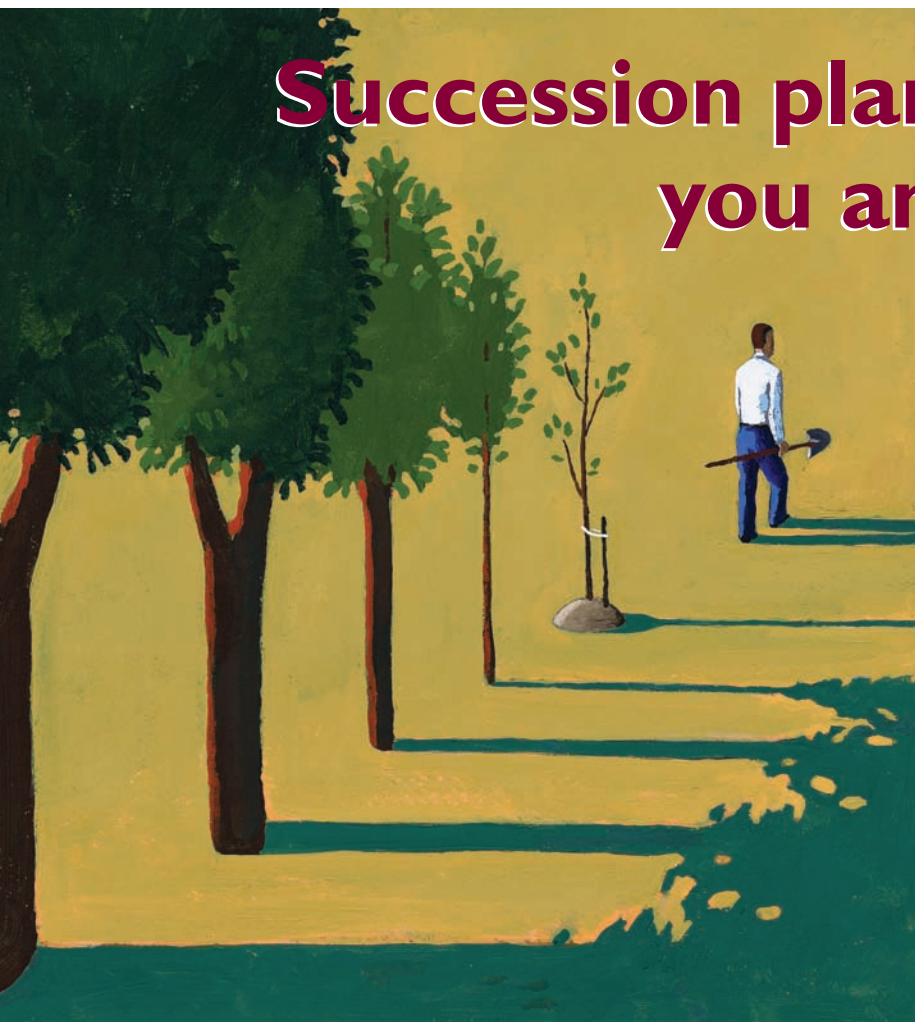


Succession planning protects you and your clients

THE NUMBER OF AGING LAWYERS WITH NO SUCCESSION PLAN IS A LOOMING CRISIS FOR THE LEGAL PROFESSION. GIVEN THAT THE LIKELIHOOD OF DISABILITY OR DEATH INCREASES WITH AGE, THOSE WHO HAVE NOT PLANNED FOR SUCCESSION, ARE SITTING ON POTENTIAL TIME BOMBS. MOST HAVE LITTLE IN THE WAY OF A CONTINGENCY PLAN TO COVER AN UNTIMELY DEATH OR DISABILITY, AND DO NOT REALIZE THAT TRANSFERRING THE DAY-TO-DAY MANAGEMENT OF THE BUSINESS CAN TAKE FIVE TO 10 YEARS TO COMPLETE.



