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Creating a Sustainable Firm

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It is no secret that if you want to build a firm that is going to sustain and remain in business long into the future, a primary goal of the current partners must be cultivating the next generation of partners. Too often, however, firm leaders concentrate more on engaging new business, maintaining and enhancing client relationships, increasing billable hours and realization rates, and managing the firm, rather than developing future leaders to their fullest potential. This can be detrimental to the firm's vision of its future. But who are these future leaders and how does one identify and nurture them?

Identifying the next generation of leaders

Wikipedia describes a leader as an individual who can "affect human behavior so as to accomplish a mission designated by the leader." At our firm, we look for the following traits to determine if a team member has the potential to be a leader:

1. A person that can fit into our culture
2. Someone who "lives our brand"
3. An individual who is passionate about learning and takes the initiative to explore new service options or niches
4. A person that has excellent technical skills and who can transfer these skills to other team members
5. Someone that is accountable, takes ownership of his/her work and is passionate about their clients and our firm

Leaders at our firm go above and beyond what is expected from them. For example, a second-year accountant recently joined our Lead Niche (*i.e.*, a "catch-all" for businesses that do not fit into our four main niche groups). At the first meeting he attended, we briefly discussed targeting automobile dealerships. He went ahead and researched services that we could offer, determined which firms in our accounting association specialized in working in this industry, developed a database of resources and identified prospects in our market. This person is clearly someone with the potential to be a leader.

Several years ago, we divided our team into two groups: future leaders and specialists. We recognize that both have an important role in our future and contribute equally to our success. Programs focused on leadership or specialist skills, such as mentoring and work/coach development, are available to everyone.

What does it mean to mentor?

Coaching or mentoring future leaders is critical to the successful transition of leadership from one generation to the next. We have found it is reasonable to identify two potential "replacements" for each partner.

The concept of mentoring can mean different things, depending on what you are trying to achieve. Ideally, everyone in the firm should be mentored so they can develop their technical and "soft" skills to their fullest potential. For future firm leaders, however, the mentoring process takes on added significance because soft skills are at least as important as technical proficiency. Training in networking, referral development, relationship management and the like should be part of the leadership program. Regular performance reviews also should be part of the program so that the individual's growth can be monitored.

The training can be done by internal staff or by outside consultants, depending on your firm's capabilities and budget. In either case, training should begin very early in a professional's career. It takes years to master these skills, and waiting until individuals become managers could jeopardize the level of their proficiency.

For a mentoring program to be successful, the firm's leaders, the mentor and the protégé must all be committed to the program. Participants need to recognize that mentoring is a "give-and-take relationship." The protégé can bring as much value to the relationship as the mentor, especially if they

have the desire and passion to be a future leader.

A mentoring relationship has to be more than an occasional lunch. The best relationships are more formal. Mentors ought to meet regularly with their protégé to discuss their goals and objectives. Mentors should also have an agenda and guidelines to follow to ensure that they are transferring the right combination of knowledge and experience.

One note of caution: mentoring relationships should be voluntary. It is beneficial for the mentor and protégé to agree to work with each other. This type of relationship does not work well if it is forced or assigned.

Developing a "future leader" program

Establishing a "Future Leader" or "Partner-in-Training" program will ensure that the professionals you identify will have the skills necessary to manage the firm when the time comes for your equity partners to retire. This type of program should include training in:

- Maintaining and growing a book of business
- Enhancing client relationships
- Developing new business opportunities
- Cultivating referral relationships
- Developing a strong organizational cultural
- Dealing with personnel issues
- Becoming respected and involved in community programs

The financial piece

However, even if you identify and train the right people to lead your firm, its

success after you retire is not guaranteed unless it can survive financially. The firm has to be in a good financial position to buy-out equity partners at retirement without affecting the ongoing operations of the practice. A good rule of thumb is that the payout to retiring partners should not be greater than 6-8 percent of gross revenue for any given year.

For example, if your firm's gross revenue is \$8 million, and two partners are scheduled to retire, a 6-percent payout would equal \$480,000. If Partner 1 retires this year and has a payout of \$260,000-per-year, and Partner 2 retires next year with a payout of \$220,000, it should not financially drain the firm. However, if Partner 2 has a payout of \$300,000, it could be a problem. It takes planning, and a solid deferred compensation plan or buyout agreement, to ensure that systems are in place to deal with this situation. Ideally, the agreement should limit the amount that retired partners can pull out of the firm, as well as the number of years. In this situation, both partners should take less money over a longer period of time to ensure that the firm is funded.

Make sure that the \$480,000 will not have a long-term negative effect on operations. You can mitigate the impact of a payout by budgeting for the buyout.

In addition, partners should give a minimum of two to three years notice of their impending retirement. Otherwise, a haircut in the buyout should be implemented. For example, if the buyout agreement calls for a payout of \$100,000-per-year, and the partner decides to give only six months notice, a 30-percent penalty could be imposed. In this case, the payout would be reduced to \$70,000.

The transition process

Planning for the transition of leadership to the next generation is crucial to the future of your firm. Start by defining a target partner age for when the transition will begin. For example, if the targeted average equity partner age is 55, identify who will reach this age in the next five to 10 years and start grooming a successor to take over their book of business. It is important to start the transition at least three years prior to retirement to ensure that it is successful.

In Year 1, the partner should identify his/her top 10 clients and bring the successor to each meeting, as well as involve them in all details of the relationship. During Year 2, the successor needs to be introduced to the remaining clients at least once, as well as the partner's referral sources. By

the end of Year 3, the successor should take full responsibility for servicing the retiring partner's clients. The relationship should be developed to the point that the retiring partner no longer needs to attend client meetings, etc.

At our firm, we have successfully transitioned a new partner to lead our Healthcare Niche. We identified a young woman ten years ago to work with the equity partner on all client engagements. This allowed her to develop a relationship with his clients and for them to become comfortable working with her instead of the partner. Clients were also encouraged to discuss situations with her if the partner was not available. During that time period, we invested in the technical and professional development training needed for her to be ready to take over for the partner. This included client relationship and business development training. We promoted her to a non-equity partner last year. Today, she is 80-percent responsible for the management and growth of the niche. By next year, she should be made an equity partner and be 95-percent responsible for the niche. This will allow the transitioning partner to work on managing the firm, while staying somewhat involved ensuring a successful transition.

Equity partners should be accountable for the transition. Include transition planning in each partner's bonus criterion. In other words, force the issue by deducting a certain percentage of the partner's annual bonus if they do not transition their clients to a successor by the time agreed upon. At our firm, equity partners that are approaching the age of 55 have to identify a younger professional to fill their role as a niche or department head. The future leader should be at least 8 to ten years younger than the equity partner.

Our partner agreement requires equity partners to sell their stock at 65 or the age that they become eligible for social security benefits. By that time, all client responsibilities should be completely transferred to their successor. They then have the option to work with us in another capacity, such as an advisor on special projects.

Although most managing partners agree that succession planning is important, the statistics show that the majority have not addressed the issue. According to the *2007 Inside Public Accounting National Benchmarking Report*, only 55 percent of non-national accounting firms have a succession plan in place, and 84 percent have a partner retirement plan. However, more than 50 percent of these retirement plans are unfunded, which presents a growing and compounding problem. Consequently, a number of firms may be forced to consider merging, and

the sheer number of firms that may have to consider this option may find the result is far less enticing than they thought. It still is not too late to plan for a succession within your firm so that it can continue and thrive long into the future. For that to happen, the next generation of partners has to be trained and ready to take their rightful place as your firm's new leaders.