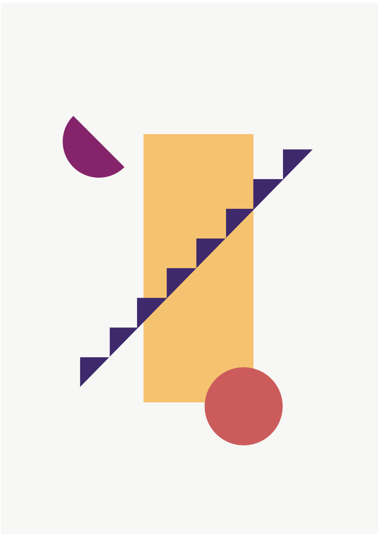
Finding You 2.0

Planning for a Successor

Cetera®



Despite the inevitability of needing one, only 27% of advisors have formal succession plans in place, according to a study conducted by the Financial Planning Association and Janus Henderson Investors.[1] That same study reports that 49% of advisors say the biggest challenge of succession is "finding a successor who can grow and manage the business."[1]

You've spent years—maybe a lifetime—building your business into what it is today. Your clients trust you. Your team follows your leadership. Your processes get results. Ideally, everything you've built would continue indefinitely into the future. Unfortunately, change is inevitable, and the time will come when you need to exit the business. Whether you exit fully or partially, by choice or chance, your practice will change. How that plays out will depend on how much (or little) you've done to prepare.

Despite the inevitability of needing one, only 27% of advisors have formal succession plans in place, according to a study conducted by the Financial Planning Association and Janus Henderson Investors.[1] That same study reports that 49% of advisors say the biggest challenge of succession is "finding a successor who can grow and manage the business."[1] Anecdotally, as witnessed by the Cetera Business Consulting Group, many financial professionals wait until they're only a year or two from retirement before they start planning their succession. The FPA study confirms this observation with the finding that only 39% of advisors within five years of retirement are "fully prepared."[1] That may help explain why so many find identifying a successor to be their greatest challenge. It takes time, effort, and planning to find the right person to run your business, and the sooner you start, the better your chances are.

In the following, we'll walk you through the process of finding and training a successor, starting with the earliest stages of succession planning.

Four key areas of focus

When you start to think about succession, there are four key areas you'll need to prepare for:

- **1. Strategic—**Establishing your timeline, defining your succession, and finding your successor
- **2. Personal—**Setting yourself up for the post-exit life you want
- **3. Structural—**Preparing your firm for sale
- **4. Mechanical—**Structuring the deal

While you're on your own for the personal element, we have the resources to help with all three of the other areas of focus. In this paper, we'll focus primarily on the strategic, but our **Business Consulting Group** is available to help with all your structural and mechanical needs.

[1] *The Succession Challenge 2018: Why Financial Advisers Are Failing to Plan for the Inevitable.* (2018). Janus Henderson Investors, Financial Planning Association.

First, Figure Out Your Goals

How you approach succession planning depends a great deal on what you hope to happen after you leave the business—and what leaving even looks like for you. To begin putting together a plan, you first need to know what you'd like your post-retirement life to look like. You may even have given that same advice to your clients, but if you're like many financial professionals, the old adage rings true: the cobbler's kids have no shoes. When it comes to your own life and business, it can be easy to overlook the advice you give your clients.

Start by asking yourself, "What do I want my post-exit life to look like?" Here are some common scenarios:

- **Complete handoff—**In this case, you would give up all stakes in your business, deregister/de-license, and hand complete control to someone else in a single buyout. With no further involvement in the business once the transaction is completed, you're free to manage your retirement life in any way you please.
- **Remain as owner emeritus—**You might choose to disengage entirely from day-to-day running of the business while still remaining involved as a high-level decision approver, relationship builder/maintainer, and presence at firm functions. Retired financial professionals in this arrangement often focus on bringing in large accounts. It's a way to partially oversee your legacy while removing the burden of daily business operations.
- **Long-term buyout—**You could partner with a successor who slowly buys the business over an extended period of time, giving you gradually less responsibility as time goes on. This tends to work well for sellers and successors who have a longstanding relationship or have determined compatibility for a longer relationship, as it involves a substantial amount of trust and collaboration.

Within each of these is room for nuance and negotiation with your buyer/successor, the terms of your departure can be determined down the road, but it's helpful now if you have an idea of what you might like to pursue. That way, you can begin to think about a timeline, as some of these scenarios take more planning than others.

