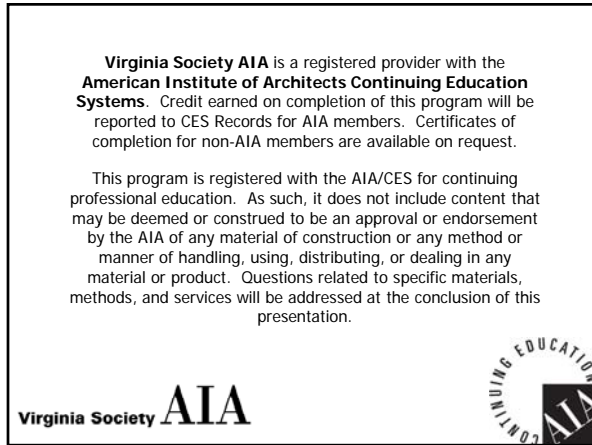
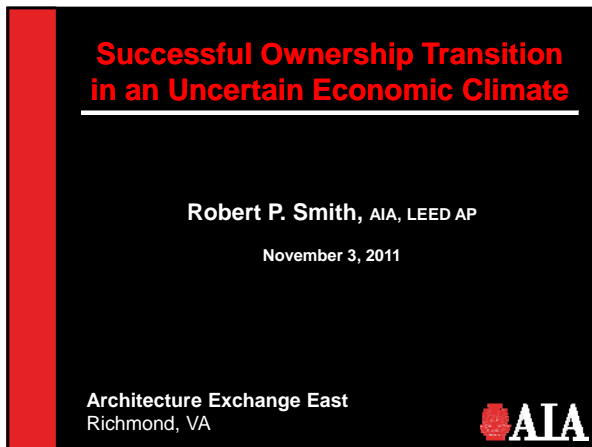


Successful Ownership Transition in an Uncertain Economy

by: Robert P. Smith, AIA







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Learning Objectives

Participants in this program will be able to ...

- ... determine WHEN to begin the transition process.
- ... define WHO represents the most appropriate candidates to lead the firm going forward.
- ... describe WHAT information to share with the selected candidate(s) as the process unfolds.
- ... recognize WHY ownership transition is primarily a "management" – not a "stock transfer" – issue.



This Program's Basic Assumption

In the vast majority of cases, the successful *Internal* Transfer of Ownership is in the best interests of sellers, buyers and your clients.



... but, what about hard times ?

Cyclical downturns can lead to:

- Severe declines in firm's backlog
- Severe reductions in firm's cash flow
- Loss of employees who might be buyers
- Shrinkage of sellers' retirement portfolio
- Unanticipated behavior
- Considerable uncertainty



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O.T. Plans must be flexible

- Our operating environment isn't wholly predictable
- However, economic cycles are inevitable
- O.T. requires a long-term perspective
- Since uncertainty cannot be avoided ... O.T. plans must be flexible



What are we talking about here ?

Fundamentally,
power and control

- who has it now,
- who'll have it next,
- managing the hand-off



Two Primary Forms of O.T.

- **Internal** - Equity transfer with insiders
 - Hand-picked successors
 - All staff via an E.S.O.P.
- **External** - Equity transfer with outsiders
 - Merger with another firm
 - Acquisition by another firm.



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Why transfer ownership - anyway ?

- Provides liquidity to current owners & their estates
- Extracts built-up value
- Demonstrates continuity to outsiders
- Helps aging owners 'wind down' gradually
- Keeps valuable professionals at the firm
- Rewards past performance
- Motivates future contribution
- Expands the pie for all



Ownership Transition Considerations

- **Managerial Considerations**
 - Planning the transition process
 - Selecting & developing successors
 - Preparing the firm
- **Technical Considerations**
 - Transfer methods
 - Valuation techniques
 - Writing the transfer plan
- **Legal and Accounting Considerations**



Planning the Transition Process

- Be clear and realistic about your **goals**
- Start **long** before you think it's necessary
- Approach OT **primarily** as a management issue
 - Identify potential candidates
 - Provide management development for candidates
 - Disclose relevant information to candidates
 - Establish a realistic transition schedule
 - Define firm governance during transition



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5 Key Questions

- WHO - are the appropriate candidates ?
- WHAT - information should you share ?
- WHEN - is the right time to begin ?
- WHERE - do you go for more help ?
- WHY - is this so difficult for us ?



