Planning for your practice like you plan for your clients
Succession planning

Do advisers take their own advice on planning for the future?

Not as much as they should.

Advisers spend countless hours with their clients discussing their long-term goals and objectives, and recommending strategies to ensure future needs and life changes are considered.

If statistics are to be believed, not enough advisers are taking their own advice. According to a 2004 report titled “Succession Planning” from LIMRA, 18% of advisers have failed to make succession planning a priority. Even among the 42% who have given it some consideration, there is a noticeable gap between thought and action. Only slightly more than one-third (37%) of advisers either have a plan or are putting one together.

Interestingly, the closer advisers are to retirement, the less likely they are to be prepared. Among those with five to 10 years to go, more than half (53%) have a plan or are actively formulating one. But two-thirds of those with retirement looming on the horizon – less than five years away – are far from ready, with only half even giving it some thought, although not taking the next step of actually putting a plan together.

It’s the classic case of the shoemaker’s children going shoeless – but in this case, more than just footwear is at stake, since advisers also have their practice and their clients to take into account.
Refusing to acknowledge the inevitable end of a career flies in the face of statistical reality. After all, the insurance industry is predicated on possibilities: recognizing that if X occurs, then Y could be the result. And it’s no different for the adviser than the client. While the circumstance necessitating the transfer of the business may not always be under one’s control, the method and effectiveness of the transition can be.

The cost of not having a well-developed succession plan in place can be high, especially if the transition is due to unforeseen events, such as a sudden illness or accident. For example:

- The adviser loses the time needed to find a thoroughly vetted successor and facilitate a warm hand-off with clients to make the transition easier for all involved.
- The successor adviser, who takes over the book of business, needs to quickly establish relationships with an unfamiliar client base – in many cases, while servicing the needs of his or her own clients as well.
- Clients find a new face handling their accounts and providing broad-based financial planning advice – a disquieting outcome that is uncomfortable at best and could ultimately result in client attrition.

“If you fail to plan, you are planning to fail” is just as true now as when spoken by Benjamin Franklin, with the impact of that failure reverberating not only through the client base, but also through the company and the successor adviser who has to step in and pick up the pieces, as it were.

Conversely, having all the elements of a succession plan in place offers numerous benefits.

- Advisers can focus on gradually scaling down their involvement as well as slowly distancing themselves emotionally from the day-to-day operation of their practice, while bringing their successor up to speed on the nuances and specifics of each client.
- Successor advisers gain the time needed to familiarize themselves with the soon-to-retire adviser’s book of business and integrate it successfully into their existing client list.
- Clients have the opportunity to form relationships and establish a comfort level with the successor adviser while the current adviser is still on board.
- The company retains a profitable client base that ensures a steady upward trajectory of growth.

The fact that the company benefits from its advisers having a succession plan in place is illustrated by the number of home offices that offer formal succession planning programs. A corollary benefit is that having such a program in place goes a long way to overcoming resistance. According to the LIMRA study, 42% of advisers associated with companies offering succession planning assistance either have a plan in place or are in the process of creating one. But among those advisers whose home offices doesn’t provide that option, only 34% have prepared for the transition.
Developing a succession plan

Succession planning is a multifaceted process, requiring a significant amount of time and effort to develop. The plan itself can play out over several months or even years, depending on the arrangement between the adviser and the successor.

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**Stage One – Determining the value of the business**

A detailed valuation will shed light on what is driving the value of a practice, as well as identify any needed adjustments that will improve its appeal to prospective buyers. This is not unlike completing updates before putting a house on the market to increase the selling price.

Maintaining up-to-date financial records play a key role in this calculation. Unfortunately, this is an area where many advisers fall short. The LIMRA report noted that, while more than 60% of respondents have current balance sheets, less than 37% have current retained earnings statements – an omission that needs to be rectified to complete the valuation process.