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Longer Versus Shorter Timeline

Certainly, it's possible to plan your succession with a one-year horizon. Cetera's Business Consulting Group has helped numerous financial professionals go from, "I want to retire in a year," to riding off into the proverbial sunset (sometimes actual, depending on the Winnebago content of that particular plan). A shorter timeline simply imposes constraints that a longer timeline wouldn't. For instance, if you haven't even begun the process of looking for a successor one year ahead of your desired retirement, you'll almost definitely be seeking an external buyer rather than one you've nurtured and groomed in your own practice. Whereas the earlier you start scouting for a successor, the more time you'll have to find—and train, if applicable—the right person. Longer timelines also give you more flexibility in structuring a deal. You can explore longer buyout plans if you give yourself more time to optimize your business for the highest possible valuation. Let's compare your options.

Succession on a One- to Two-Year Horizon

Start by identifying the kind of future you want for yourself, with your time constraints in mind. On a short timeline, a straight buyout may be the easiest option on which to set your sights. A one-year horizon doesn't preclude other arrangements, but the time required to build relationships and work out logistical details might not be manageable. You may be able to position yourself as an asset to a buyer if you stay on in a more limited role, easing the transition between your leadership and theirs. With the right buyer, this can be a tremendous asset, though for some external buyers, it can be seen as a liability. Some new leaders don't like to have their predecessors hanging around.

With a limited timeframe, there are no guarantees about what kind of buyer you'll be able to find and what kind of arrangement you'll be able to come to, but having an idea in mind will help you set your search in the right direction.

Next, understand the valuation of your business. With a shorter horizon, you might not be able to do much to affect this number, but you may be able to make some small improvements, like upgrading your systems. Buyers are looking for practices that work in the modern marketplace, so if you can incorporate small changes like videoconferencing, you may be able to garner a small bump before finding your buyer.

Even if your valuation isn't exactly where you plan to get it, your search for a buyer should begin immediately. Most likely, you'll be looking for an external buyer—unless you happen to have someone with the right capabilities and resources already in your firm. Because the timeline is short, you'll be looking for a more seasoned individual who can take the reins immediately, without a training onramp.

You won't have time for a lengthy and exhaustive search, so you'll likely be looking within your current network or working with a firm that matches buyers and sellers. For example, at Cetera, affiliated financial professionals have access to a matching service that connects sellers with qualified buyers within our network.

Once you've identified your buyer, you'll set to work structuring the deal. Your timeline will limit the length of negotiations, but this stage can often take months on its own. It's a significant factor in limiting your runway to improve your valuation. Even if you were able to implement some value-increasing changes within a year, you realistically have a shorter timeline before negotiations begin.

Succession on a Three- to Five-Year Horizon (or Longer)

When you give yourself a longer lead for planning your exit, more opportunities open to you. Instead of tempering your desired retirement future with concerns over time constraints, you can imagine and set to work pursuing the exact arrangement you want. Set your sights on any scenario, and you'll have time to either achieve it or land on an alternate option.

Among the biggest differences of a longer-horizon succession is that you'll have time to groom a successor. Rather than limiting yourself to external buyers who are seasoned and prepared to fully take over the business, you can look to recruit younger team members into your firm or develop talent already on your staff. You'll have potentially years to identify just the right person to run your business—and to help your successor grow into the leader your clients and team need.

You'll also have a longer timeline for optimizing your business value. If you work with a partner like Cetera's Business Consulting Group, your business's valuation will be coupled with concrete strategies for improving it. Since you will have given yourself years to prepare, you'll have plenty of time to set those recommendations in motion. With a long enough timeline, you can bring younger clients into your book, reduce concentration risk, upgrade systems, and increase the portion of your revenue that comes from recurring sources, such as advisory business.

At the same time, you can begin a broad search for the right buyer. On a longer timeline, you have freedom to look far and wide for your successor. Your search can include recruitment strategies, networking among peer groups, and working with matching services.

Your deal-structuring negotiations will also have plenty of time to evolve naturally. Instead of rushing toward a finish line, you can take your time to make sure everyone involved—including your team—is comfortable with the terms. This is particularly valuable if you're working with a buyer who's not just looking to take over your book but also your staff as well. When you take more time to involve stakeholders in the process, you reduce the risk of critical individuals leaving and increase the value you're able to garner for your book.

In virtually every facet of planning your succession, a longer timeline will serve you better than a shorter one. If it's possible to start planning early, start as soon as you're able.

What About an Unexpected Exit?

Succession planning isn't just about foreseeable exits. If you've been thorough, your plan will include contingencies for if something goes awry and you need to make an unplanned departure from running your business.

