Succession Planning

Module 8

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8.1 Introduction

As professional accountants grow older, their thoughts inevitably turn to their exit—not only from the firm, but from practicing accountancy altogether. As they consider their departure from business life, they wonder if the firm they have built up will have value in someone else's eyes.

It has provided them with an income stream over the years, and allowed them to serve the community. They have built relationships with clients over this time, helped them, served them and supported them. Yet the question remains, will the firm be worth anything to anyone else? And if so, how much and to whom?

A succession plan allows for the orderly exit of the practitioner. This means it is not left to chance, and there is a plan in place. This gives a degree of comfort to those involved, particularly staff.

This module considers these questions and many more. Its objective is to assist you in coming to terms with the issues you need to consider and to help you get "succession-ready."

8.2 Succession Planning for the Sole Practitioner

The number of issues currently facing the profession has been well documented and covered in previous modules. These include:

- The aging of the profession;
- Trouble attracting and retaining staff;
- Compliance and regulatory pressures;
- Time pressures on sole practitioners; and
- Client requirements at a high level, which means practitioners have little time to focus on their succession plan requirements.

In addition, a large percentage of accounting firms are one- to two-partner firms. This is what the practitioners wanted, but many sole practitioners will need to consider taking on partners as part of their succession plan. Many will find this difficult, as they will have been on their own for many years. This may seem contrary to the whole philosophy of operating as a sole practitioner.

If anything, this highlights the fact that the sooner the succession plan is underway, the sooner these issues can be dealt with.

This module provides checklists and resources to assist in this process. In this module, the term "succession planning" is used essentially in the context of firm exit.

8.3 Developing Your Succession Plan

One of the most common questions asked by practitioners as they begin to consider succession planning is, "Will someone pay me for this firm?" The answer is usually "Yes," but the answer to the question, "How much?" depends on a number of factors.

8.3.1 Understanding Your Firm

One of the best ways to enhance the value you realize on exit is to plan for it in a structured manner. Table 8.1 sets out pertinent considerations for those thinking of retiring. The answers to these questions will help you determine the approach you should take with your succession, and also help you assess which of the potential options you should consider.

Table 8.1 Understanding you and your firm better

	Question	Response/Action
1.	What options do I have?	
2.	What needs to be done to make it all happen?	
3.	What would I like to see happen to my clients?	
4.	What would I like to see happen to my staff?	
5.	What restraints of trade will I find acceptable?	
6.	When should I start talking to potential purchasers/ partners?	
7.	How much do I think my firm is worth?	
8.	How much is my firm really worth?	
9.	How much money do I want to exit with?	
10.	Do I enjoy working with others, or prefer working on my own?	
11.	How long will I need to stay involved in the firm after I sell my interest?	
12.	Whom should I start talking to about buying my interest?	
13.	Are any of my staff potential purchasers?	
14.	How profitable is my firm?	
15.	What systems, procedures and processes do I need to put in place to enhance the performance of my firm?	
16.	Would my firm represent a worthwhile investment to someone else?	

Once you have answered these questions, you need to review the rest of this module to gain an understanding of the succession options available. This module discusses eight such options in detail. At least one of these will stand out to you as the preferred option. You should plan to position your firm in such a way as to maximize the return you can achieve by pursuing that option.

8.3.2 Your Future Purchaser

Whichever option you choose, if you plan to sell one day, you must always be mindful of your future purchaser. Your future purchaser will need to have the following questions satisfied:

- Is this a good investment?
- Will it provide me with a good return on my investment?
- Does it represent good value?

The first step in succession planning is to get your firm “succession-ready.” The best way to do this is to consider the questions a potential purchaser, or future partner will ask. You should then develop your firm in such a manner as to be able to give strong, positive answers to these questions.

A purchaser will typically assess their purchase against the criteria shown in Table 8.2.

Table 8.2 Purchaser considerations

Area	Level	Analysis	Response
Fees	History of fee levels	What have fees been over the last one, three, and five years?	
		Calculate and assess growth over these years.	
	Maintainability of fees	Will fees be maintained?	
		Is there evidence of sustainable cash flows?	
		What evidence exists to support this?	
	Impact of non-recurring fees	Identify non-recurring fees.	
		Assess impact on expected future maintainable fees.	
Profitability	History of profits	Identify profits over last one, three, and five years.	
	Maintainability of profits	Will profit levels be maintained?	
		What impact will the succession event have on profits?	
	Impact of non-recurring fees on profits	Identify non-recurring profit component.	
		Assess as to impact on recurring profit.	
	“Add backs” of non-operating expenses	Identify non-business expenses.	
		Add back non-operating expenses to assess operating profitability from a business perspective.	
		Items may include excessive wages to owner, travel and accommodation, utilities.	
		Assess normalized profit against purchase criteria.	
Debtors	Debtors position	Review debtors.	
		Review and assess bad debts.	
		What are current levels of bad debt write-offs?	
		What are expectations for future?	

Area	Level	Analysis	Response
	Debtors control process	Identify current debtors control process.	
		Identify collections history.	
		Assess effectiveness.	Adjust as appropriate.
Work in progress (WIP)	WIP position	Review WIP.	
		Assess WIP and likelihood of converting to fees and collection.	
		What are current levels of write-offs and expectations for future?	
	WIP control process	Identify current WIP control process.	
		Assess effectiveness	Adjust as appropriate.
Client base	Stability of client base	Assess client numbers over last three years.	
		Check number of clients acquired over last three years.	
		Check number of clients lost over last three years.	
	Spread of clients	Check spread of clients across industry sectors.	
		Check size of clients; that is, turnover, number of employees, etc.	
	Age of business owners in client base	Check age of business owners in client base. If close to retirement age, this will likely have an impact on future earnings of firm.	
Dependency	Clients	Check for dependence on any one client, or few clients.	
	Industry	Check for dependence on any one industry, or few industries.	
	Practitioner	Check for dependence on existing practitioner, from both clients and staff.	
Staff	Quality of existing staff	Assess for competence and ability.	
		Assess qualifications and experience.	
		Review and assess billings history.	
Systems	Internal infrastructure	Assess internal infrastructure, processes, systems, quality control procedures.	

Area	Level	Analysis	Response
Compliance	Government regulator	Identify any outstanding issues.	
		Assess impact on new owners.	
	Government tax department	Identify any outstanding issues.	
		Assess as to impact on new owners.	
Weighting	Value of top five clients as percent of fee base	Identify top five clients.	
		Determine their fees.	
		Total these and calculate as a percentage of fee base.	
Transition	Handover process	What is the “handover” process?	
		How long is vendor prepared to stay for handover?	
		Look for planned approach, which should include:	
		Strategy for handover;	
		Strategy for communicating with key clients, e.g. meetings to be held with each;	
		Communication strategy for balance of client base;	
		Strategy for communicating with existing staff, e.g., team meeting; and	
		Training on systems and procedures.	
	Restraint	Assess restraint of trade conditions.	
		Assess non-compete issues.	
	Ethical	Assess as to existence of ethical issues within client base which may impact on ethical position of firm.	