Law Society statistics show that 32 per cent of lawyers are aged 50 to 65 and a further nine per cent are over 65, totalling 41 per cent of all members. Of the 20,345 lawyers working in law firms, 34 per cent are sole practitioners and another 29 per cent work in firms of two to 10 solicitors. The exodus of baby boomers and the expected labour shortage will impact the profession in general, but will be a greater challenge for retiring sole practitioners and partners in small firms looking to transfer their assets.

A 2006 survey by the Oregon Attorney Assistance Program¹ found that 80 per cent of sole practitioners do not have a contingency plan detailing who would service their clients in the event something happened to them. Those who are reactive rather than proactive in planning for the future are putting their financial security, their families, their colleagues and their clients at risk.

The inertia stage

“These lawyers are sitting in what we call the inertia stage of their transition process (see *Figure 1*),” explains Daphne McGuffin, program manager for The SuccessCare[®] Program, a national organization that provides support for the transition of entrepreneurial and family businesses and developer of the Law Society’s *Succession Planning Toolkit*. “They don’t know what they don’t know, so can’t get started on planning their inevitable exit from their practice. For some, it is fear that is holding them back: fear that retirement will result in a loss of income or purpose in life. It is not surprising that people are reluctant to spend time contemplating death or disability. For others, it is a perceived lack of time or knowledge that is preventing them from planning for the future.”

There are many sole practitioners who envision that they will just wind down their practice one day, closing files in an orderly fashion as they are completed. What this plan fails to take into account, however, are two things: the need for financial compensation for the work that they have invested in their practice as the basis of a retirement plan, and the fact that disability or even death may catch them unawares, leaving their clients without representation.

Other practitioners would like to exit with some return on their investment in their practice, yet do not have a concrete plan that will first enhance their maintainable earnings, and then either groom a successor or find a purchaser for their practice. Small firms often ignore the fact that a senior partner is aging, mainly because the issue of succession is considered too “personal,” then are forced into crisis mode when he or she announces plans to retire. Whatever the reason for the inertia, failure to plan increases the likelihood of an involuntary sale – an exit from the practice that is outside their control.

The succession plan

Although financial considerations may underlie the decision to work beyond 65, lawyers must plan for the eventuality that this may not be possible due to age-related decline. A good succession plan will ensure that clients’ interests are not compromised, and retirement planning should include personal financial planning.

Failure to plan

Under the provisions of the *Law Society Act*, the Trustee Services department of the Law Society may obtain a variety of orders to enable the winding up of practices where a lawyer or paralegal becomes incapacitated for any number of reasons.

A typical example will involve the sudden death of a sole practitioner with a large real estate practice, where there are

Figure 1 © The SuccessCare® Program

a number of transactions with imminent closing dates. “Unfortunately, this type of incident occurs about six times a year,” says Margaret Cowtan, manager of Trustee Services. “What is required is immediate access to the lawyer’s trust account so that client funds can be released for the closing dates. In 99 per cent of cases where no provisions are in place for a transition, we will have to obtain a court order to be able to access the trust fund.”

Alternate signing authority

She suggests that as a minimum, every sole practitioner should have another lawyer who has alternative signing authority on the trust account in the event of an emergency. Only licensed lawyers or paralegals are permitted to deal with trust accounts; therefore a trustee, employee or family member who is not licensed will not be able to access the trust account – the only exception being that the Law Society will generally permit one cheque to transfer the full balance of the account to a licensee. For clarity, practitioners can also lodge a letter with their bank confirming this authority.

