Practice Continuation Agreements:

A Practice Survival Kit

A resource prepared by the American Institute of CPAs (AICPA) and the National Association of State Boards of Accountancy (NASBA), adapted from the original AICPA publication by John A. Eads, CPA.

What would happen to your clients and practice if you were to become incapacitated or unexpectedly pass away? Do you have a plan in place to ensure your clients' services and your employees' salaries continue uninterrupted? Unfortunately, few sole practitioners do. In fact, a 2016 survey by the AICPA Private Companies Practice Section (PCPS) found that only 7% of sole practitioners have a practice continuation agreement in place.[1]

A practice continuation agreement is a contract that ensures your practice is transferred to another CPA firm or individual in the event of your disability or death. These agreements make arrangements for both temporary and permanent situations, thereby protecting your clients, your staff and your family. Practice continuation agreements ensure that there is no significant break in your clients' accounting and tax services, provide your staff with some assurance of immediate future employment and offer your family financial support and peace of mind when they need it the most.

[1] American Institute of CPAs. (2016). AICPA PCPS Succession Survey, single-owner firms.

Board of Accountancy Considerations

Boards of accountancy throughout the 56 U.S. jurisdictions are responsible for the licensure and regulation of CPAs and public accounting firms. Before entering into a practice continuation agreement, it is important that you and your attorney familiarize yourselves with the laws and rules of your jurisdiction to determine what restrictions, if any, exist regarding the creation and implementation of a practice continuation agreement.

For a list of boards of accountancy, go to the NASBA website at nasba.org/stateboards.

Types of Practice Continuation Agreements

While individual agreements can vary considerably, the three most common types of practice continuation agreements include:

- **One-on-one agreements** — A continuation agreement made between two sole practitioners — usually in the form of a buy/sell agreement or cross-purchase agreement
- **Group agreements** — Several CPAs act as successors to each other's firms; when death or disability strikes a member of the group, his or her clients are asked to select a new CPA from among the surviving members
- **State society plans** — Also known as an emergency assistance plan, these help the surviving spouse or heirs with the disposition of a member CPA's practice if that member failed to make his or her own arrangements ahead of time

For more detailed information on what to include in your agreement and for sample plans, access the AICPA Practice Survival Toolkit at ***aicpa.org/PracticeSurvivalKit.***

Working Toward a Practice Continuation Plan: Key Steps

01

PRACTICE ANALYSIS

A realistic review of your firm's goals, procedures and characteristics prepares you to compare practice philosophies, clients, marketing techniques and personnel policies with prospective successors.

Firm Basics
Honestly evaluate your firm's:

- Reputation
- Specialties
- Rates
- Efficiency
- Staff
- Location
- Profitability

Financial Considerations
There are significant control statistics that indicate a practice's financial health and should be discussed during negotiations with potential successors. For a sample list of these, go to AICPA's Survival Kit website at aicpa.org/SurvivalKit.

Client Information
A critical step in preparing for practice continuation discussions is to summarize basic data about each client. This includes information on each client's type of business, years with firm and billings by type of services rendered. Client profiles may also include an assessment of client personalities, business philosophies, and goals.

Sample valuation methods are available at ***aicpa.org/PracticeSurvivalKit.***

02

PLACING A VALUE ON YOUR PRACTICE

In a normal buy/sell situation, the seller actively participates in the negotiations at the time of the sale. However, this is not possible when death or some types of disability occur. As such, both parties to any continuation agreement will need to agree to the valuation method as part of that agreement. There are several methods for assessing the value of a practice, but the balance sheet and income statement from operations are vital components of any valuation.

