Attorneys: Will Yours Be a Future by Chance or a Future by Design? Insights for Practicing Attorneys and Equity Partners on Succession Planning

By Lawrence J. Ganim

Is your name on the door at your law firm? For many of you, the answer is yes. Congratulations on your accomplishments and your career because as all attorneys know, this is the ultimate goal you work towards from the minute you pass the Bar exam. A question you may be asking yourself today is, how long do you want your name to remain on the door? Do you want to keep that title and ownership forever or do you dream about the day you will successfully sell or transition your practice and retire? Either way, the decisions you make (or fail to make) today could mean hundreds of thousands, if not millions, of dollars in tax savings, for you, your family, your partners and your employees. And whether you desire to completely walk away from your practice in your 60s, 70s or 80s or just take a step back, the tax savings can make the difference between dreams and dreams realized.

As a financial professional I have collaborated with many practicing attorneys over the years. This experience has confirmed that far too many business owners, including founders and equity partners of professional firms, lack sufficient business planning. Most assume that their partners, colleagues or heirs will take over the business. Unfortunately, most lack a well thought-out Ownership Conversion Plan (OCP) to make this happen. The U.S. Census Bureau shows that a huge wave of baby boomers has been pushing through the workforce and is now at or within sight of retirement age. ABA data confirms that this is certainly true of the legal profession, estimating that as much as 40% of the U.S. lawyer population is at or nearing retirement age and making transition planning of vital importance.

Conscious Design Can Help You Realize Your Legacy

To better illustrate the importance of planning, the following example contrasts the difference between a future by chance (Attorney F.B. Chance) and a future by design (Attorney F.B. Design).

Chance Looks Like This:

- No clear plan for stepping aside from the practice—may work until the end;
- No documented plan for the financial future;
- No documented or implemented plan for practice succession;
- Has a 401k Profit Sharing plan and is funding that at whatever level he/she can each year;
- Insufficient liquid or income producing assets outside of the practice to meet his/her personal financial needs.

Design Looks Like This:

- Knows when he/she would like to be Financially Independent (Retire-able);
- Knows what after-tax inflation proof cash flow will be needed;
- Knows the pool of assets which will be required to fulfill this need;
- Design implemented a "Personal Hedge" plan to meet these needs that includes:
    - ◇ A pool that will provide tax free income equal to approximately 30-40% of his/her income requirement;
    - ◇ A pool where contributions are tax deductible to the practice and grow tax deferred—income will be taxable upon distribution;
        - Greater than 90% of the contributions accrue to the owner/partner;
        - Contributions are over six figures per year to the benefit of the owner/partner.
- Design has a documented succession plan in place that incentivizes younger associates to become equity owners and carry the practice forward when Design steps aside.
- Design has created a plan to address the Empty Chair possibilities prior to the plan being completed.
    - ◇ Ensuring the practice continues if Design does not or cannot;
    - ◇ Provides the liquidity to ensure this and that Design's family receives the appropriate value.

Preparing Your Firm to Transition into the Future

When you're an owner or equity partner of a law firm, there is much more than finances to consider. You must contemplate your trusted relationships with clients and the preparedness of the legal teams responsible for serving and retaining those clients. To ensure the future of the organization, firm leaders often face a structure that places short-term profits for individuals ahead of long-term strategic planning and stability for the firm. A failure to plan for the stewardship of the firm and its transition to the next generation can put the future of the firm at great risk.

Experience teaches that firms without solid succession plans are often unprepared to deal with a wide range of issues. A shortage of junior and mid-level attorneys, increasing life spans of baby boomer senior partners, and the increasingly volatile business and economic environment that all businesses face are just a few of these concerns.

One additional concern, unique to professional service firms, is that most law clients place a higher value on the relationship they have with "their attorney" than they do the "firm" that employs the attorney. In contrast to manufacturers or distributors who sell a tangible product that will be available long after their sales representative is gone, the attorney-client relationship is a very personal one, built on trust between two individuals.