It can be a very intrusive and often expensive undertaking if Trustee Services is required to resort to an order to enable a practice to be wound up. As an alternative,

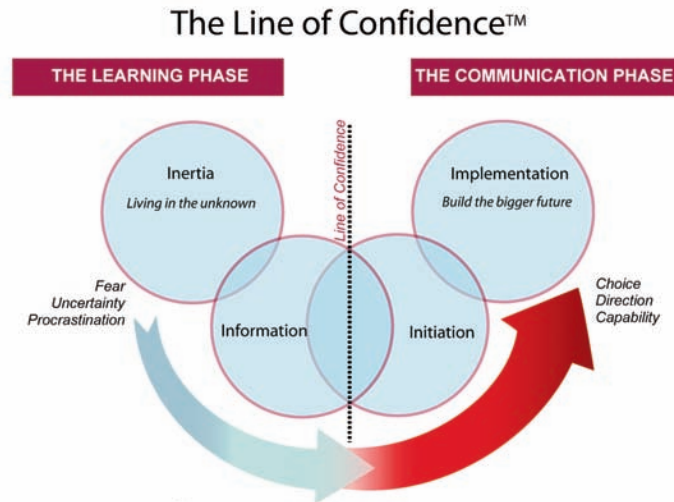
practitioners can name a licensed lawyer as a limited trustee in their wills for the sole purpose of winding up the practice. By appointing another lawyer as a trustee for the purposes of the practice, on death, that lawyer can not only take professional responsibility for the trust account and make appropriate distributions to clients, he or she can review client files, continue matters should clients elect to engage them, or return files to clients as appropriate.

Communication

“An essential part of this process is to communicate your plans to your family, partners, employees and the appointed trustee so that any transition can be as smooth as possible in the circumstances,” says Cowtan. “We often see family members grappling with these responsibilities at a time when they are grieving and undergoing enormous emotional upheaval. Making these prior arrangements can take a large burden from them.”

Maintain clear records and files

“Lawyers should ensure that they shred files at the appropriate time so that only active files and those that are required to be stored are in their offices. Clear



labelling and clear records of files will enable your family and/or successors to manage the winding down process more quickly and efficiently. We have had instances where we have had to spend three or four days going through old files to determine what has to be kept and what has to be shredded, which is an expense for the estate.” Clear financial records, as well as records of active files and relevant limitation periods for litigation practices, should also be maintained and readily available.

Many sole practitioners or small firms will have a “will bank”, that is a large collection of wills that have been written for clients over the course of a practice. Again, it is important that records for these are kept up-to-date so that a trustee knows which are current and does not have to review old or superseded wills. If a lawyer has been named as a trustee for the purposes of the practice, he or she can at least advertise that the wills are in his/her possession so that clients can contact the office to retrieve them, as well as inform the Law Society of their location.

Another wrinkle is the fact that many firms now operate as LLPs. For a sole practitioner, this means that the shares are normally held by them. The practitioner’s will can provide that on death, the shares are transferred to another lawyer to hold in trust for the estate so that lawyer can wind up the practice and pass any assets to the proper beneficiaries.

Power of attorney

“Practitioners should take their own legal advice on what provisions to include in their wills, but they should be aware that a non-lawyer trustee may not be able to deal with some of these issues easily or efficiently,” says Cowtan. “It is also advisable that lawyers consider these types of issues for powers of attorney in the event that they become temporarily incapacitated through illness or an

accident. That way, they can help ensure that they have a viable practice to return to.”

Voluntary sale

Whether you are a sole practitioner or work in a small or large firm, a good succession plan will allow the retiring partner to realize the value of the business that he or she has built, allow successors to take over a viable business, and ensure that clients’ interests are served.

“The better option by far is the opportunity to create a **voluntary** sale where you choose how and when you want to exit,” says McGuffin. “The key words here are choice and control: planning allows you to control the timing of any change, as well as whether you make an internal sale to someone inside the practice – an existing partner or prospective partner – or an external sale to someone outside the practice – likely a larger firm – who will pay some percentage of the value of your practice. In a worst case scenario, an external sale would be a decision to wind down your practice and voluntarily transfer your clients to someone outside your firm.”