8.3.3 Succession Plan

Whichever succession option you choose, your firm may need to improve its financial position to be a more attractive investment option for potential purchasers.

There are typically a number of key areas in which a firm can improve and which will have a positive impact on financial performance. It is important that these improvements have been implemented and are ingrained in the firm before putting the firm up for sale.

Key areas for firm assessment include:

- Revenues;
- Profitability;

- Liquidity;
- Debtor control;
- Work in progress control; and
- Growth.

Other modules discuss approaches to improving these areas.

8.4 Selecting Your Succession Option

It is important to consider which succession option is most naturally attractive to you and which you think will maximize your final settlement amount. There are three to choose from.

- The first is joining with others and becoming larger. This ensures you have others who are in a position to buy you out. These options are covered in Section 8.6, and include partnership, consolidation, and merger alternatives.
- The second is selling off the firm, whether in total, or selling a fee parcel at a time, or on a progressive sell-down basis. These options are considered in Section 8.7.
- The third is a series of internal options, which are covered in Section 8.8 and include internal succession, the introduction of new partners and sale to existing partners.

Each option is quite distinct and brings its own set of considerations. As Table 8.3 shows, a number of issues apply to each.

Table 8.3 Issues to consider when selecting your succession option

	Issue	Comment	Response
1.	Planning	Set date for completion. Discuss with key stakeholders. Identify checklists to complete.	
2.	Taxation	Consider tax implications of alternative options. Identify any reorganization of entity structures required. Put in place new structures within time frame requirements.	
3.	Funding	Consider funding requirements for your exit. Organize financial arrangements as required. Introduce topic of funding early in discussions with potential purchasers to ensure capacity.	
4.	Exit	Consider full impact of your exit from the firm. Consider strategies to ensure minimal disruption to ongoing firm performance. Implement strategies to ensure effective handover on your final exit.	

8.5 Valuation Methodologies

8.5.1 Introduction

The valuation of your firm is an important step in your succession plan. If one of your objectives is to maximize the amount you receive at settlement when you leave, you should focus on ensuring that this valuation is as high as possible. By understanding the component parts of the valuation methodology, you can concentrate on those areas that need to improve.

It is well established that valuation is more of an art than an exact science, albeit with sound methodology behind it. It is also important to be clear on the definition of the actual valuation. The technical definition would be, "The fair market value is the price that would be negotiated in an open market between a knowledgeable, willing but not anxious buyer and a knowledgeable, willing but not anxious seller dealing at arm's length." This would correctly establish the fair market value, but may be different from the amount which is finally paid.

There can be many reasons for this, including external factors beyond the control of the parties. These would include factors such as the economic climate, interest rates and the supply and demand of firms for sale at that particular time.

It may also include other factors over which the parties do have control, such as the state of readiness the firm is in at the time of sale, the internal systems and procedures, the level and capability of staff, or the financial position of either the vendor or purchaser.

Value is usually a function of profitability multiplied by a "multiple," where the multiple takes into account growth prospects, risk, quality of earnings, and other factors discussed throughout this module. However, it is also wise to consider the synergistic benefits available to potential purchasers. This could be the elimination of a competitor, opening a new market, or adding fees to an existing cost base.

To maximize value, it is important to recognize such factors and incorporate them into your strategy for the future sale of the firm. At the same time, it is important to acknowledge the areas over which you do have control, and put strategies in place to improve these.

It may take a number of years for these strategies to have an impact on the value of the firm, which highlights the need to start the succession process early.

8.5.2 Valuation Methods

The traditional methods used in business valuation include:

- Capitalization of future maintainable earnings;
    - value is based on expected future earnings, relative to the risk return expected, where a capitalization rate, or multiple, is applied against an estimate of future maintainable earnings,
- Rule of thumb, or industry method;
    - value is based on an "industry standard" applied to each firm, with the value expressed in terms of a multiplier, or cents in the dollar.
- Net book value;
    - value is simply based on the net book value of the assets of the firm.
- Discounted cash flow
    - value is based on estimated future cash flows discounted to give their present values, where the discount rate used reflects the risk of the expected future.

The most commonly used method is the capitalization of future maintainable earnings method, followed by the rule of thumb method. Where partnership agreements are in place, the agreement would normally nominate the valuation formula to be applied and identify certain key components, such as number of years' earnings to be included and capitalization rate to be used.

8.5.3 Capitalization of Future Maintainable Earnings

This is a widely used method for valuing accounting firms.

This methodology seeks to determine the current value based on expected future earnings, relative to the risk return expected.

There are two key elements in this model.

The *capitalization rate* is the rate that will be applied to the earnings to determine the value. It is essentially an application of the price/earnings ratio. It is not a precise figure that can be applied universally, as each situation will be different. However, it is often within a range that takes into account the particular circumstances of a case.

Future maintainable earnings is an estimate of the earnings the firm will generate on a maintainable basis into the future. Earnings from the recent past are taken as a guide. Traditional accounting firms with a strong audit or compliance base tend to have a high level of recurring income. This provides them with strong earnings potential, as their clients come back year after year.

Other factors that will impact earnings need to be taken into account, such as the loss of a key client, or the introduction of new services. Also, non-recurring income is identified and removed from the calculation.

This approach can be expressed as a formula:

$$\text{Valuation} = \frac{\text{Future maintainable earnings}}{\text{Capitalization rate}}$$

8.5.3a Capitalization Rate

The capitalization rate is essentially the return on investment that the valuer expects from that particular investment. Factors to consider include:

- The current "risk free" rate of return available in the market, usually the government bond rate;
- Bank interest rates;
- Price earnings ratios of publicly listed shares;
- Ability to re-sell the firm, supply of ready buyers;
- Industry and business risks;
- Length of time the firm has been operating;
- Impact of technology on the firm;
- Where the firm is in its business life cycle;
- Dependency on clients, staff, or practitioner;
- Impact of any regulation changes; and
- Comparative rate used in comparative firm sales.

The starting point is the risk-free rate, which is then adjusted according to consideration of factors influencing the rate, such as those listed above. A common way to express the capitalization rate is to invert it and refer to it as the "multiple." That is, 1/Capitalization Rate is the multiplier.

8.5.3b Discounted Cash Flow

Discounted cash flow is a valuation approach that determines what someone is willing to pay today in order to receive the anticipated cash flow in future years. Essentially it means converting future earnings into today's money. The future cash flows are discounted in order to express their present values to properly determine the value of the investment under consideration.