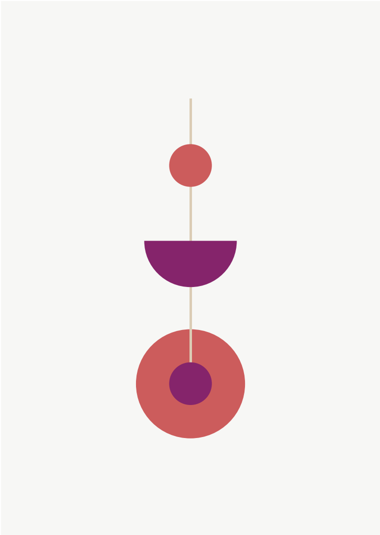
While the ideal scenario is a well thought-out and seamlessly executed retirement, circumstances like early onset dementia or medical emergencies could interrupt even the best-laid plans. All too often, financial professionals will have life and disability insurance but no contingency plans for their businesses.

To help address this gap, Cetera recently introduced a program called **Legacy Builder**, which works like insurance in helping ensure the purchase of your practice in the event of the unexpected.

With Legacy Builder, Cetera will either find a qualified buyer or finance a portion of the transaction with an existing advisor within its network. If no Cetera-affiliated buyers can be identified, we will purchase or ensure purchase of the practice.

Even if your retirement still looks hazy, your contingency plans should be set as soon as possible.

Internal Versus External Successor



If you have $100 million in assets under management and $90 million is with a single client, that would be a significant red flag for an external buyer. To them, it's a substantial concentration risk. To an internal buyer, that risk might not be as significant.

When it comes to where you find a successor, there's no right answer. Sometimes an external buyer is the exact fit you need, but more often than not, your best bet for realizing the full value of your business is finding and grooming an internal successor.

Not only does working with an internal successor give you the opportunity to train someone into the methods and processes your clients and staff are familiar with, but it gives all stakeholders the opportunity to know your replacement. When you leave, you won't be putting them in the hands of a stranger; you'll be offering them the care of someone they know, whom they've seen in meetings and already trust. In terms of valuation, this dramatically reduces retention risk. Clients are less likely to leave if they're already familiar with the new leadership.

Similarly, an internal buyer is already familiar with the clients, which helps them understand the value of your book from a more holistic perspective. For example, if you have $100 million in assets under management and $90 million is with a single client, that would be a significant red flag for an external buyer. To them, it's a substantial concentration risk. To an internal buyer, that risk might not be as significant. They already know and have a relationship with the client, so there's far less fear of them walking out the door. They wouldn't need to discount your value quite as significantly as an external buyer would.

An internal successor also opens the door to more deal structuring options. If you have a long timeline and a known buyer, you could explore options like phantom equity, where the buyer doesn't have to generate capital immediately to begin receiving equity. Often this takes the form of restricted stock units (RSUs) with guaranteed future payment. This can be a great way to work with a younger advisor who might not have access to the resources to buy your business outright, but who can build it up with a little time. Because they're a known entity, you can feel more comfortable offering that flexibility.

Conversely, an external buyer is less familiar with the ins and outs of your business. With a long enough timeline, you can work together on any number of arrangements and reduce retention risk by staying on to help them become familiar with your clients before you fully exit. The main element you're missing with an external buyer is the degree of flexibility and familiarity. It's not out of reach, just more difficult to achieve.

Building Your Bench Strength

In a perfect world, you already have a junior advisor on staff with the management chops to take over your business on your ideal timeline. For many, if not most independent financial professionals approaching retirement, this simply isn't reality—yet. You can get there by building up your bench strength through various recruiting strategies. Ideally, you'd be pursuing multiple avenues concurrently, starting as early as possible.

Possible recruiting strategies include:

- **Create an internship program and path for advancement.** This is a grassroots way to bring new talent into your firm and identify people with leadership potential. As noted in our recent white paper, *Are You Part of the 29%?*, there's a dearth of young talent in the financial services industry. In fact, headcount is expected to decline by 5.8% between 2017 and 2022, compared to a 1.6% increase between 2012 and 2017.[2] Where wirehouses once churned out classes of trained young advisors, there are fewer defined paths for interested young people to pursue today. You can help them find a way into the industry by creating it. Not only does this give you the opportunity to identify a successor, but it's also a great way to boost the valuation of your business, as young staff signal continuity and can help bring in younger clients.
- **Partner with local colleges and high schools.** Whether you start an internship program or not, connecting with academic centers is a great way to find promising young talent. According to CNBC, "There are now more than 200 colleges and universities offering 300 financial planning programs that enable graduates to take the CFP® exam. That compares to about 125 five years ago."[2] By building relationships with local academic centers, you'll be able to make connections promising new talent.
- **Network among peer groups.** In addition to brand-new talent, look within your professional network for young to mid-range advisors who might be seeking new opportunities. With more experience and capital resources, they could be well poised to take over your business on a shorter timeline than someone who's entirely green.
- **Seek career changers.** According to a study by Cerulli Associates, only half of independent rookie advisors are from within financial services, and among that group, former roles include client service or operations, external wholesaler, mortgage or commercial lending, investment research, or product specialist and management.[3] The implication is that advisors are more likely to be career changers than freshly minted college graduates, so in addition to looking for new graduates and peer advisors, build relationships with other individuals within financial services who might be interested in advising.

