

Succession: a tough nut to crack

Succession is a tricky issue for small firms and early planning is vital, says *William Franklin*



William Franklin

William Franklin is a founding partner at PettFranklin LLP pettfranklin.com



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Succession and how to approach it is one of the most difficult issues facing a niche firm today, but it is a vital issue.

At my firm, we are not about short-term thinking; it's not about senior lawyers working at the back end of their career for a couple of years on a few existing clients after leaving a large firm.

We train people for the future and firms and other professionals have a moral obligation to do so. But at the other end of the spectrum we must consider the matter of succession.

Although we are a training firm – and our trainees get an excellent training – one of our problems has been retaining them. This is because once qualified their training experience with us means they can be lured away for large amounts of money by big competitors who don't show quite the same commitment to training – and that is a problem for many niche firms.

Working to hang onto them after qualification so they then form part of the firm's succession plan is a perpetual challenge.

Firms need to consider the issue of succession regularly

because they need to have continuity when partners retire or want to do something else. Clients want and need to know there's a plan for succession and contingency should their lawyer leave.

Around three years ago, we went through the retirement of my co-founder. When we first established the firm 10 years ago, the thought that PettFranklin would be more successful than ever without him might then have seemed inconceivable. But we got through his retirement and the firm became stronger because we anticipated change and succession planning.

However, it's not easy and I would not say we have entirely cracked it. You have to keep working at it. It is, for example, important to have a conversation with the individual early on. You need to actively discuss the issue with them because you've got to be thinking all the time about the long term.

You also need to work out what is in the best interests of the clients, the firm and the individuals – in that order.

And you need to be adaptable: circumstances can change – sometimes quickly. When you are working in a small team, something unexpected or unanticipated might happen to one individual which means you have to change your plans, for example, serious illness, sudden deaths and unexpected family situations.

This means you must always be flexible, thinking ahead and having another plan as well as your main plan. Having a plan B is absolutely essential.

There is a deeper question which applies to all firms – but perhaps most urgently for smaller firms where new equity partners are expected to contribute capital to help fund at least the working capital of the business. That question is whether the traditional partnership model of ownership, including the current limited liability partnership (LLP) form, is sustainable in the long term.

LLPs do continue to have tax advantages compared with a limited company model, and value can be shifted between the owners without creating capital gains tax disposals. That flexibility gives an LLP advantages over a limited company. Equity partners are taxed as self-employed so their compensation is not subject to employers' national insurance.

But the LLP model requires working capital to be funded out of after-tax profits; while a limited company can be funded from retained earnings, which have only been subject to corporation tax. This is still substantially lower than the tax on partners' profits – where the tax is also paid irrespective of whether or not the profits are distributed.

Succession in a limited company raises different issues from succession in a partnership. It will be interesting to see over the next few years whether law firms attracted to the limited company model will also be attracted to a different business ownership model in the form of John Lewis-style employee ownership – and abandon the traditional concept of partnership entirely. **SJ**