The discounted cash flow or DCF approach describes a method of valuing an investment using the concepts of the time value of money. All future cash flows are estimated and discounted to give their present values. The discount rate used is generally the appropriate weighted average cost of capital that reflect the risk of the expected future cash flows. The discount rate reflects two things:

- The time value of money. Investors would rather have cash immediately than have to wait; therefore, they must be compensated by paying for the delay.
- The risk premium. This reflects the extra return investors demand because they want to be compensated for the risk that the cash flow might not materialize after all.

The DCF for the purchase of an accounting firm is calculated by estimating the investment you will have to make at the start and the return you think you will receive. The timing for when you expect to receive the payments also needs to be estimated. Each transaction then needs to be discounted by the opportunity cost of capital over time between now and when you expect to receive the return on your investments.

8.5.4 Rule of Thumb

The rule of thumb valuation method applies an "industry standard" to each business within that industry. It is typically expressed in terms of a multiplier, or cents in the dollar. It is applied to either the net earnings of the business, that is, earnings before interest and tax (EBIT), or to its turnover.

For instance, accounting firms may apply a certain level of cents in the dollar to their gross fees. This valuation method is popular for smaller firms, where other factors affect the valuation decision. Likely purchasers of fees at this level are sole practitioners looking to enter business at a low fee level. Essentially, they want to "buy a job," and are prepared to pay a higher price for the fees than the price point at which traditional methods would value them.

If there is a high reliance on low-value work, such as income tax return preparation, they tend to be toward the lower end of this price range. If there is a strong recurring base of business client work, it tends to be at the higher end of the price range.

The main drawback to adopting the rule of thumb approach is that it assumes all firms are run and managed in the same way. It assumes clients interact the same way and pay their bills in similar ways, and the cost structure of the firm is the same. Clearly this will not be the case, but even so, this method is fairly widely used. The main reason is its simplicity; it is also widely understood.

8.5.5 Net Book Value

The net book value valuation method is used where there is unreliable profit and loss information or where the business being valued is trading at a loss. If it is trading at a loss, the future maintainable earning method cannot be applied.

This method may be appropriate in situations where vendor and purchaser agree that there is some value in the firm but that this will not be realized from future earnings. The value is essentially held in the balance sheet, and both parties agree to accept that as the starting point. It is mostly used in those situations where the firm is asset rich but earnings poor.

In such situations, it is advisable to engage an independent valuer for the assets of the business, because the assets are likely to be stated at historic cost value, and depreciation is likely to be charged at tax rates, not useful life. The written-down book value may be quite different from the market value in such cases.

8.6 Options for Partnerships, Consolidations, Mergers, and Acquisitions

One succession pathway is to join others and become larger. This may allow the practitioner to become a more attractive investment target, or provide a ready pool of fellow partners who are in a position to buy out the practitioner. There are a number of structures to consider.

1. Partnership

Two or more people carry on business in common with a view to a profit. Rules relating to partnerships include joint ownership, participation in gross returns, sharing of profits and losses, and the exercise of partners' rights. One of the key issues in a partnership is joint and several liabilities of all partners; this will be subject to your country's laws or professional regulations.

2. Consolidation

A larger company purchases a number of smaller firms and "consolidates" them into one larger entity, seeking to achieve operating efficiencies and cost savings. The consideration is usually a combination of cash and shares in the larger company. The shares in the larger company are typically held in escrow and cannot be sold until a prescribed time period has elapsed. Consolidators are typically structured in a corporate model, with external investors, board of directors, chief executive officer and management team.

3. Merger

Two firms combine to make one larger firm. It works best when the two firms are of similar size; otherwise it tends to be more of a takeover. The equity of each partner in the combined firm is typically based on the proportionate value of the fees going in.

As you can see, there is a common thread running through each of these structures: the coming together of existing businesses and structures. Note that the issues involved in working with others in joint ownership are quite different from issues relating to the sale of a firm, or the sale of fee parcels, which are covered later. As such, there are a large number of issues common to partnerships, consolidations and mergers, which need to be considered prior to the actual event.

8.6.1 Thinking About Shared Ownership

For many sole practitioners, the idea of sharing the ownership of their firm is contrary to the philosophy of their professional careers. Some may have been involved in or worked in partnerships previously and decided it was not for them. Others may simply have decided to be on their own from the start. One thing is certain: being involved in a partnership, consolidation or merged firm is distinctly different from being a sole practitioner.

Accordingly, prior to becoming involved in such structures, the practitioner should self-assess their aptitude and carefully consider the questions in Table 8.4.

Table 8.4 Self-assessment questionnaire for those considering partnership, consolidation or merger

	Question	Response Comment
1.	Do I really want to share decision-making, control, and profits with others?	
2.	What am I really getting myself involved in?	
3.	Do I want to share ownership of the firm?	
4.	Does the upside of shared ownership outweigh the downside?	
5.	Can I trust my partners?	
6.	Will they work as hard as I do?	
7.	How much money will I make?	
8.	Will I make more in the new structure, or less?	
9.	What are the key reasons I am doing this?	
10.	Have I considered the advantages and disadvantages of each? What are they?	

If you have decided that this is the most suitable succession pathway, it is important to consider each option in greater detail.

8.6.2 Partnership/Merger

In the context of succession, there are two important steps in the partnership or merger process. The first is the challenge of the partnership or merger itself. The second is the exit of the practitioner. Remember that the main reason for choosing this option is to enable your exit from the firm.

It is important that all partners have a clear understanding of this from the outset and clear expectations. It is essential that the partnership agreement takes this into account and documents how and when the exit is to occur. The partnership agreement should also deal with valuation issues. The value on exit is typically determined by the value of the partnership or the merged firm, unless prior agreement has been reached among the partners.

There are a number of advantages and disadvantages of partnerships and mergers.

Advantages

- Expected economies of scale;
- Broadening of experience and skill base within firm;
- Potential broadening of services offered to the market;
- Cost savings proceeding from reduction in duplication of resources;
- Broadening of knowledge pool from which firm can draw internally; and
- Larger pool of resources from which firm can pay out exiting partner.

Disadvantages

- Challenges of aligning firm cultures;
- Practitioners' sense of loss of control;
- Discomfort with shared decision-making and profit sharing; and
- Lack of enjoyment in working with partners after merger takes effect, therefore lower professional satisfaction than previous situation.

Appendix 8.1 (Partnership/merger checklist) provides a useful framework to work with as you consider these issues.

One of the key issues to remember when considering a partnership or merger is the need for compatibility between the partners of the new firm. The ability of partners to work together in a harmonious and productive manner cannot be underestimated. Many mergers never materialize because at the end of long talks the partners discover they are not meant for each other, or believe they could not work together. Even though significant time, effort and resources may have been spent on the process up to this point, it is an important conclusion to reach and may well save much grief in the future.