Additionally, look for career changers within your own firm. You never know what your non-advisor staff has in mind for their futures, so keep a pulse on the aspirations and capabilities of support team.

Anyone with the right skillset can be trained into an advisor, and you may be surprised who's been right under your nose this whole time.

[2] Osterland, A. (2019, June 25). *Firms try to attract and retain tomorrow's advisors.* CNBC. Retrieved from https://www.cnbc.com/2019/06/25/firms-look-to-attract-and-retain-tomorrows-financial-advisors.html.

[3] *U.S. Advisor Metrics 2018: Reinventing the Client Experience.* (2018). Boston, MA: Cerulli Associates.

How To Identify A Successor

As you ramp up your recruiting strategies and build your bench strength, it's important to know what you're looking for in a successor. While it may be tempting to create a demographic profile in your mind—someone within a certain age range with a certain amount of experience—it will be more useful to focus on character traits and mindset.

Succeeding as a leader takes an entrepreneurial spirit, which you likely know well. When things get difficult, who's more likely to handle it well: the youngest advisor on your team who regularly works nights and weekends to go the extra mile or the mid-range advisor who always leaves at 4:30 p.m.? Work/life balance is important, but if you're looking for someone to protect the business you've built, you'll want someone who cares as much as you do.

You'll also want to look for core competencies like business acumen and tech savvy. Technology is rapidly evolving, and business strategies are evolving within the financial services industry. When searching for a successor, look for someone who has the ability to weather changes and take your practice into the future.

Most importantly, you're looking for someone whose service mindset matches your own. Your clients have grown with you, and they've come to expect the kind of service you deliver. If they're suddenly subjected to someone whose style dramatically differs from your own, it could create discord and unhappiness for all parties. Even if you've completely exited the business, you'll want to know your clients are being cared for the way they expect (and deserve).

Training Your Successor

Whether you're training an internal successor or selling your business to an external buyer, the most helpful thing you can do is let that person into your key client relationships. The closer you are to the buyer, the more you can share about the clients and your processes, but at a minimum, you'll want to provide opportunities for the new leader to show their face. Give the clients a chance to learn who they are before they take over, and help them build trust in each other.

With an internal successor, you can take a gradual approach to involving them in management decisions, gradually shifting control to them. During this period, you can use key meetings as coaching opportunities. In the earliest phases, you can share your tips for success before meetings and debrief afterward to ask them what they learned. Over time, as they begin to take more control, you can act as a coach, giving them pointers and thorough reviews.

No two training periods will look the same, but as long as you're willing to be transparent and to let go of control, you'll be able to help your successor, clients, and staff find success with the next generation of leadership.

Cetera Resources

Cetera offers resources that help you in every stage of your succession planning journey. Our Business Consulting Group is available to help you with:

- **Staffing strategies—**We'll help you find and develop talent who may be able to take over your business.
- **Buyer and seller matching—**If you're looking for an external buyer, we'll help you find another Cetera-affiliated advisor who's a great match.
- **Valuation—**We'll show you where you are now and walk you through strategies for raising the value of your business.
- **Deal structuring—**When it's time to draw up a contract, we'll help you reach terms that work for all stakeholders.

Cetera's Legacy Builder program is also available to protect you in the event of an unplanned exit, offering assurance your practice will be purchased.

If you’re looking to partner with a firm that will help you build and protect your legacy, contact the Cetera Business Development team at **800.336.8842.**

About Cetera Financial Group®
Cetera Financial Group (Cetera) is a leading financial advice firm. It empowers the delivery of an Advice-Centric Experience® to individuals, families and businesses across the country through independent financial advisors as well as trusted tax professionals and banks and credit unions. Located at 200 N. Pacific Coast Highway, Suite 1200 El Segundo, CA 90245-5670

Comprehensive services include: wealth management solutions, retirement plan solutions, advisory services, practice management support, innovative technology, marketing guidance, regulatory support, and market research.

“Cetera Financial Group” refers to the network of independent retail firms encompassing, among others, Cetera Advisors, Cetera Advisor Networks, Cetera Investment Services (marketed as Cetera Financial Institutions and Cetera Investors), Cetera Financial Specialists, and First Allied Securities. All firms are members FINRA/SIPC.

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