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Advisor Succession *Planning Guide*

Advisor Succession Planning Guide

Introduction

Many financial advisors are looking to grow their businesses by buying a practice while others are looking at selling their practice and/or developing a succession plan.

Since it is Investment Planning Counsel's goal to help our advisors to build a better business, we have prepared this guide to assist both buyers and sellers. This guide will be covering some of the key issues under consideration as follows:

- Is Buying a Practice Right for Me?
- Is Selling my Practice Right for Me?
- Valuation Methods
- Factors that may increase/decrease the price
- The documentation, the terms of an agreement
- Financing
- Transition Plan
- Formula for Success

Is Buying a Practice Right for Me?

Buying a financial advisory practice can double your assets overnight. It can also double your workload but it may not double your revenue or profitability.

In purchasing a practice the buyer commits to:

1. a financial investment
2. a professional investment to service the new clients
3. a personal investment to build one on one relationships with the new clients

In consideration of a purchase transaction, a buyer should consider what of the following main drivers are important:

- Increase AUA
- Increase revenue
- Increase profitability
- Take the business to the next level
- Jump start the business
- Utilize excess capacity in my existing practice
- Grow faster than you can organically

In addition, it is equally important to understand what you are buying. Consider the following elements you may be acquiring:

- Goodwill of the business and clients
- The sellers time during a transition period
- The sellers records and systems
- Prospect lists and databases
- The reputation and brand of the practice and dealership
- Furniture and other fixed assets
- Real estate and/or lease commitments

It is critical for the buyer to understand the relative value of the above assets in addition to the client base.

Is Selling my Practice Right for Me?

In order for a transaction to happen, there must be a willing seller and willing buyer. Consider some of the following reasons why you might consider selling your practice:

- Time to retire
- Don't like the business anymore
- Competition is tougher
- Client demands are increasing
- Health issues
- Family issues
- Approached by a buyer with an attractive offer
- Its just not fun anymore
- Bored with the business
- Increasing compliance

One of the big deciding factors to consider is - ***are you selling a viable business or a sole practitioner practice?*** The value you will derive from the sale will no doubt be directly correlated to the answer of this key question. One way to quickly assess this is to ask yourself another question that is "Will your practice continue to run without you?"

IPC, as your business partner has been and will continue to assist advisors in helping them build a better business, a business that at some point in the future will be worthwhile to a purchaser as a viable business built around simple business concepts.

In selling your practice, consider the following assets for sale:

- Client lists
- Client assets
- Prospect lists
- Guaranteed revenues
- Work in progress
- Well defined business systems and processes
- Profits
- Other business assets

In preparing your business for sale at the maximum value, it is important that a seller focus on the key elements of running a better business. To run a better business, advisors need to follow good practice management and focus on:

1. Increasing your reoccurring revenues (trailer fees, renewals, etc.)
2. Decreasing the cost of operating your business (complexity)
3. Building loyal client relationships to business systems – not people
4. Manage a “low risk” investment portfolio of assets in a limited number of holdings

Valuation Methods

There are many methods that can be used in the valuation of a practice, but unfortunately the buying and selling of financial planning practices is still a relatively new transaction to the marketplace.

Some of the methods used are as follows:

- AUA based
- Recurring revenue based
- Operating income based (net free cash flow after normalized earnings)

Based on IPCs history of assisting advisors with book purchases, it is our believe the most predictable method of valuation is a multiple of recurring revenues generated in the practice. The range of this multiple is between 2 to 3.5 times net annual recurring revenue. The multiple used to calculate the value of the business should be dependent on the attributes of the book (both positive and negative).

Consider the example:

Assets Under Administration	= \$40 million
Annual Gross Dealer Commission	= \$400,000
Annual Trailer Commissions	= \$200,000
Advisor Payout Rate	= 85%
Net Annual Recurring Revenue	= Annual Trailers × Advisor Payout Rate
Net Annual Recurring Revenue	= \$200,000 × 85% = \$170,000

In this example, the book is worth 2 to 3.5 times Net Annual Recurring Revenue, or \$340,000 to \$595,000.

In evaluating other products like insurance renewal commissions, and GICs, the same valuation method can apply so long as the future revenue potential is predictable and repeatable.

Factors that Impact Purchase Price

There are many factors that will impact the financial purchase price between a buyer and seller. Some of the key factors include and the impact on value is as follows:

Factor	Impact on Value
What buyer is willing to pay	Decrease ▼
Outstanding compliance/client complaints	Decrease ▼
Client attrition once a transaction is announced	Decrease ▼
Forced sale due to death, disability	Decrease ▼
Practice is in decline/distress	Decrease ▼
Buyer is more competent than seller	Decrease ▼
What the seller is willing to accept	Increase ▲
Seller and buyer have good knowledge of clients	Increase ▲
Practice is run as a business and not as sole practitioner	Increase ▲
High use of efficient managed money solutions	Increase ▲
History/trends of the business using financial ratios	Increase ▲
Revenues based on commission income	Decrease ▼
High rate of clients with an IPS and/or financial plan	Increase ▲
Declining practice profitability	Decrease ▼
Significant amount of unprofitable client relationships	Decrease ▼
Extensive variation in product usage	Decrease ▼
Untapped potential for insurance sales	Increase ▲
Declining expenses or synergy opportunities	Increase ▲
Large number of clients/families	Decrease ▼
AUA in depletion and/or payout phase	Decrease ▼

The Documentation

IPC is pleased to provide you with all the sample documents necessary to implement a transaction. To access this information, please refer to our advisor portal at www.ipcc.ca under the section Total Client Experience, Buying and Selling a Book. You will find access to information and templates on the Seven Step Process required to successfully acquire or selling a book of business. Contained within our portal are samples of:

- Confidentiality Agreements
- Requests for Information
- Letters of Intent
- Purchase and Sale Agreements
- Promissory Notes
- Dealer Notifications
- Client Retention Letters

For further information on how to purchase or sell a book of business please feel free to contact Frank Sagebiel at fsagebiel@ipcc.org.