8.6.3 Consolidation

From a succession perspective, the consolidation model is very attractive. This is particularly the case where the consolidator is a publicly listed company. It is often a win-win situation: the practitioner wins by having a ready market of investors to purchase shares after the escrow period. The consolidator wins by ensuring the practitioner stays motivated to generate profits and facilitate a smooth transition of clients, as otherwise this will have a negative impact on share value, and hence the firm's future value.

There are a number of advantages and disadvantages to the consolidation model.

Advantages

- Ready market of investors to buy shares after escrow period;
- Larger firm infrastructure of consolidator that can benefit and assist the practitioner;
- Structured training and development program;
- Career path for staff of practitioner; and
- Large knowledge pool from which the practitioner can draw.

Disadvantages

- Challenges of aligning firm cultures;
- Practitioners may feel sense of loss of status, autonomy and control; and
- Practitioner may be uncomfortable with regular performance checks.

Appendix 8.2 (Consolidation checklist) provides a useful framework to work with as you consider the issues involved.

Objective for vendor

Your objective as a vendor is to make your firm as attractive an investment as possible. Do all you can to ensure you maximize the return you get for the investment you have made over the years. This will also let you maximize the return available to the purchaser.

Action plan

As you review the above list, you may think of improvements you can implement immediately in your firm to start getting succession-ready.

8.7 Sale of Firm, Fee Parcel or Progressive Sell-Down

8.7.1 Sale of Firm

Sale of firm is the most common succession option. This is where the whole firm is sold to a new purchaser. Potential purchasers who consider the purchase of an existing firm an attractive option include:

- First-time entrants to public practice;
- Employees from another public firm looking to go into business on their own;
- An employee or employees from your own firm;
- Another firm of smaller or similar size looking to increase their critical mass and achieve economies of scale; and
- A larger firm looking to increase its fee base, and/or looking for geographic presence.

In a sale to an existing staff member, it is likely that they will continue to operate the firm in much the same way initially, with only minor changes. Other improvements are likely to be introduced on a staged, progressive basis, particularly if you are still involved in the firm and the new owners do not wish to disturb you.

A larger firm is unlikely to seek your infrastructure or systems. It is more likely they want your client base and recurring income stream. They will probably also be interested in your staff who have client relationships and institutional knowledge and history.

As part of their due diligence, most purchasers will consider issues such as those raised in Table 8.2, earlier in this module. You should ensure your firm has been developed in such a way as to give strong, positive answers to these types of questions.

Typically the purchaser wants the business assets, not the existing business structure. This includes plant, equipment and goodwill. The debtors, work in progress and creditors are usually retained by the vendor.

The sale of a firm has advantages and disadvantages for the vendor.

Advantages

- Ongoing commitment to firm ceases once handover period and agreed obligations are met;
- Once the money is banked, the transaction is over, and the vendor's involvement ends;
- There is a certain amount of professional satisfaction for the vendor in knowing that they ran a business of sufficient value to be saleable; and
- Sense of finality, knowing the transaction is complete.

Disadvantages

- Once sale is complete and professional involvement ceases, it may take some time for vendor to adjust; and Appendix 8.3 (Sale of firm checklist) provides a useful framework to work with as you consider these issues.

Objective for vendor

Your objective as a vendor is to make your firm as attractive an investment as possible. Do all you can to ensure you maximize the return you get for the investment you have made over the years. This will also ensure you maximize the return available to the purchaser.

Action plan

As you review the above list, you may think of a number of improvements you can implement immediately in your firm to start getting succession-ready.

8.7.2 Sale of Fee Parcel

The sale of a fee parcel is more straightforward than the sale of a firm, as the fee parcel is the asset being purchased. There are typically no other assets sold or transferred at this time.

There are a number of potential purchasers who consider the purchase of a parcel of fees an attractive option:

- First-time entrants to public practice;
- An employee or employees from your own firm;
- An employee or employees from another public firm, looking to go into business on their own; and
- Another firm looking to increase their critical mass and achieve economies of scale.

The sale of a parcel of fees has advantages and disadvantages for the vendor. These include:

Advantages

- Can select which clients to parcel and sell off;
- Can continue with firm, albeit on a lesser scale;
- May allow for specialization, by selling off clients outside areas of key interest; and
- May also allow vendor to reduce other costs, as resources required to service remaining clients may not be as great.

Disadvantages

- May lose professional relationship with those clients included in parcel which is sold off; and
- Some clients may not wish to move to another accountant, which reduces the sale price accordingly. Appendix 8.4 (Sale of fee parcel checklist) provides a useful framework when you are considering these issues.

Objective for vendor

Your objective as a vendor is to make your parcel of fees as attractive an investment as possible. Do all you can to ensure you maximize the return you get for the investment you have made over the years. This will also ensure you maximize the return available to the purchaser.

Action plan

As you review the above list, you may think of improvements you can implement immediately in your firm to help you get succession-ready.

8.7.3 Progressive Sell-Down

This is where the vendor progressively sells down a percentage of his or her equity in the firm. This means that during the time of sell-down there is a partnership in place, even if it is limited to the period of the sell-down.

This option is of interest to vendor practitioners who do not wish to abruptly cease their professional careers, and who may wish to withdraw progressively, from active service.

There are a number of potential purchasers who are typically interested in this option:

- New entrants to public practice, who want to take the incremental approach to equity ownership, as their confidence and knowledge increase;
- Existing staff members, who take on greater equity as their confidence increases, and as their borrowing capacity allows; and
- Another firm, who wishes the vendor partner to stay on for an extended period to assist with client transition and handover.

Finance considerations may also be a factor.

This can be one of the most delicate and sensitive succession options, as the purchaser and vendor will need to work together for the period of sell-down. It is in the best interests of both parties to make it work; however, it can be an emotionally charged time.

Issues typically include:

- Vendor still involved, but conscious that their reign is coming to an end;
- New partners with lesser equity may want certain things to change, but the senior partner still controls the votes; and
- Vendor partner may have run the firm as a sole trader for many years, and struggles with dealing with new partners.

The progressive sell-down has advantages and disadvantages for the vendor.

Advantages

- Vendor continues to remain involved in firm;
- Allows purchaser to take up equity in incremental steps; and
- Existing partners may take up additional equity on progressive basis.

Disadvantages

- Can be an emotional time as vendor partner comes to terms with their pending departure; and
- As sell-down period may take years, all parties must ensure they can work together for the time required. Appendix 8.5 (Progressive sell-down checklist) provides a useful framework when you are considering these issues.

Objective for vendor

Your objective as vendor is to make your firm as attractive an investment as possible. Do all you can to ensure you maximize the return you get for the investment you have made over the years. This will also ensure you maximize the return available to the purchaser.

Vendors are often concerned that the interests of their clients and staff will be taken care of. This should be discussed fully with potential purchasers.