03

IDENTIFYING A POTENTIAL SUCCESSOR

The ideal successor is a practitioner you have known for a number of years and with whom you have discussed a wide range of practice issues, including personnel-related and engagement-related matters. You should consider the following when assessing a potential successor:

- **Professional qualifications** — Recent peer review, organizational and planning abilities, proper monitoring and control of engagements, technical proficiency, client satisfaction, ability to train and develop staff, ability to generate fees and knowledge of the value of the services performed, ability to bill and collect promptly, and sense of professional responsibility
- **Personal qualifications** — The appearance and presentation of the firm and its personnel, leadership within the firm, evidence of oral and written communications skills, good relations with colleagues and clients, gradations of expertise within the firm, useful mixture of personalities within the firm, and growth potential
- **Community and professional standing** — The firm's image, leadership in the community and profession, ability to bring in new clients through individual contacts, and accomplishments

Constructing an Agreement

Once you place a value on your practice and identify your successor, you are ready to begin negotiating and constructing the agreement. You may want to consult with an attorney as part of the negotiation process, as your contract will cover many technical legal areas. At a minimum, your contract should address the following:

- Definitions (temporary disability, permanent disability, death, retirement, etc.)
- Assumption of a practice on a temporary basis (in the event of disability)
  — Assignment of staff and other employees
  — Compensation arrangement with the successor
  — Conclusion arrangement
- Assumption of a practice on a permanent basis
- List of clients
- Working papers (tax and accounting standards applied to each client)
- Files (billing, personnel, etc.)
- Books and financial statements
- Work in process and accounts receivable
- Equipment and supplies
- Existing leases
- Employee records
- Liabilities and malpractice insurance
- Property and casualty insurance
- Fees and billing information
- Payment for the practice
- Noncompetition clause
- Termination of the agreement
- Arbitration
- Client notification, including transfer of files

Once the agreement is completed and signed, make sure to inform your attorney, staff and spouse of the details to ensure the smooth transfer of the practice. You should also inform your clients at the time you enter into a practice continuation agreement so as to prevent any surprises down the road.

Payment Methods

Generally, you must be willing to agree to multiple installments to get a good price, as your successor may have minimal available funds or be unwilling to make a full commitment to the terms of the agreement until they can be sure of client retention. The most common method of paying for an accounting practice is to spread the payments over a period of five to seven years. Some agreements have called for payments in as few as three years, and others in as many as 10. Down payments are between 10% and 20%. Outright cash payments for an accounting practice are uncommon unless severely discounted.

Make it as easy and financially undemanding as possible for the successor to pay for the practice. Remember, the successor must pay your staff immediately — long before receiving fees from the clients transferred.

Developing a Practice Continuation Agreement

Sample Action Plan

This action plan can be modified to suit your purposes, and resources for each step are available at aicpa.org/PracticeSurvivalKit.

1. Review the kinds of practice continuation agreements

- Summarize the pros and cons of one-on-one and group plans and decide what's best for you
- If your state society has an emergency assistance program, review it to determine its benefits

2. Make basic preparations

- Determine what effect your business and personal objectives will have on your choice of successor, the valuation of your firm and your preparations for negotiation
- Conduct an assessment of your firm's reputation, specialties, rates, efficiency, profitability, location and staff
- Get your practice into shape. Update your client files and prepare client information for review by your successor

3. Assess the value of your practice

- Choose a valuation method, and consider using more than one to establish a range of values for negotiations
- Prepare a valuation of your fixed assets, accounts receivable and work in process

4. Search for a successor

- Consider the options: your staff, other sole practitioners, previous employers or a larger firm
- Draw up a list of possible candidates and then reduce the list to the most likely prospects.
- Approach the candidates and hold preliminary talks — avoid any rush decisions

5. Begin formal negotiations

- Determine the subjects of negotiation
- Set limits on how much you are willing to compromise

6. Implement the plan once negotiations are completed

- Contact your attorney to prepare a draft agreement
- Discuss your plans with your spouse and attorney
- Finalize letters of instruction to spouse, clients, attorney and staff to be delivered in the event of your death
- Communicate in writing to all parties what their roles in the transfer will be
- Ensure that all copies of the agreement and relevant documents are secure
- Set up a meeting with your successor
- Set up a date for the first annual review of the agreement