Three kinds of capital

Selling a sustainable practice involves the transition of three distinct types of capital, each of which is essential to the success of the firm:

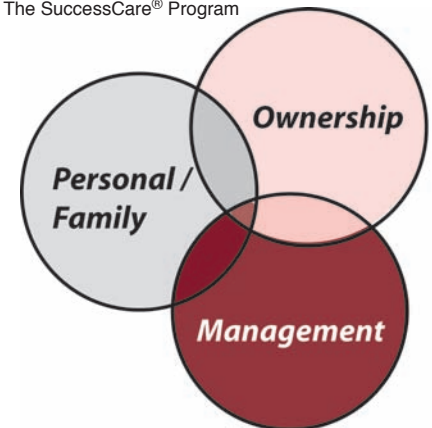
- the physical capital which resides in the ownership circle in Figure 2
- the intellectual capital which is the basis of the management area
- the social capital which is nurtured in the personal / family area.

Addressing the ownership circle by transferring the physical or tangible assets is tactical and therefore easier to understand. This includes things like premises, office equipment, accounts receivable and work in progress. A potential buyer will also want to see how the other, more intangible, assets which



Figure 2

© The SuccessCare® Program



Adapted from the 3-circle Model by Tagiuri & Davis

are probably more critical to the ongoing sustainability of the firm, will be transferred. “The social capital defines the culture of the firm and is equally important to its continuity. It impacts not only how the individual team members and their families feel about the organization, but also the impressions received by clients, lenders and referral sources,” says McGuffin. The reputation and integrity of the firm must be protected by transitioning competencies, wisdom, experience and business connections.

Five years to plan

Preparing for an internal sale generally takes longer than an external sale, especially for a sole practitioner who needs to first identify, recruit and then groom a junior lawyer or a prospective buyer. In a small firm, it can take time to develop junior partners to a point where you can ensure that your firm has all

these capabilities. An effective succession plan will develop the leadership capabilities of junior partners, which will mean that the firm will survive and will engender confidence in your clients that their interests are being served.

Preparing for an exit begins with gathering information. Information allows the practitioner to plan with confidence to ensure they have maximum choice around how and when they exit.

“You need to start early and be committed to the process. Above all, you need to have confidence that it is worth the effort and that the changes you will make will enhance your success,” says McGuffin. “Transition planning is not an event, but a process. The earlier you begin, the greater the choice you will create for your future.” ■

ⁱ Oregon Attorney Assistance Program, “Speaking of Retirement”, *In Sight*, Issue No. 63, September 2006.

Thanks to co-author Daphne McGuffin of The SuccessCare® Program for her contribution to this article.

Got a Plan?

The sustainability of a law firm after the departure of a senior partner depends on the following factors:

- ❖ **Legal expertise:** What was the retiring partner’s area of expertise? Does another partner have that expertise? Is it an important part of the practice?
- ❖ **Client retention:** Clients have to understand the reason for the change, as well as have confidence in the new partner taking on their work.
- ❖ **New business development:** Was the retiring partner the rainmaker? Is someone else groomed for that role? Can business relationships be carried on?
- ❖ **Firm management and leadership:** What role did the partner have in the management of the firm? Financial control? Strategic planning? Does someone else have the requisite skills to take those roles?
- ❖ **Profitability and cash flow:** What is the impact of the departure on cash flow?

Formal plan integral to all involved

ROD FERGUSON KNOWS FIRST-HAND THE PERILS OF FAILING TO CAREFULLY THINK THROUGH A SUCCESSION PLAN.

Called to the Bar in 1970, Rod Ferguson moved from Toronto to Midland to join a law firm led by Gord Teskey. In 1990, he established his own firm Ferguson and Boeckle. He specializes in litigation, primarily personal injury work, and built his firm on an interesting business model: realizing that many general practitioners in small towns eschew litigation work, he began taking on a “counsel” role for firms across Ontario. “We expanded geographically without having to open

offices by seeing clients in the offices of the referring solicitors.”

In the late 1990s, he began thinking of succession, and entered into a venture with three younger lawyers in his office in a phased buy-out that he hoped would fund his retirement. “I didn’t think that I should work past 65, and wanted to realize the value of the business that I had built.” The four formed a partnership that unfortunately unravelled in about three years. “It was a very difficult experience,” he says, “and I certainly



Rod Ferguson

hadn’t planned on having to start a new firm at the age of 58. But I think that I learned some important lessons from the first attempt at succession planning that have made me more aware of potential pitfalls this second time around.”