Action plan

As you review the above list, you may think of improvements you can implement immediately in your firm to help you get succession-ready.

8.8 Developing Internal Succession Plans

As discussed in Module 4, the third pathway of succession planning focuses on internal options:

- Internal succession;
- Introduction of new partners; and
- Buyout by existing partners.

8.8.1 Internal Succession

The main focus of internal succession is assisting senior staff in progressing to partnership. It is most effective when there is a deliberate strategy in place and the objective is clearly communicated.

From a succession perspective, it manages the retirement of partners through the appointment of new partners. To be successful, it requires that the firm have the following four attributes:

- Firm growth sufficient to allow for another partner;
- Recruitment of willing and capable staff;
- Development program for managers and senior staff; and
- Firm performance that is attractive to aspiring partners.

Such a process allows for succession to be handled in a managed way, and provides for the progressive handover of control of the firm, and the client base.

Advantages

- Incoming partners have familiarity with firm culture and client base;
- Staff and internal systems and procedures are well known;
- An existing business model is operational and already in place; and
- There is minimal disruption to existing clients, staff and internal arrangements, systems and procedures.

Disadvantages

- Gaining respect in new position from long-term staff; and
- Incoming partner may have limited exposure to other accounting firms.

Appendix 8.6 (Internal succession checklist) provides a useful framework when considering these issues.

Objective for vendor

Your objective as vendor is to make your firm as attractive an investment as possible. Do all you can to ensure you maximize the return you get for the investment you have made over the years. This will also ensure you maximize the return available to the purchaser.

Action plan

As you review the above list, you may think of improvements you can implement immediately in your firm to help you get succession-ready.

8.8.2 Admission of New Partners

This applies where an existing partnership is already in place. The exit of one partner will still leave one or more partners at the firm. The idea is to find a replacement partner for the retiring partner, sourced externally from business practice or commerce.

There are a number of risks associated with this strategy, mostly to do with managing the transition of the retiring partner while dealing with the introduction of an incoming partner. Once the prospective new partner has been identified and agreement has been reached, there is a higher success rate when the incoming partner commences twelve months prior to the exit of the retiring partner.

Advantages

- An existing business model is operational and already in place; and
- There is minimal disruption to existing clients, staff and internal arrangements, systems and procedures.

Disadvantages

- Issues may arise with assimilation of new partner into existing firm culture; and
- Some of the existing partners may have wanted to take up equity.

Appendix 8.7 (Admission of new partners checklist) provides a useful framework when considering these issues.

Objective for vendor

Your objective as vendor is to make your firm as attractive an investment as possible. Do all you can to ensure you maximize the return you get for the investment you have made over the years. This will also ensure you maximize the return available to the purchaser.

Action plan

As you review the above list, you may think of improvements you can implement immediately in your firm to help you get succession-ready.

8.8.3 Buyout by Existing Partners

This succession option allows for the buyout of the retiring partners by the existing and remaining partners. The remaining partners take up the shares of the retiring partner under pre-emptive rights, or under separate arrangements made between the individual partners.

Normally, existing shareholders are first offered the opportunity to take up the available shares in proportion to their existing shareholding. If there are still shares remaining after this offer, then it is left to individual negotiations between partners.

The partnership or shareholders' agreement would normally outline the process to be followed. It should also contain the valuation model and methodology to be used.

Advantages

- This is an internal negotiation, and has no impact on those outside the existing partnership;
- It provides certainty of position to all partners if the partnership agreement has taken this option into consideration;

- There is minimal disruption to existing clients, staff and internal arrangements, systems and procedures; and
- An existing business model is operational and already in place.

Disadvantages

- May cause financial stress to existing partners; and
- Ongoing reduction in total number of partners in firm, unless new partners are admitted.

Appendix 8.8 (Buyout by existing partners checklist) provides a useful framework when considering these issues.

Objective for vendor

Your objective as vendor is to make your firm as attractive an investment as possible. Do all you can to ensure you maximize the return you get for the investment you have made over the years. This will also ensure you maximize the return available to the purchaser.

Action plan

As you review the above list, you may think of improvements you can implement immediately in your firm to help you get succession-ready.

8.9 Exit Considerations

Whichever option for succession you have decided on, the day will come when you leave your firm. Such an event will undoubtedly carry with it many mixed feelings. However, you will have planned for it, and will be ready to move on.

There are a number of issues you should consider before the big day occurs.

8.9.1 Taxation Implications

Subject to your country's laws or professional regulations, your exit from your firm is likely to have several taxation consequences. For this, your last big transaction, do everything in your power to minimize the taxation impact.

Ensure that you have arranged your affairs in such a manner as to allow you to take the most advantage from the rules in place. This may involve the establishment of alternative structures. It may also require you to operate in a certain manner for a prescribed period of time. Be aware of the laws and professional regulations that govern these transactions, and strive to maximize your advantage.

8.9.2 Constraints of Trade

You will almost certainly be required to sign some form of constraint of trade when you exit your firm. This is a very common business practice. The purpose is to provide some level of certainty to the purchaser that their investment is secure.

Constraints of trade usually cover a number of key areas. They typically apply for a prescribed period of time during which you are restrained from setting up a similar business to the one you have just left. They also typically apply to a geographical distance from your previous firm. These contracts are enforceable by law if they are considered to be in line with reasonable business practice.

If the constraints are considered excessive, they can be challenged in court. The basic principle is that a restraint of trade cannot prevent you from earning a living from your skills and training. Constraints that are overbearing or enforce too much restriction will likely be considered extreme and therefore unenforceable.

8.9.3 Lifestyle Changes

Perhaps the most difficult aspect of succession is the dramatic lifestyle changes that occur after leaving a firm. Many people have worked long hours for many years. Many have foregone holidays and weekends in order to work on client matters. Work has given them meaning in life, stature in their communities, and a feeling of being wanted and needed. Many practitioners know that if it weren't for them, their clients would be in all sorts of trouble with the regulators.

And then it all stops.

The phone stops ringing, the clients stop hassling, the emails go quiet. Your former clients no longer ring you for advice, because they now deal with your successor. Most of the issues are handled, and your firm seems to be able to continue quite well without you.

You would be entitled to feel slightly upset that the world did not crash without you at the helm!

Unfortunately, many practitioners fail to move on and find new interests. They live in the past, reliving their glory days. This is not a healthy strategy.

It is important that you give as much thought to "life after firm" as you did to life in the firm. This will let you move on to the next stages of your life in full mind and spirit, able to enjoy every moment. Take the time before your exit to think of other interests you might like to explore. What are the things you always wanted to do? You might finally now have the chance to do them.

If you give this serious thought before your exit, you will be well placed to make the most of all the opportunities that come your way.

8.9.4 Compliance Issues

When you finally leave your firm, there will undoubtedly be a range of compliance issues that need to be attended to. Appendix 8.9 (Compliance issues checklist) provides some guidance as to the areas you may need to attend to.

