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Maximizing Equity in Your Practice with Strategic Succession Planning

Maximizing Equity in Your Practice with Strategic Succession Planning

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1/3 OF CANADIAN ADVISORS WILL RETIRE WITHIN THE NEXT DECADE[1]

Advisors provide guidance every day for their clients in how to be proactive in retirement and financial planning. Despite this, a quarter of advisors don't have any succession plans in place for themselves[2].

When is the best time to start succession planning for your established business? Likely 10 years ago. But if you haven't started yet, the second-best time to act is now. Whether you're planning to retire in the next few years or decades from today, you can start by considering these succession planning strategies to maximize the value of your business.

COMPETITION TO SELL IS ON THE RISE

Only a small percentage of advisory practices are sold in Canada, while the remainder are exiting by attrition. If you don't want your business to wind down to the point where you cannot sell it, kickstart your succession planning by asking these three questions:

1. What is the potential equity of your business?

Advisors who have grown a book and practice into a successful business have surpassed the typical 80–90% fail rate of wealth management practices in Canada[3]. If you're in this top 10%, exiting by attrition will leave valuable equity on the table. Keeping a steady hand on the value of your practice is critical when it comes time to sell because pricing at fair market value will play an important role in the success of this transaction.

Within the next 10 years, a third of Canadian advisors are expected to retire[4] and 30% of assets available for transfer are expected to be lost due to a lack of succession planning[5].

Work with your firm and a trusted accountant to assist with the valuation of your book size and identify which method to use:

- Multiple of revenue
- Multiple of earnings before interest, taxes, depreciation, and amortization (EBIDTA)
- Multiple of earnings before owner compensation (EBOC)
- Discounted cash flow

Advisors are known for guiding their clients to take proactive action around planning for their retirement and financial futures. Yet, ironically, they can fail to plan well for their own. This often leads to the loss of a considerable amount of potential equity. Seek the advice of a tax professional to understand the tax implications of the transition and to develop a tax-efficient plan.

The longer your runway, the better you'll be able to absorb fluctuations in the market and unforeseen circumstances, like a global pandemic, that can impact the timing and valuation of your book. After determining the value of your business, the next step is to protect what you have built.

2. Who will you entrust with your clients?

Your reputation has been cultivated over years of trusted interactions and you owe it to your clients to think carefully about who else is capable of effectively managing their money. Failing to plan is risky for your reputation as well as those who remain associated with your practice and your firm.

The unexpected can occur at any time, so think well in advance about who you'll entrust with the financial futures of your clients to before you decide to retire and/or sail off into the sunset.

Advisors looking to merge or acquire a practice can use these same strategies to increase revenue and scale their business. As with any new venture, do your due diligence. Understand the associated costs and how much financing you may need to purchase a practice.

Smaller firms might team up with a similar-sized practice, creating a reciprocal agreement for succession planning. If you go this route, consider if the client demographic of an outside practice matches yours. Selecting a firm with the same (or better) services and opportunities for clients will go a long way when you're communicating to reassure them about why you've made this decision and how it benefits them in the long term. Additional considerations should include:

- Determining the capacity to integrate new clients.
- Balancing the competing desires of purchaser and seller, or the terms of a reciprocal agreement.
- Accounting for attrition of assets within a defined period.

A smooth transition plan must be robust and legally compliant, and will involve employees, clients, and your trusted group of accountants, lawyers, and financial advisors. Document all your business processes and procedures, including client files, investment strategies, and financial reports. Review your legal and financial arrangements, such as partnership agreements, insurance policies, and estate plans, to ensure they are up to date and reflect your wishes. This will help ensure a smooth transition and continuity of service for your clients.

If there are no suitable family members, colleagues, or third-party buyers you would consider as potential successors, you can build a succession team or bring on an individual to prep and season for succession.

3. What are you doing to attract top talent?

The Canadian wealth management industry has seen a significant decline in new advisors joining the business, with many long-standing vacancies that remain unfilled[6]. It's become increasingly difficult for firms to hire enough new talent to fill the pipeline of an industry with many advisors between 55 and 60 years of age who are thinking about retirement.

Consider what you and your firm are doing to attract and retain top talent, and to mentor those who might step in as part of your succession planning.

If you don't have someone today that you're comfortable handing over your business to, you'll need to focus on hiring or nurturing the talent of key members of your team. Are you offering the latest technologies to improve efficiencies, digitally upskilling your team, and offering opportunities for advancement?