Formal planning

One of the factors Ferguson emphasizes is the importance of having a formal plan. “It’s vital for all parties to articulate two things: their vision of the firm and their expectations of the relationship. You cannot assume that the other parties will agree with you on either of these things.” Moving forward without agreed goals and operational plans can quickly lead to disillusionment on both sides of the relationship.

For the sole practitioner/senior partner, there are psychological factors to consider. “Having been responsible for directing the strategy of the firm for so many years, it is difficult to let go of the reins of power,” says Ferguson. “But again, you can’t assume that just because you’ve done something successfully for years, your junior partners will accede to continuing that strategy without their explicit buy in.”

For Ferguson, this meant that the new firm took a drastically different shape from his former firm. Previously, he had taken on work from referring counsel across a broad geographic area. His partners launched a plan to open offices in other towns. This resulted in increased overheads, but also meant that the firm was effectively competing for business with the firms that had previously given them business. “Whether that strategy was the right one or not is not the issue,” says Ferguson. “What I learned was that I had made assumptions about how the business would operate going forward, and my partners had a very different vision. We voted by share of capital, and when their aggregate total was greater than my share, I was out-voted. In some respects, I felt that little value was placed on my experience, and that demotivated me going forward.”

Planning for succession necessarily means planning for giving up control. It doesn’t have to mean, however, that the transition cannot be a gradual one which values the experiences and wisdom that

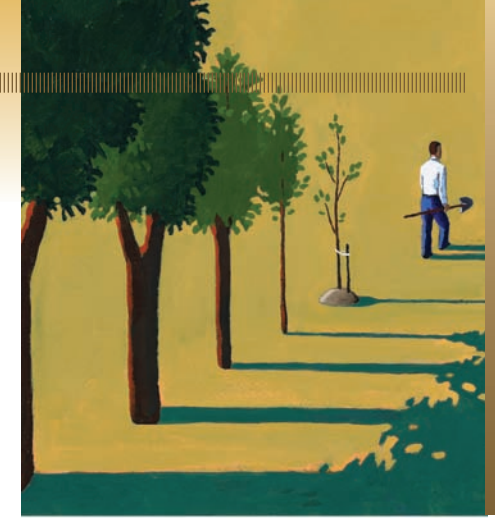
the owner/entrepreneur has gained. Sharing the history of the evolution of the firm, and the reasons certain decisions were made enables junior partners to understand the retiring partner’s values and to commit to a strategic plan. “I gave up the managing partner position, which meant I didn’t deal with the bank, didn’t control the intake of files, and didn’t control the distribution of the files.”

Generational differences

“Our differences were also compounded by generational differences,” comments Ferguson. “That doesn’t have to be fatal, and it doesn’t mean that you can expect a different generation to want the same things out of their work or for their lives as you do. It is important to recognize and acknowledge those differences, and how they will affect how you work together. For example, our attitudes toward debt were different. Every business needs a certain amount of working capital, and sometimes that involves borrowing. We quickly, however, got to levels that I personally wasn’t comfortable with, though my partners were.”

Another vital aspect to succession planning is that all parties should get independent legal and accounting advice. “Again, with hindsight, we should have done that. Instead, we all relied on one accountant, who unfortunately gave us bad advice, and we drew up our own partnership agreement that proved almost impossible to unwind.”

“Why did I enter into this agreement? Looking back, I’m not sure. I think I felt the pressure of work, and had started to count down to the point I would be able to retire. I wanted to ensure that I had a reasonable lifestyle on retirement, and could realize a fair return on the years I had invested in building the business. I was worried that the younger people in my office were getting impatient and needed the incentive of being partners to



continue working at the firm. All of that was probably true, but as it turned out, I didn’t have to give equal partnerships immediately, relinquishing control.”