8.10 Conclusion

This module has covered many of the areas you should consider when making your succession plan. As it is likely to be one of the most significant occasions in your practice life, it is of great importance that you plan for it very carefully. This final chapter sets out the options that are available to you and suggests ways to organize your path toward retirement from the firm.

The various firm valuation methodologies are discussed, together with a consideration of internal and external strategies to think about. The Appendices provide a number of checklists that can be used according to the succession option you decide on, to help you take all the relevant issues into account.

The module ends with a discussion of steps to be considered as part of your eventual exit from the firm. If these steps are followed, they should ensure that the succession plan is well developed and in place and that you, as a retiring practitioner, can look forward to a busy and interesting time, knowing that your firm is in good hands and will continue as a profitable entity.

8.11 Further Reading and IFAC Resources

The IFAC Global Knowledge Gateway is a digital hub where professional accountants can easily access thought leadership and resources from IFAC, member organizations, and other notable groups and individuals.

The Gateway Practice Management section includes additional articles, videos, and resources to complement this module. We encourage you to review the content, provide feedback, engage with contributors, and share your own insights on contemporary practice issues.

Appendix 8.1 Partnership/Merger Checklist

	Issue	Response	Date
1.	All parties to sign confidentiality agreement.		
2.	List terms and conditions required on merger.		
3.	Agree on new entity structure.		
4.	Agree on management, dispute resolution, exit provisions, valuation formula, and capital investment.		
5.	Agree on services to be provided.		
6.	Agree on decision-making process.		
7.	Determine process for deciding on managing partner.		
8.	Develop partnership/shareholders agreement.		
9.	Determine partners' remuneration.		
10.	Determine partners' access to profits.		
11.	Agree on charge-out rates.		
12.	Agree on target client profile.		
13.	Agree on process for any existing clients outside of new client profile.		
14.	Determine time period allowed and scope of due diligence on each other's firm.		
15.	Agree on valuation of each firm's interest at time of initial merger.		
16.	Determine valuation formula and process on partner exit.		
17.	Agree on location and number of offices to be maintained.		
18.	Assess office and storage requirements.		
19.	Agree on organization chart, partner responsibilities and staff structure.		
20.	Agree on quality control systems and procedures to be used.		
21.	Determine computer hardware and software platforms to be used, including accounting, tax and firm management database.		
22.	Determine employment terms for all staff, and review salary levels for equality.		
23.	Consider any staff redundancies.		
24.	Determine working capital requirements and funding for the firm.		
25.	Agree on firm bankers.		

	Issue	Response	Date
26.	Agree on firm lawyers.		
27.	Agree on professional indemnity insurer and level coverage required.		
28.	Agree on firm name.		
29.	Provide access to historic information on client base, fees by client and fees by service range for due diligence purposes.		
30.	Agree as to whether pre-merger debtors and creditors are to be combined in new firm, or collected separately post-merger.		
31.	Agree as to whether work in progress of the firms is to be billed out prior to merger.		
32.	Instruct solicitor to commence drafting merger agreement or partner/shareholder agreements.		
33.	Professional bodies to be advised on new entity and new registration.		
34.	Develop merger plan and timetable.		
35.	Allocate partnership/merger responsibilities.		
36.	Determine communications strategy and plan.		
37.	Determine strategy to advise clients.		
38.	Issue new employment agreements for all staff.		
39.	Agree on human resources policies and firms.		
40.	Transfer or assign existing commitments, leases, etc., to new entity.		
41.	Agree on timing of changeover.		

Appendix 8.2 Consolidation Checklist

	Issue	Response	Date
1.	All parties to sign confidentiality agreement.		
2.	List terms and conditions required on sale.		
3.	Is vendor prepared to sign restrictive covenant on final exit?		
4.	Is vendor prepared to accept period of escrow restricting sale of shares for a given time period?		
5.	Set your asking price. Be prepared to justify and validate this figure. Ensure you have applied sound valuation techniques and methodology.		
6.	Identify the systems and procedures that are in place, complete documentation as required, and confirm with staff that they work as intended.		
7.	Consider time period you are prepared to allow purchaser for due diligence.		
8.	Consider period of time you are prepared to assist with handover, client transition and training, subject to escrow period.		
9.	Make available historic information on client base, fees by client and fees by service range.		
10.	New employment agreements will need to be issued for all staff, likely to be prepared by consolidator.		
11.	Determine if responsibility for debtors and creditors pre-consolidation will be vendor's, or included in sale terms.		
12.	Determine if work in progress is to be billed out prior to settlement.		
13.	Transfer or assign existing commitments, leases, etc., to purchaser. This may include rent of premises, photocopier, hardware and software licenses.		
14.	Determine communications strategy and plan.		
15.	Decide on appropriate strategy to advise clients and staff.		
16.	Ensure client notes and files are complete and fully documented.		
17.	Ensure no client matters are unresolved.		
18.	Determine time frame for entire process to be completed.		
19.	Remember, your final payout is likely to be linked to the successful retention of clients by the purchaser. It is in your interest to do all you can to ensure a successful transition.		

Appendix 8.3 Sale of Firm Checklist

	Issue	Response	Date
1.	All parties to sign confidentiality agreement.		
2.	List terms and conditions required on sale.		
3.	Is vendor prepared to sign restrictive covenant?		
4.	Is vendor prepared to accept part of settlement as contingent on future revenue performance of the firm?		
5.	Is vendor prepared to accept “clawback” provisions, subject to agreement?		
6.	Set your asking price. Be prepared to justify and validate this figure. Ensure you have applied sound valuation techniques and methodology.		
7.	Identify the systems and procedures that are in place, complete documentation as required, and confirm with staff that they work as intended.		
8.	Consider time period you are prepared to allow purchaser for due diligence.		
9.	Consider period of time you are prepared to assist with handover, client transition and training.		
10.	Do you expect payment for your time involved with handover, client transition and training?		
11.	Make available historic information on client base, fees by client and fees by service range.		
12.	Issue new employment agreements for all staff.		
13.	Determine if responsibility for debtors and creditors will be vendor’s, or if it will be included in sale terms.		
14.	Determine if work in progress is to be billed out prior to settlement.		
15.	Transfer or assign existing commitments, leases, etc., to purchaser. This may include rent of premises, photocopier, hardware and software licenses.		
16.	Instruct solicitor to commence drafting sale contract.		
17.	Determine best method of marketing the firm for sale.		
18.	Develop sale of firm plan and timetable.		
19.	Determine communications strategy and plan.		
20.	Decide on appropriate strategy to advise clients and staff.		
21.	Ensure client notes and files are complete and fully documented.		
22.	Ensure no client matters are unresolved.		
23.	Determine time frame for entire process to be completed.		
24.	Remember, your final payout is likely to be linked to the successful retention of clients by the purchaser. It is in your interest to do all you can to ensure a successful transition.		