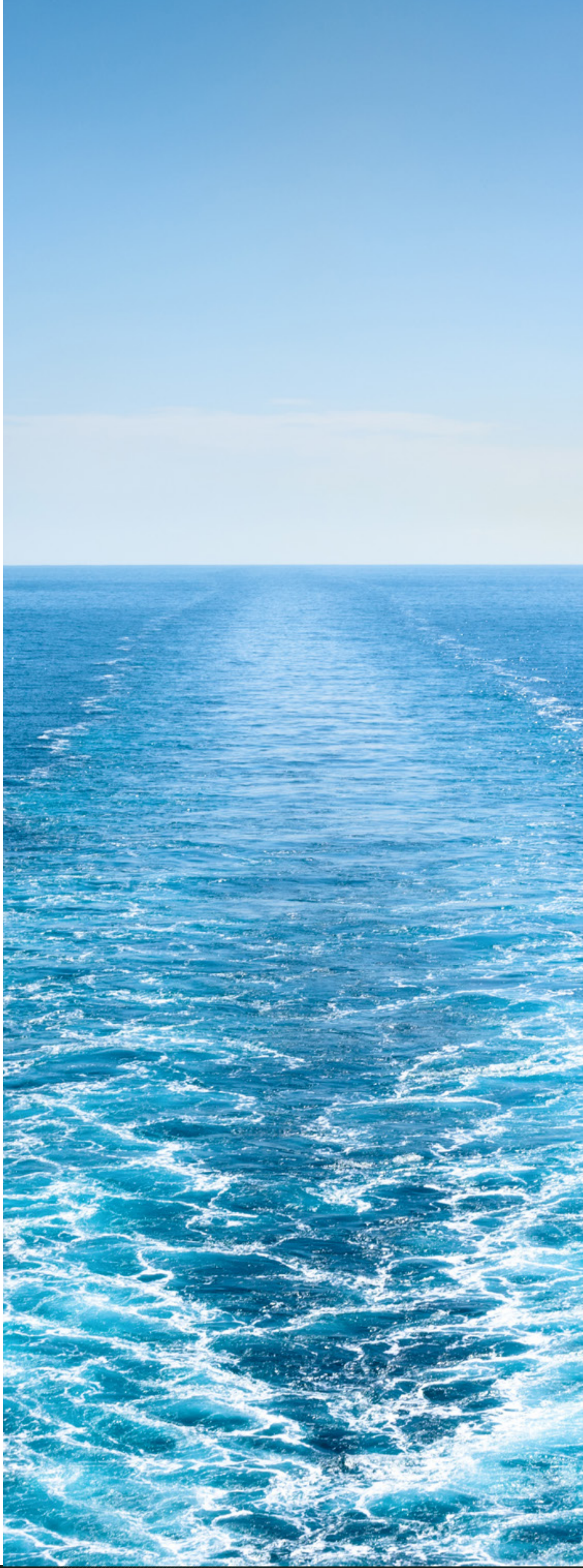
"Re-wired investors," part of the next generation of digital-native investors, expect the same quality of digital service and engagement from their advisor as they receive elsewhere online.

SUCCESSION PLANNING DOESN'T HAPPEN ALONE

You can unlock the value in your business while also protecting your book and your client relationships. By surrounding yourself with the people you need, you can develop new opportunities and overcome challenges by thinking strategically about succession planning over the long term.

Additional Resources

- Succession Planning for Financial Advisors: Building an Enduring Business by David Grau Sr.
- The Ultimate Succession Planning Guide for Financial Advisors by John Anderson
- The Handbook of Succession Planning for Financial Advisors by David Grau Jr.



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If you're interested in learning more about succession planning for your business needs, get in touch with Harbourfront by visiting:

WWW.HARBOURFRONTWEALTH.COM

[1] https://www.barrons.com/advisor/articles/cerulli-succession-plan-financial-advisors-retire-51655084377
[2] https://www.barrons.com/advisor/articles/cerulli-succession-plan-financial-advisors-retire-51655084377
[3] https://www.advisorperspectives.com/articles/2022/02/15/an-unexpected-solution-to-the-high-failure-rate-among-new-advisors
[4] https://www.barrons.com/advisor/articles/cerulli-succession-plan-financial-advisors-retire-51655084377
[5] https://www.fa-mag.com/news/the-financial-advisory-space-stands-to-lose-one-third-of-advisors-to-retirement-in-the-next-decade-52579.html
[6] https://www.theglobeandmail.com/investing/globe-advisor/advisor-practice/article-what-a-declining-number-of-advisors-means-for-the-investment-industry