WHO are the appropriate candidates ?

... what criteria do **you** think candidates should meet before being invited to become an owner in a firm ?



WHO are the appropriate candidates ?

- Emotional maturity
- Professional contribution
 - Project work
 - Client relationships
 - Rain-maker
 - Leadership skills
- Shared values
 - Work ethic
 - Teamwork
 - Integrity
 - Community involvement
 - Long-term Orientation



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All firms have different needs ...

... while your own criteria may be complex, try **always** to address the firm's long term needs.



WHAT information should you share ?

- Confidentiality Agreement
- History of the Firm
- The Firm's Long Range Plans
- What it **Really** Means to be an Owner
- How the Transaction will Occur
- Ownership Guidelines
- Financial Statement Highlights
- Summary of Shareholders' Agreement
- Copy of Shareholders' Agreement



WHAT does it mean to be an Owner ?

- Exposure to Risk
 - operating losses
 - loss of capital
 - debt guarantees
 - professional liability
- Business Development
- Staff Development
- Managerial Responsibility
- Community Involvement



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Motivations and Concerns

Sellers

Buyers

- Control Relinquish reins slowly Assume reins quickly
- Price As high as possible As low as possible
- Payout Period ... As short as possible As long as possible
- Initial Cash As high as possible As low as possible
- Perks Current level What makes sense
- Guarantees Maximum Minimum
- Future Role Clarity Clarity



WHEN is the right time to begin ?

- **The Readiness Assessment**
 - the sellers
 - the buyers
 - the firm
- **The Transition Schedule**
 - 5 years is the barest minimum
 - 10 years is more realistic
- **Allow Time for Mistakes**



WHERE do you go for more help ?

- **Professional Advisors**
 - accountants
 - attorneys
 - management consultants
- **Published Materials**
- **Professional Associations**
- **Professional Colleagues**



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WHY is this so difficult for us ?

- **Procrastination** - tomorrow will be soon enough (if it ever arrives)
- **Ego** - 'indispensability' syndrome
- **Power** - discretion to decide
- **Trust & Confidence** - belief that junior personnel never quite measure up
- **Money** - 'market' vs. 'perceived' value



Let's talk a little about 'value'

- Value is not an absolute concept
- Involves the exercise of judgment - not a science



What about 'goodwill' ?

There are two types:

'business goodwill'

and

'personal goodwill'



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Variables in the Valuation Process

- What is being valued
- Date of valuation
- Purpose of valuation
- Accounting methods
- Profitability
- Revenues
- Backlog
- Potential liabilities
- Vulnerabilities



Some Observations about Value

- **Value:** relates directly to firm's ability to provide economic benefits to current and future owners
- **High Value:** reflects 'high economic benefits' accompanied by 'sustainability' and 'predictability'
- **Low Value:** reflects 'low economic benefits' and/or 'uncertainties' or 'vulnerabilities'



Valuation Formulae in Design Firms

- Multiple of Book Value
- Multiple of Net Revenue
- 'Weighted Average' Approach



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Ultimately

- Value = whatever the buyer and the seller agree that it is
- Value arises from sound business practices:
 - business development
 - financial management
 - solid project delivery
 - effective human resources
 - succession planning



Summary

- Start the process as early as possible
- Be honest & realistic about your goals – including expectations about value
- Build in flexibility against uncertainty
- Make the offer in a structured manner
- Manage the OT process like a project
- Work towards a 'win-win' solution
- Change course if it's not working out



**Any
Questions
?**