One of the keys in the legal profession is realizing that the future of your firm depends on your ability to transition clients from one generation to the next, successfully. This is a major challenge for many law practices, and one that requires teamwork. Rather than harboring the client, founding or senior partners must learn to delegate in order for the client to become comfortable with others in the firm doing their legal work. This requires involving younger attorneys in meetings with clients over a substantial period of time. It's the only way to make other lawyers in the firm knowledgeable about the clients' business and to determine if the attorney-client chemistry will be healthy over the long term.

These may seem like elementary steps, but the two must build a rapport and a trusted relationship. Building the required level of confidence takes time. And while there are circumstances that are somewhat unique to succession in the legal profession, every business owner, including owners of private practices and equity partners in professional firms, needs to plan for the future. Having an Ownership Conversion Plan (OCP) is the only way to ensure that the current owner's legacy will be realized while preventing partners and younger colleagues from being pulled apart by a lack of knowing what the future may hold.

With a well thought out OCP, equity partners, associates and their families will not be left to wonder what to do in the case of an unexpected death or disability. Equally important, clients can receive an even more in-depth level of service as senior partners lead legal teams dedicated to meeting their specific needs. Major elements of an Ownership Conversion Plan typically include the following:

***1. Cement Your Future Vision* –** Determine the ideal future for you, your family and your firm. Consider how involved you want to stay in your practice, the resources you have available for retirement and your level of protection against the unexpected.

***2. Size of the Pot* –** Do you know the value of your firm in cash? What other income do you have outside of your practice what is and your ability to handle "gap shock" – the difference between what you feel your firm is worth and what a buyer knows it is worth.

3. *The Butterfly* – A buyer will be attracted to a business that is thriving and showing potential growth in the future. Working with experienced advisors can help you correct problems, create value and make your firm more attractive to a potential buyer.

***4. The Empty Chair* –** Protecting your OCP can ensure that your firm has enough liquidity to overcome the sudden loss of a key partner or contributor. Incentivizing key colleagues to stay, leveraging financial instruments, and tax planning are possible options.

***5. Your Personal Hedge* –** Growing non-business assets enhances your ability to negotiate for ownership conversion, and current laws provide many opportunities to create assets outside of the firm, with favorable taxation.

***6. The Intersection* –** When your estate plan and Ownership Conversion Plan are coordinated, your wealth will be preserved and more value will be created for you, your equity partners and a qualified buyer, inside or outside the firm.

***7. The Harvest* –** Preparing your OCP and protecting it with a well-documented and communicated succession plan helps you reap what your efforts have achieved, decreases business and personal risks, motivates key personnel and allows for timing on your terms.

While planning for transition will require a tremendous commitment on your part, and perhaps that of your fellow partners, you must have other professionals on your team. You should have a core OCP planning team that, at a minimum, includes a qualified experienced OCP/Succession planning professional, your CPA, and perhaps outside legal counsel experienced in succession planning, all working as a team. Their expertise can prevent future problems and prescribe solutions for any present conflicts. Clear communication will help you and your partners create a 'Future by Design' vs. a 'Future by Chance'—the future everyone desires, allowing each person the ability to grow professionally according to their own respective goals.

Legacy begins from the bottom up and not from the top down. Founding and senior partners will have lasting success as they prepare for the ownership conversion with the future generation in mind.

Legacy begins from the bottom up and not from the top down. Founding and senior partners will have lasting success as they prepare for the ownership conversion with the future generation in mind. You cannot be the owner(s) forever, and your main focus is the firm's success, which needs to continue supporting clients, colleagues and the greater community long after your leadership ends.

Larry Ganim is the founder and President of Ganim Financial, which has the aim of adding value to each client's life and business. His areas of expertise include business and estate planning, employee benefit planning, executive benefits, insurance planning, and pension planning. In addition to Ganim Financial, he is the founder and President of GFS Wealth Management Advisors, Inc., a registered Investment Advisory firm in the State of Connecticut. He is registered as an Investment Advisory Representative with GFS, is a Registered Representative with Kestra Investment Services, LLC, and has been a licensed insurance broker since 1981.

Larry is also the author of *Designed Destinations*, published in 2017, which provides guidance to entrepreneurs on how to prepare for the successful sale or transfer of their business and avoid the unnecessary tax burden and family conflicts that often occur when a lack of planning exists. Larry can be reached at (203) 335-0851 and lganim@ganimfinancial.com.