Appendix 8.4 Sale of Fee Parcel Checklist

	Issue	Response	Date
1.	All parties to sign confidentiality agreement.		
2.	List terms and conditions required on sale.		
3.	Is vendor prepared to sign restrictive covenant?		
4.	Is vendor prepared to accept part of settlement as contingent on future revenue of the fee parcel?		
5.	Is vendor prepared to accept “clawback” provisions, subject to agreement?		
6.	Set your asking price. Be prepared to justify and validate this figure. Ensure you have applied sound valuation techniques and methodology.		
7.	Consider time period you are prepared to allow purchaser for due diligence.		
8.	Consider period of time you are prepared to assist with handover, client transition and training.		
9.	Do you expect payment for your time involved with handover, client transition and training?		
10.	Make available historic information on client base, fees by client and fees by service range.		
11.	Instruct solicitor to commence drafting sale contract.		
12.	Determine best method of marketing the firm for sale, consider firm broker.		
13.	Develop sale of parcel of fee plan and timetable.		
14.	Decide on appropriate strategy to advise clients and staff.		
15.	Ensure relevant client notes, work papers and files are fully documented and completely handed over.		
16.	Ensure no client matters are unresolved.		
17.	Determine time frame for entire process to be completed.		
18.	Remember, your final payout is likely to be linked to the successful retention of clients by the purchaser. It is in your interest to do all you can to ensure a successful transition.		

Appendix 8.5 Progressive Sell-Down Checklist

	Issue	Response	Date
1.	All parties to sign confidentiality agreement.		
2.	List terms and conditions required on sale.		
3.	Is vendor prepared to sign restrictive covenant?		
4.	Is vendor prepared to accept part of settlement as contingent on future revenue performance of the firm?		
5.	Is vendor prepared to accept “clawback” provisions, subject to agreement?		
6.	Agree price up front. Vendor may need to justify and validate this figure.		
7.	Identify the systems and procedures that are in place, complete documentation as required, and confirm with staff that they work as intended.		
8.	Consider time period you are prepared to allow purchaser for due diligence.		
9.	Make available historic information on client base, fees by client and fees by service range.		
10.	Determine if work in progress is to be billed out prior to settlement.		
11.	Instruct solicitor to commence drafting sale contract.		
12.	Develop sale of firm plan and timetable.		
13.	Determine communications strategy and plan.		
14.	Decide on appropriate strategy to advise clients and staff.		
15.	Determine time frame for entire process to be completed.		
16.	Remember, your final payout is likely to be linked to the successful retention of clients by the purchaser. It is in your interest to do all you can to ensure a successful transition.		

Appendix 8.6 Internal Succession Checklist

	Issue	Response	Date
1.	All parties to sign confidentiality agreement.		
2.	List terms and conditions required on sale and transition of firm equity.		
3.	Is vendor prepared to sign restrictive covenant?		
4.	Is vendor prepared to accept part of settlement as contingent on future revenue performance of the firm?		
5.	Is vendor prepared to accept “clawback” provisions, subject to agreement?		
6.	Set your asking price. Be prepared to justify and validate this figure. Ensure you have applied sound valuation techniques and methodology.		
7.	Consider time period you are prepared to allow incoming partner for due diligence.		
8.	Consider period of time you are prepared to assist with handover, client transition, and training.		
9.	Consider financial arrangements between incoming partner and retiring partner.		
10.	Make available historic information on client base, fees by client and fees by service range.		
11.	Determine terms for dealing with work in progress.		
12.	Instruct solicitor to commence drafting sale contract and adjustment to partnership/shareholder agreement.		
13.	Update registrations with authorities, professional bodies and professional indemnity insurers for new partnership.		
14.	Check transfer or assignment of existing commitments, leases, etc., to newly constituted partnership. This may include: rent of premises, photocopier, hardware and software licenses.		
15.	Develop internal succession plan and timetable.		
16.	Decide on appropriate strategy to advise clients and staff.		
17.	Determine optimal time frame for entire process to be completed.		
18.	Remember, your final payout is likely to be linked to the successful retention of clients by the new partnership. It is in your interest to do all you can to ensure a successful transition.		

Appendix 8.7 Admission of New Partners Checklist

	Issue	Response	Date
1.	All parties to sign confidentiality agreement.		
2.	List terms and conditions required on sale and transition of firm equity.		
3.	Existing partners to agree to sale of retiring partner's equity to incoming partner.		
4.	Identify requirements of continuing partners in regard to new partner selection.		
5.	Incoming partner to agree to existing partnership/shareholder agreement.		
6.	All partners to agree on remuneration and access to profits for incoming partner.		
7.	Review and as appropriate re-allocate clients among partners.		
8.	Determine role of new partner within firm.		
9.	Is vendor prepared to sign restrictive covenant?		
10.	Is vendor prepared to accept part of settlement as contingent on future revenue performance of the firm?		
11.	Is vendor prepared to accept "clawback" provisions, subject to agreement?		
12.	Set your asking price. Be prepared to justify and validate this figure. Ensure you have applied sound valuation techniques and methodology.		
13.	Consider time period you are prepared to allow incoming partner for due diligence.		
14.	Consider period of time you are prepared to assist with handover, client transition and training.		
15.	Consider financial arrangements between incoming partner and retiring partner.		
16.	Make available historic information on client base, fees by client and fees by service range.		
17.	Determine working capital requirements.		
18.	Instruct solicitor to commence drafting sale contract and adjustment to partnership/shareholder agreement.		
19.	Update registrations with authorities, professional bodies and professional indemnity insurers for new partnership.		
20.	Check transfer or assignment of existing commitments, leases, etc., to newly constituted partnership. This may include rent of premises, photocopier, hardware and software licenses.		
21.	Develop transition timetable.		
22.	Decide on appropriate strategy to advise clients and staff.		
23.	Determine optimal time frame for entire process to be completed.		
24.	Remember, your final payout is likely to be linked to the successful retention of clients by the new partnership. It is in your interest to do all you can to ensure a successful transition.		

