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Stan Sterna • Aug. 21, 2017

Succession planning is a major area of concern for CPA firms. With baby boomers hitting retirement age, the following statistics underscore why it is such a compelling issue to the profession:

- The average age of a CPA in the U.S. is 55[1]
- 75% of CPAs in the U.S. will be at or near retirement by 2019[2]
- 84% of firm owners expect succession issues to become a major concern within 10 years[3]
- While 100% of firms with 200+ employees have succession plans, only 23% of firms with 1-8 employees have plans in place[4]

Small firm owners mistakenly assume they will be able to fund retirement by selling their practice. It's a little more complicated than that. This article seeks to provide insight into two common types of succession plans.

Transfer of Ownership

This form of succession planning involves the sale of your practice to a partner or outside accountant. While this is the preferred method of succession for smaller firms, it comes with certain challenges.

- **Leadership Development**

This exit strategy hinges on the development of a competent successor. Over the next 5 years while 35% of CPA firms are expected to transfer ownership, only 26% have formal mentoring programs in place.[5.] Whether they will come from within or outside the firm, identify your successor early on and determine what is needed to

percent of CPAs say they plan to work after they reach age 65. By continuing to work full or part-time, many CPAs defer transition because they are unable to relinquish control of their clients. This eventually leads to tension with their successor, causing them to seek employment elsewhere.

Specify the timing of events within your succession plan. Include a timetable to transition your clients to your successor, your plan for reducing your hours and your retirement date.

- **Creating an Equitable Plan**

While large firms have finance and human resource departments, partners at small firms are primarily responsible for these functions. When an owner holds all the reins, they are often less inclined to provide their designated successor within the firm the requisite compensation to be able to buy them out. Rather than creating a lasting legacy, you may be guaranteeing your firm's ultimate demise if your successor cannot meet the payment terms.

The successor needs to feel the plan is a good deal for them. Formalize the process for the delegation of responsibilities and the commiserate salary that goes with them. Develop a fair and equitable payment plan that is achievable and agreeable to all parties.

Sale or Merger

Nearly half of sole practitioners nearing retirement indicate their plan is to merge or sell their practice to another firm. Yet, only 7% have such a plan in place.[7]

With high number of CPAs retiring in the next five years, the competition to sell or merge will increase, making it a buyers' market. Without a succession plan in place, waiting to the last minute could result in receiving less than expected for your practice.

- **Firm Valuation**

transition to do due diligence. Assess whether your client mix and fee structure will work well with the new firm. Analyze their technology, processes and address issues with difficult clients. Consider steps can you take to further enhance your firm's value. Use the PCPS Quick Start Guide, Due Diligence Guide and the PCPS podcast, First Three Steps in Creating Your Succession Plan, for guidance.

- **Notifying Clients**

A sale or merger will have a considerable impact on your staff and clients. Keep them apprised of your plans and allay any misgivings they may have. This can help ensure they stick with the new firm, which can have a bearing on your payout.

Send a letter to your clients letting them know you are committed to making sure their needs will continue to be met. For your longest and most lucrative clients, set up a face-to-face meeting to answer any questions they might have. The PCPS Succession Planning Resource Center provides letter templates and additional advice that can help you manage this process.

Insurance Considerations

Professional liability coverage is also an important consideration. Most policies are written on a 'claims-made and reported' basis. For coverage to exist, claims must occur *and be reported during the policy period*.

If someone alleges an error or omission in the rendering of professional services *after* the CPA has discontinued their practice and canceled their professional liability policy, most policies provide a "grace period" (often 60 days). However, claims reported after this short grace period can be denied.

Do not cancel or allow your professional liability insurance to lapse for nonpayment of premium after you retire or end your practice. Consider adding an Extended Claim

Reporting Period (ECRP) endorsement to your policy. Known as 'tail coverage', an

Stan Sterna, JD is Vice President, Risk Management and Amy Massaro is Vice President, Business Development at Aon Insurance Services. Aon has been the endorsed administrator of the AICPA Professional Liability Insurance Program since 1974. To learn more about the AICPA Program, visit www.cpai.com.

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[1]LBA Haynes Strand, "Merging Accounting Firms – Why CPA Firms Are Merging at a Rapid Rate," www.lba-cpa.com, June 16, 2014.

[2]Ibid.

[3]AICPA, "CPA Firm Succession Management: Multi-Owner Survey Report," Private Companies Practice Section, 2016, pg. 6.

[4]Ibid, pg. 5.

[5]Ibid, pg. 7, 36.

[6]Ibid, pg. 11.

[7]Ibid.