Financing

When looking at a book purchase, you must consider how you will actually pay for the book.

One method is for the Seller of the practice to take back a note from the Buyer. IPC can agree to be party to the agreement in this circumstance, however, only to the extent that we agree to take from the Buyer's commission and give to the Seller in the event of non-payment of the note.

Another method is to take advantage of **IPC's Advisor Book Financing Program**. This program is available through Laurentian Bank; and can be an excellent vehicle for advisors who want to grow their existing book of business by acquiring another one.

The following outlines the highlights of the program, minimum advisor requirements, advisor benefits and book finance documentation requirements:

Loan Program Highlights:

- For SASP & Non SASP Advisors
- Minimum \$100k per loan
- Maximum of \$3.5 million for total program
- Laurentian Bank, on demand:
- SASP at Prime plus 0.5%
- NON SASP Prime Plus 0.75%
- Option for fixed rate/term
- Payment schedule - a maximum of 5 years

- Limit of 50% of Security Value of Advisor Total AUA.
- Security Value - 3 times 75% of Gross Annual Trailer Commissions
- Available only for the purpose of expanding the Advisor's AUA book and/or business
- Secured by pledge of Advisor Book and Guarantee of IPC-FN or IPCL (not IPC Inc or Dealerships).

Minimum Advisor Requirements:

- Minimum investment of 25% - cash or existing book
- Meets IPC's professional standards
- Clean compliance review of purchased book
- Clean background check on Vendor
- Agreement to include non-compete and non-dealing clauses
- Personal guarantee of Advisor if loan to corporation
- Guarantee Agreement, between IPC and Advisor; providing on default for:
- Termination of registration
- Purchase option on the book, at 75% of Security Value

Advisor Benefits:

- Low interest cost
- IPC will support transfer transactions
- Can accelerate growth in Advisors' business
- Succession Planning
- Sellers have opportunity to get larger portion in cash
- Predetermine arrangements for death or disability
- Special deals for SASP Advisors

Book Finance Information and Document requirements:

To get the process rolling, please provide the following documents so that we may present your application to Laurentian Bank.

- \$500 cheque payable to Laurentian Bank, for the loan application fee
- \$2,000 cheque payable to Investment Planning Counsel Inc. for loan package/submission documentation and loan guarantee legals, \$1,000 of which is refundable if the loan does not proceed
- Loan amount requested
- Direction for distribution of proceeds of the Loan
- AUA/GDC Data

- List of Clients, Dealer Rep Codes & Current AUA for your existing Book, along with a Statement of Gross Trailers and GDC for the last 12 months
- Resume of your work history and details of business achievements
- Information to obtain Credit Bureau Report
- Full Legal Name
- Full Residence Address and Phone Number
- Social Insurance Number
- Birth Date
- Support for Net worth Statement
- Statement of Cash & Equivalents from Financial Institution
- Most recent Municipal Assessment Notice for Real Estate
- Description, perhaps itemization, of Personal Assets
- Recent Mortgage statement from Lender
- Recent Credit-line statement from Bank
- Personal tax returns for the last 3 years, including copies of Business Income Statements and assessment notices
- Description of operations in the event that you operate through a Corporation, including:
 - Commission or cost sharing relationships with your Corporation
 - Copies of any material contracts of the Corporation
 - 3 years of financial statements

For further details on the **IPC Book Financing Program**, please feel free to contact Frank Sagebiel at fsagebiel@ipcc.org.

Transition Plan

All the details have been worked out, the deal looks like a “go”. At this stage, it’s vital to both seller and buyer that a transition plan has been established to maximize client retention.

The transition includes everything from repapering the business, introducing the new advisor to the clients and the buyer and seller working together for a period of time to ensure a smooth “hand off”.

A successful transition plan should include the following:

- Client communication plan outlining the new value proposition of the buyer and what’s in it for clients!
- Address any staff issues, i.e. job security, job roles, and any compensation changes
- Quickly setup client meetings and/or client events for the seller to introduce the successor advisor

Formula for Success

A successful transaction is one where everyone wins, the seller, the buyer and the clients. For this to happen:

- The price needs to be fair to both parties
- They buyer and seller have to work together towards the common goal of retaining client assets
- The clients must see the change as a positive outcome for their needs and not simply a purchase/sale agreement

Eventually, every advisor will leave the business on the account of retirement, career change, disability or death. Since a practice is largely valued based on predictable and repeatable revenues, sellers need to focus on continued growth of revenues, pay attention to expenses and improve profitability. Buyers equally need to carefully assess the value of buying a practice and what advantages it will create for the overall practice and clients.

In considering an exit strategy within the next five years, now would be a good time to evaluate your practice and commence some succession planning. A long term exit strategy might include:

- Hiring a junior associate with a view of having them acquire your business over time
- Enter into a “buy/sell” arrangement with another IPC advisor
- Enter into confidential discussions on pre-selling your practice with IPC using The IPC Senior Associate Share Program
- Consider the SASP to create an additional retirement portfolio over time and to protect your estate

To support you in either side of a transaction, your IPC partner is here to help. Please feel free to contact Frank Sagebiel at fsagebiel@ipcc.org.