As for the actual formula for valuing an existing business, the LIMRA study notes that revenue is the most common factor used, with a typical multiplier of 2.5 times. Commissions are next in line, with a typical multiplier of 2.3 times, followed by earnings (multiplier of 1.75) and income (multiplier of 2.0).

While positive dollar figures are obviously a major selling point, successor advisers are also looking for less currency-based indicators of a viable operation worth their time, their commitment and their money. Strong practice management examples include:

- Well-defined processes and systems for marketing and client service
- Good client records and well-documented client communications
- A clear identity for the practice, tied to well-chosen market segments
- Efficient use of technology and staff
- Formal training programs for both current agency advisers and successor advisers.

Successor advisers will also be evaluating what they will gain from this affiliation, such as a wider customer base, expansion into other areas or collaboration with an adviser team.
**Stage Two – Selecting the right successor adviser**

Selecting the right candidates can be a challenge, as evidenced by the LIMRA report noting that among the 37% with a plan in place, only 25% have named a successor. It requires not only a significant amount of time and effort on the part of the adviser, but also a difficult realization: the reality that the relationships established over decades will ultimately be in the hands of another.

Despite this unpleasant reality, advisers owe it to themselves and their clients to take a proactive approach and begin the search for a successor well in advance of the need.

Points to consider include:

- **The aspects of an ideal transition:** how long the transition period would last, how the client transfer would take place and what role the adviser would play once the transition is completed.

- **The qualifications of an ideal successor adviser:** what personal and professional criteria such as business philosophy, experience and objectives matter most to the adviser and to the existing client base, and the size or type of block of business he or she will be bringing to the table.

The next step is to explore various sources for potential successors, from members of the firm and other colleagues to existing or potential team members. The potential successor pool can include ambitious up-and-comers, an independent financial professional, established teams and new recruits to the profession.

The goal is not always to find a successor adviser who is a mirror image (in method, strength or attitude) of the current owner, but one who understands the business as it is now and can adapt to whatever changes may occur in the industry down the road. Equally critical is for the adviser (who is most likely several decades older than the candidates) to recognize that what motivates the younger advisers can be dramatically different from their older counterparts.

After conducting an appropriate level of vetting to reduce the group to a select few candidates, a strategic consult will gauge each candidate’s compatibility with the other financial professionals involved, explore shared objectives and expectations and ultimately determine if this is a good fit.

Once the successor adviser is chosen, he or she will be part of the succession plan formulation.

**Stage Three – Structuring a formal succession plan**

This stage will most likely involve the potential successor adviser and other professionals, such as a business attorney and members of management. Key points to discuss include:

- Whether the succession plan covers all lines of business or only specific ones
- How long the adviser will continue playing an active role in the business, and in what capacity – full time, part-time, or on an as-needed basis
- When and how the successor adviser will be introduced to the adviser’s client base
- Under what conditions the succession plan will go into effect
Stage Four – Working with the chosen successor

Following the formulation of the succession plan, a defined trial period involving the successor adviser takes place. This serves several purposes:

- It allows both parties to evaluate how well their personalities and work styles fit together.
- It affords the successor adviser the opportunity to meet internal members as well as the opportunity to become familiar with the case work and to meet clients.
- It provides sufficient time to discuss the details of the succession plan and address any questions and concerns that either party may have.

Transitioning the business

Following a successful trial period, the succession plan can now be formalized. In general, this should be done with the assistance of a qualified third party in order to achieve a transaction that is beneficial to both parties and is seamless to clients.

The terms and timeframe of the actual transition can vary, with some successor advisers buying the book of business outright, and others operating more as partnership, with the adviser’s responsibility gradually lessening as the successor takes on a more active role. Since the majority of successors have their own book of business, this transition stage also allows them to continue servicing current clients while establishing connections with the new client base.

In some cases, the adviser may opt to remain in the business after the transition, either as a part-time partner or as an adviser with no ownership responsibilities. In such cases, both the adviser and successor adviser would have to mutually agree to these terms.