

CLIENT TRANSITION – PART 1

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One of the most talked about issues regarding succession is “client transition.” Why? Because all too often, partners retire still owning many of their key client relationships. This creates a problem with no good solution because the firm is acting too late and is in a poor position to invoke consequences.

At least in the Billiverse, if the retiring partner has not properly transitioned his/her client relationships to the remaining partners, then the retiring partner should not be entitled to monthly retirement payments. In addition, if the retiring partner disparages the firm publicly at any time during the retirement payoff period, all payments should stop until damages can be assessed or public retractions occur. It comes down to this ... with professional service businesses, justification for the purchase of a revenue stream is the expectation of the continuance of that stream and its related profits. If the retired partner has not properly transitioned the relationships or is undermining the marketing efforts of the firm through public disparagement, then the value assessed for a partner's interest in a revenue stream will be overstated by the lost clients and/or reputation damage.

Unfortunately, with many CPA firms, senior partners often rape and pillage the firm on their way out under the rationalization of “this firm would not exist without me so I am entitled.” My comment is that most of the time, the senior partner is paid market value for his/her share of the firm but wants even more on top of it. This is typically accomplished through a number of side agreements. Common ones include the firm:

- being required to pay the retiring partner to stay on and manage client relationships that are already included in the value of the revenue stream being purchased,
- having to pay more than market value for the services of the retired partner. Instead of being paid within a range of 25-40 cents on the dollar for each hour the partner bills and collects, the retired partner may make 50% or more on their personal billings,
- having little say about the continued employment or terms of the retired partner. Instead of the firm determining whether, how or how long the retired partner is allowed to perform work for the firm, the retiring partner sets the terms and conditions of that relationship as part of the exit package (in other words, the firm can not easily fire the partner even after he/she is retired), and/or
- provides perks, often including secretarial support, office space, phone, equipment, health coverage, insurance, club dues, etc, all of which are not tied to future work performance but rather entitlement.

All of this comes down to one issue ... poor business management practices. Regardless of how much ownership the senior partner has in an organization, the remaining partners have significant control as to how their futures unfold. The most common threat is that the senior partners will sell the firm, or worse, stay on indefinitely if the remaining partners don't acquiesce. The reality is that few firms want the clients without the associated talent – like the remaining partners. That means that if the remaining partners are hostile to any deal, few firms will be willing to finalize any purchase or merger because of the ugly complications this situation creates. Also, if the younger partners band together and threaten to secede from the union, this will generate a wake up call to any retiring partners. Not only will either of these alternatives be far worse for the retiring partner from an economic status, even more important, the senior

partner is not going to be interested at this stage of his/her life to put in the effort required to rebuild a fragmented firm.

I don't cover this trying to create rifts within firms. I cover this because everyone in the firm has a really good reason to sit down and work out an equitable solution. And that solution needs to be put together with the firm in mind – what choices can we make that pay people for the asset they have grown while insuring that the firm continues to be strong and prosperous.

So, here is where transition comes in again. This process is fairly simple. But before I go into some of the details, I need to define the word “retirement” as I use it. When I say “retirement,” what I am really referring to is that point in time when a partner is required to sell his or her ownership interest in the firm to the remaining partners. I am not referring to a required physical departure from the firm.

The first step in this process is to establish a mandatory retirement age. The reason for this is to ensure that the senior partners don't extend their ownership life beyond reason. Since the workload for senior partners is typically light as compared to other partners, and the compensation for that effort is usually high, who in their right mind would leave such a situation if they did not have to. The most common age for mandatory retirement is 65 with some firms extending it to reflect the social security age. In very large firms, you will likely find retirement much earlier, like 55. However, it is my belief that for firms under several hundred people, allowing your partners to retire around 55 is way too early. Between 55 and 65 are very productive years, and given that our profession has a staffing shortage, motivating some of our most talented people leave early while they still have a lot of fire in them is a bad strategic move.

By the way, it is absolutely OK for retired owners to continue working for the firm, but obviously as W-2 employees. In addition, the new position for a previous owner is one of technical manager or senior consultant (project managers). Finally, the employment decision has to rest solely in the hands of the firm. Obviously, if an offer is made, the retiring partner doesn't have to take it, but the key is that the retiring partner has to be offered. And this should be in the form of an annual contract that automatically cancels – not automatically renews.

Now that we know when someone is going to retire (because we have a mandatory age), we are finally positioned to implement a transition policy. Why? Because if retirement is forced at age 65, then we know the retiring partner has to follow a transition plan starting at some point in time before that.

My suggestion is to make this a three year transition plan. Here are some general guidelines as to how I would set it up:

- A transition plan will be created for each retiring partner 3 years from his/her date of retirement
- The managing partner should create a plan which outlines every client the retiring partner manages.
- “A” level clients will be the first to be transitioned (this is because larger clients – “A” clients -- take more time to transition and need to be transitioned in an incremental manner). Because of the amount of service provided to “A” clients, firms need the 3 years to provide enough time for the new partner to build a strong relationship with the owners before the retiring partner leaves.

- For each client, the managing partner should assign a new partner or manager to take over the client relationship. While the retiring partner's input is important to this process as to who might be a good fit for the client, the retiring partner only has that – input. It is the firm's call as to how to divide up the client base, and it is the managing partner's job to put together a plan for this to occur.
- For each account, an action plan should be identified outlining the details of the turnover process.

Now, here the way this works. If the retiring partner follows the plan outlined by the managing partner, then for each client properly transitioned (in other words, the steps outlined were followed), then those clients will be signed-off as having been transitioned. Regardless as to whether those clients stay or leave the firm, the retiring partner is not at risk. Why? Because if the retiring partner did the job we asked him/her to do in order to transition the client relationship, if we loose the client, then it is our fault. In this case, the new partner had time to build a relationship but failed to do so (by the way, if this happens often, we have a problem with the remaining partner that we need to deal with right away).

However, for those clients that were not signed-off as having been properly transitioned (and this decision is at the sole discretion of the firm, not the retiring partner), then the retiring partner is at risk. For all clients that were not properly transitioned and leave within 24 months, 1 year's annual fees for each lost client should be deducted from the outstanding retirement benefit owed the partner.

We are at a good stopping place. The next step is to delve into more detail as to what this plan might look like. So I will pick this up in my next column "In the Billiverse." I hope you are having a great summer.