

The Long Goodbye

Second in a series: Partners need to factor in the frequency of their client visits, among other things, as they transition into retirement.

by Joel Sinkin and Terrence Putney, CPA

About the Series

Powerful forces are transforming the accounting profession in the United States. The Baby Boomers are heading into their retirement years. Baby Boomer CPAs are in charge of most U.S. accounting firms, and most U.S. accounting firms don't have a signed succession or practice-continuation plan in place.

These realities are rewriting the rules for U.S. accounting firms and CPA firm owners. Firms must contend with unprecedented financial, cultural, and marketplace changes. The *JofA* is presenting a succession series designed to help accountants navigate the new landscape of succession and mergers. This month's installment, the second in the series, looks at how much time accounting firms need to develop, implement, and execute a succession plan.

The best time for an accounting firm to start work on a succession plan is the day the firm is formed. Of course, most firms don't do that. The question in many cases has become: "How quickly can I put together a succession plan and head into retirement?" The answer depends on a number of factors.

Partners plotting a path to retirement need to compare the frequency that they meet in person with their clients to how many more years they desire to work full time before slowing down.

Note the phrase "work full time before slowing down." Many practitioners focus on when they want to retire, but most owners don't go from full time to retirement in one step. Instead, they gradually reduce their time commitment to the firm. Thus, the focus when determining the timing of a succession plan should not be on when the partner plans to retire but on when the partner plans to slow down.

This is a crucial point when combined with the need to understand how often partners meet in person with their clients. Face-to-face meetings used to take place multiple times per year, but not anymore. More than 85% of accounting firm clients meet in person only once a year with the owner or partner. Communication still occurs on a regular basis, but it's in the form of phone calls, email, and, in the case of some firms, via video conference technologies including Skype. The increasing popularity of portals and internet-based accounting systems allows firms to access clients around the world, tearing down geographical barriers but making it harder

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to meet in person. As a result, look for the frequency of face-to-face meetings to decrease further.

This is important because face-to-face meetings are the best way, in the authors' opinion, to work through the transition of clients to the successor partner or firm that a departing CPA would like to handle those clients' accounts in the future. Consider what that means for partners who want to reduce their time commitment to the firm in the next five years. Half a decade might seem like an eternity, but for most partners, it's only five visits with each client. A two-year window allows for only two visits.

> Face-to-face meetings are the best way to work through the transition of clients to the successor partner or firm.

Brand Loyal or Partner Loyal?

The next factor in calculating the time to retirement is honestly determining whether clients are brand loyal or partner loyal. Generally speaking, the smaller the firm, the better the chance that clients are partner loyal. If clients are partner loyal, it likely will take longer to transition them and execute a successful succession.

Most large firms assume all their clients are brand loyal, but in almost all cases, at least some clients are more attached to an individual than to the firm. Firms need to factor this in when designing succession and transition plans. Avoid treating all partners the same under the plan. Client loyalty can vary by partner.

Smaller firms frequently find it more challenging to make their clients brand loyal, because in many cases a single partner has developed and managed the clients during their entire relationship with the firm. Getting clients acclimated and comfortable with other team members can help mitigate this issue, but it rarely disappears.

There are always other factors that influence the timing behind commencing a succession plan. For example, if a partner in a firm has a very specific skill set, it will likely take longer to identify and potentially train a successor. All told, it usually takes a minimum of two years to transition a client from one partner/owner to the next.

Lease Considerations

A key issue that too few firms consider in the succession planning process is leases. Consider this real-world example: A four-partner firm with $4 million in annual revenue wants to merge with a larger firm that can facilitate long-term growth for two partners but near-term succession for the other two. The two partners staying on have the desire but not the capacity to replace the two senior partners. The firm recently signed a 10-year lease extension and enjoys a well-appointed space, great location, parking, and rent at below market value.

What's the problem? The firm is targeting suitors ranging from as small as $8 million in revenue to top 100 status. Firms that size already have offices. Firms considering a merger or sale should avoid tying potential successor firms to a lease. By signing the 10-year lease, the firm in this example eliminated from its list of potential buyers all the firms that don't want a satellite office, especially if a potential buyer already has an office in the same area. Potential buyers are likely to reduce their purchase offer to account for the costs of carrying the additional overhead of the lease.

> All told, it usually takes a minimum of two years to transition a client from one partner/owner to the next.

EXECUTIVE SUMMARY

- **Partners assessing how quickly they can retire need to factor in how frequently they visit with clients.** More than 85% of accounting firm clients meet face to face with their CPA only once a year.
- **Most CPA firm owners don't go from full time to retirement in just one step.** Consequently, partners should think in terms of how much time they have left before they want to reduce their time commitment to the firm, as opposed to when they want to retire.
- **Firms need to assess whether clients are partner loyal or brand loyal.** Clients who are more loyal to a partner than to the firm take longer to transition to other professionals in the firm. It usually takes at least two years to transition a client from one partner to another.
- **Firms should avoid locking themselves into long-term leases,** which can hurt the possibilities of making an external sale to fund retirement for a partner or partners. Outside buyers that already have an office in the market where the selling firm is located will not want to assume a large, long-term lease. Having one on the books can scuttle a deal or lead to a lower purchase price.

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To comment on this article or to suggest an idea for another article, contact Jeff Drew, senior editor, at jdrew@aicpa.org or 919-402-4056.

Conclusion

The time for succession planning is now. Firms that don't have a plan in place are in danger of seeing opportunity and firm value melt away as the number of firms seeking buyers rises over the next few years. CPA firm partners need to understand the realities of the succession landscape and plot an appropriate course for a gradual transition into retirement. Failure to plan properly could prove costly for firms and partners alike. ❖

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■ "Planning and Paying for Partner Retirements," April 2012, page 28
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■ "Accounting Firm M&As: A Market Update," Nov. 2010, page 30
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