Appendix 8.8 Buyout by Existing Partners Checklist

	Issue	Response	Date
1.	All parties to sign confidentiality agreement.		
2.	List terms and conditions required on sale and transition of firm equity.		
3.	Review exit terms under existing partnership/shareholder agreement.		
4.	Review existing partnership/shareholder agreement for buyout protocol and procedure. If silent, gain agreement with partners as to process.		
5.	Review and re-allocate as appropriate clients among partners.		
6.	Is vendor prepared to sign restrictive covenant?		
7.	Is vendor prepared to accept part of settlement as contingent on future revenue performance of the firm?		
8.	Is vendor prepared to accept “clawback” provisions, subject to agreement?		
9.	Set your asking price. Be prepared to justify and validate this figure. Ensure you have applied sound valuation techniques and methodology.		
10.	Consider period of time you are prepared to assist with handover, client transition, and training.		
11.	Consider ongoing consulting arrangements.		
12.	Instruct solicitor to commence drafting sale and transfer contracts, and adjustment to partnership/shareholder agreement.		
13.	Update registrations with authorities, professional bodies, and professional indemnity insurers for new partnership.		
14.	Check transfer or assignment of existing commitments, leases, etc., to newly constituted partnership. This may include rent of premises, photocopier, hardware and software licenses.		
15.	Develop transition timetable.		
16.	Decide on appropriate strategy to advise clients and staff.		
17.	Determine optimal time frame for entire process to be completed.		
18.	Remember, your final payout is likely to be linked to the successful retention of clients by the new partnership. It is in your interest to do all you can to ensure a successful transition.		

Appendix 8.9 Compliance Issues Checklist

	Issue	Response	Date
	Statutory		
1.	Are you required to de-register from any taxation registrations or obligations?		
2.	If so, are there any adjustment events that need to be reported?		
3.	Are you required to issue any final notifications or payment summaries to former employees?		
4.	Ensure you complete all payments on behalf of former employees as required by your local regulators.		
5.	Cancel any policies or registrations that are in your name, if not transferred across to your previous firm.		
	Contractual		
1.	Ensure all directors’ and secretaries’ resignations have been completed and lodged, as required.		
2.	Withdraw and remove any relevant guarantees, particularly in regard to bank facilities, lease arrangements, or any other areas relating to the business.		
3.	Ensure payouts are made for those financial obligations for which you are responsible.		
4.	Ensure leases or hire purchase agreements are transferred on any equipment being transferred.		
5.	Ensure you perform handover, client transition and training as per contractual obligations to your purchaser.		
6.	Ensure you abide by any restraint of trade obligations as per contractual obligations to your purchaser.		
	Housekeeping		
1.	Advise firm bankers and confirm your exit from the firm.		
2.	Advise professional indemnity insurers and confirm your exit from the firm.		
3.	Establish professional indemnity run-off insurance as appropriate.		
4.	Advise firm insurance brokers and confirm your exit from the firm.		

	Issue	Response	Date
5.	Ensure your obligations cease in regard to business and property insurance.		
6.	Ensure you have copies of all relevant partnership/ shareholder agreements.		
7.	Ensure you have copies of all documents reflecting your resignation as director/secretary and your withdrawal from personal guarantees.		
8.	Advise creditors and confirm your exit from the firm.		
9.	Advise your professional body and confirm your exit from the firm.		
10.	Ensure responsibility for all utilities has been transferred.		
11.	Issue final invoices to clients for work completed up until settlement, in accordance with sale agreement.		
12.	Subject to jurisdiction, consider arrangements for voluntary pension plans and compulsory pension schemes.		

Appendix 8.10 Case Study

Case study 8.1

This case study relates to Section 8.6.2*, "Partnership/Merger."*

William and Indira had recently met another accountant, Manu (see Case study 6.1). Over the following months, they got to know each other better and started discussing the opportunity of working together. William and Indira had been practicing together as partners for a number of years and found that the arrangement suited their needs. They had learned to work together well and respected each other's strengths and weaknesses.

They had also become used to the structure they had adopted regarding the firm's running and management. Each of them was responsible for their own billing targets, and they also had separate responsibilities for managing the firm. This was based around the organization chart for the firm.

They had also developed a regular routine for management meetings to run the operational aspects of the business. These meetings were held each Monday morning with the full staff, and the priorities for the week for each staff member were identified and noted. William and Indira also met once a month at a partners meeting, at which they discussed higher-level reporting and strategy.

Manu, on the other hand, was a sole practitioner, and had begun to feel the pressures of running a firm on his own. He had done this for a number of years, starting with just a handful of clients. Over time he had built the firm up and now had three staff members covering accounting and administrative functions. He was attracted to William and Indira's firm, not only because it was successful, but because it was well managed and had a good culture.

When the three of them got together to discuss a potential merger, William introduced a checklist he suggested they work through, as it covered many of the issues relevant to merger discussions. The key issues identified were:

1. Share of profits

They agreed to split profits according to their proportionate interest in the partnership and would only draw on funds when their cash flow position allowed.

2. Admitting or terminating partners/directors

All agreed that the basis for admitting or terminating partners would be an essential element of any arrangement. They agreed to all contribute their thoughts on this important matter and discuss it fully next time they met.

3. Frequency and timing of partners meetings

William and Indira were keen to continue with their regular monthly partners meeting and Manu agreed that the meeting was an important management tool. This was one area where Manu felt particularly disadvantaged as a sole practitioner as there was no one at his level he could discuss important issues with.

4. Expectations of a partner within the firm and managing outside interests and obligations

Discussion around this point included the roles and responsibilities assigned to each partner, productivity levels (e.g. billing hours) expected from each partner and any non-chargeable work allowed for voluntary activities during work hours, such as professional bodies, *pro bono* work, and charity work.

5. Drawing policy and loan accounts

They all felt it was important to have a policy about the timing and formula for drawings as well for dealing with any loan accounts of any individual partners. Again, this would be discussed at their next meeting.

6. Determining goodwill calculations on entry and exit

They all agreed that it was extremely important to establish a formula for the valuation of goodwill. They felt that when a new partner is either admitted or retired, each party should have a clear understanding of how much consideration they may expect to pay/receive, and the bases for such a calculation were arrived at. They all felt this would add more certainty to their situation.

7. Restraint requirements and notice period on retirement

They agreed that restraints should be imposed if a partner was to leave but were conscious that any restraint requirements must be enforceable and would not invalidate the whole agreement. They recognized this as a complex area and agreed to seek separate legal advice on the matter.

8. Leave entitlements

They all agreed there should be no confusion or ambiguity about their leave entitlements, which would include annual, special, sick, long-term, carer's or maternity leave. Indira was asked to draft a policy which they could all consider at their next meeting.

Manu was pleased with the progress of discussions and was looking forward to becoming part of a larger team, while William and Indira each had mixed feelings about the possible merger. William was secretly pleased that he would have another partner to discuss matters with, as he felt superior to Indira and was seeking her counsel less frequently. However, he felt that Manu was quite aggressive and was not sure if Manu's style would suit the culture of the firm.

On the other hand, even though she outwardly appeared to be in favor of the merger, Indira was quite anxious about having another partner. She felt that her working arrangement with William suited her well, and that having another party involved might change the dynamics of their working arrangement. She also doubted whether Manu would work as hard as she did, even though he would want his equal share of profits. Indira decided she would wait until after the next meeting with Manu to see how she felt and would then discuss her concerns with William.