The new plan

Now, his former partners operate as sole practitioners in three locations, and Rod has launched a new firm, Ferguson Barristers LLP, to which he admitted partners in 2007. Ferguson Barristers LLP is a partnership between Ferguson’s own company and his three new partners’ company. “The details of our specific arrangement probably aren’t important because every situation will have different priorities and strategies,” he says. “What is important is that we drew up a formal plan and operating strategy, and discussed everyone’s expectations of the relationship. We each took independent legal and accounting advice so that we each feel secure with our positions and our responsibilities, but we also have simplified termination and escape clauses in case it doesn’t work out.”

“What’s important,” he continues, “is that I have an opportunity to pass on my firm to associates I am comfortable with. I have learned that they are going to operate their firm differently than I did, but I also feel that my experience of building the business is respected and valued. I have an opportunity to have a comfortable retirement, and I know that when I do retire, any ongoing files or long-term clients will be taken care of.” ■



Succession planning: the regulatory framework

Rule 2.01 (1) defines a “competent lawyer” as “a lawyer who has and applies relevant skills, attributes, and values in a manner appropriate to each matter undertaken on behalf of a client” and explicitly includes:

- (e) performing all functions conscientiously, diligently, and in a timely and cost-effective manner
- (i) managing one’s practice effectively

Rule 2.01 (2) provides that a lawyer shall perform any legal services undertaken on a client’s behalf to the standard of a competent lawyer.

The commentary to Rule 2.09 (1) says that “having undertaken the representation of a client, the lawyer should complete the task as ably as possible unless there is justifiable cause for terminating the relationship.” A succession and/or retirement plan should ensure that all outstanding client matters are either completed or passed on to another lawyer acceptable to the client before retirement, so that no client is left without legal representation.

Rule 2.09 (7) provides that withdrawal from a file is mandatory if a lawyer becomes incompetent due to sudden illness, disability or impairment. An appropriate succession plan should set in place procedures that minimize expense, avoid prejudice to your clients, and facilitate the orderly transfer of client matters to another lawyer if unforeseen events occur.

Rule 6.01 (3) provides that lawyers have an obligation to report the mental instability of a lawyer or any other situation where a lawyer’s clients are likely to be severely prejudiced.

Succession Planning Resources

The Succession Planning Toolkit reviews the process to plan for the voluntary sale of your practice. The toolkit shows how to initiate a progressive transition that will ensure you:

- control the process
- plan for continued financial independence
- meet professional obligations to facilitate an orderly transfer of client matters
- treat your partners and staff with respect
- reduce stress for your loved ones in the event of your untimely death or disability.

The Succession Planning Toolkit is available free from the Law Society website.

An upcoming CLE program entitled *Succession Planning for Your Practice* will be held May 20. This will be a Teleseminar Plus program.

The Law Society has prepared a *Guide to Closing Your Practice* which is available free-of-charge and is downloadable from the website. This contains a series of checklists and guidance on how to deal with active as well as closed files, as well as sample letters to clients and file transfer directions. It also contains sample **Law Firm Inventory Checklist** and **Law Office List of Contacts** which should be kept current by all law firms, setting out information like computer and telephone passwords, banking information, insurance policies, important contacts and other information that will be essential for anyone taking over a practice in the event of untimely death or disability.

Past CLE programs and materials available from www.lsuc.on.ca include:

Buying and Selling a Law Practice: this program is designed for lawyers who are either considering or in the process of buying or selling their law practice.

Sunsetting Your Practice: A Guide to Closing Your Practice: proactive succession planning for a practitioner in the event of illness or sudden death.

The Canadian Bar Association has prepared a document entitled *Planning Ahead for Partner Retirement*. This includes advice on developing transition plans, compensation, transitioning clients and firm management, and sample retirement provisions and is downloadable from the CBA website at <http://www.cba.org/CBA/PracticeLink/MF/partnerretirements.aspx>.

LAWPRO has prepared a document entitled *Managing Practice Interruptions*, which provides a comprehensive review of the steps you can take to prepare for unexpected minor and major practice interruptions, and how you should respond to them. This is downloadable at <http://www.practicepro.ca/disasterbooklet>.