Vol. 67, No. 5 | May/June 2010

Classifieds | Display Ads | Back to contents

A Second Bite of the Apple: Preserving Income in Retirement

The attorney looking ahead to retirement need not be reconciled to a precipitous loss of income or of the value built up in practice. By carefully planning and negotiating the terms of their departure, retiring lawyers can both ease the transition and come away with more of the value they invested in their practice.

By Roy S. Ginsburg & Eric T. Cooperstein

When approaching retirement, most attorneys take a careful look at their assets to determine when they can retire, as well as get a good idea of what type of lifestyle they can afford. For most, that means a review of their brokerage statements and appraisals of whatever real estate or other tangible assets they own. After all, except for government lawyers, most attorneys do not have a defined benefit plan to pay them income in their retirement.

Or do they?

Instead of riding into the sunset and leaving behind the books of business and referral networks that they worked for years—perhaps decades—to develop, lawyers should evaluate whether their practices can generate value even as they wind them down.

Many lawyers, regardless of the size of their law firm, fail to recognize that their practices may have significant value that can enhance their nest eggs. Depending upon a lawyer's book of business, practice area, geographic location, and degree of advance planning, it is very possible to derive value from one's practice to either enjoy during retirement or pass along to one's heirs.

Valuing Your Practice

We've all heard stories of the lawyer who died at his desk without giving any thought to transitioning his practice. When that occurs, as a practical matter, there's little value to recover. If the deceased was a solo practitioner, the estate may collect outstanding receivables but has no claim on future client income. Longstanding clients or clients with open files will simply find other counsel, providing no financial benefits to the deceased lawyer's estate. The result is usually no different if one works in a large law firm. Upon a lawyer's retirement or death, the other lawyers in the firm scramble to maintain the client relationships. Any financial benefits from the book of business go only to the firm's other lawyers.

Even those attorneys who consciously plan a departure date, more often than not, make no attempt to extract any value from their practice. This occurs for a variety of reasons. Some simply do not realize

that there are means to obtain value. Among those who do, some conclude that gleaning what remains is more bother than it is worth. Finally, of those practicing in firms, some apparently prefer to give the value away to their partners based on feelings of institutional loyalty.

Income-Preserving Exit Strategies
Let's examine the situation of hypothetical lawyer, Sara Sage:

> *Sara has been with Dewey, Cheatem, & Howe for 30 years. At 62, she's earned a comfortable living but is thinking she'd like to wind down. Sara would like to earn some income at least through her late 60s, but she wants to spend a few months a year traveling to see her grandkids, who live in other states. She wants to work part-time and be done in about five years. Sara's book of business is better than that of most of her partners. Her firm doesn't have a mandatory retirement date, but there's no formal retirement plan either. When partners are done, the firm throws a party and the retiring partner sends post cards from Florida.*

Sara has a number of options to consider that will enable her to continue to benefit from her investment in her firm.

Of Counsel—Same Law Firm. A first option for Sara is to go "of counsel" with her firm. Historically, the profession has acknowledged the notion of older lawyers winding down their practices. Especially at larger law firms, attorneys would become "of counsel" and negotiate an arrangement that suited the needs of the law firm and the "of counsel" attorney. This can be a win-win situation: the "of counsel" lawyer may work fewer hours and accept lower compensation, but keep an office, some support staff, and most importantly, his reputation as an experienced practitioner and role as a rainmaker and mentor. The firm is relieved of some financial obligations and continues to receive business and the benefits of the attorney's institutional knowledge or substantive expertise. Most importantly, a well-thought-out "of counsel" arrangement provides a timeframe and blueprint to properly transition clients of the "of counsel" attorney to others at the firm.

As defined by the ABA, the term "of counsel" signifies that the lawyer has a "close, regular, personal relationship" with the firm.1 From an ethics perspective, the relationship provides the firm and the lawyer greater flexibility in sharing fees that may be generated by the lawyer continuing to work on files or from new business originated by the lawyer. Indeed, the advantage of the "of counsel" model is that the terms and conditions of the financial arrangement are usually limited only to the creativity of the lawyer and the law firm. When negotiating its terms, lawyers like Sara with a respectable book of business may have more leverage than they think.

Transitioning clients takes time and effort and one should be compensated for what is, for all intents and purposes, a sale of the lawyer's good will to the law firm. In large firms, management may wrongly assume that some clients feel loyalty to the entity. In a more and more competitive legal marketplace, that assumption could prove to have disastrous consequences when the "of counsel's" client relationships turn out to be far more personal than institutional. On the flip side though, Sara should not overplay her hand. For example, some of her relationships may very well be with corporate constituents who are also retiring and may not be so easy to transition. In small firms, other partners' dreams of taking over the senior lawyer's client base and finally obtaining the full benefit of all the hard work they have done for those clients at no cost may be naïve.

There is no typical or standard compensation arrangement for an "of counsel" lawyer. Much like

partners in any size firm, attorneys "of counsel" typically are compensated based on revenue collected, hours worked, and business brought in. The only real difference is that the formula may recognize the time and effort spent transitioning the attorney's book of business to others at the firm. After all, someone like Sara will be transferring her good will to the benefit of her partners and its worth should be taken into account. Hence, it may be appropriate to pay the retiring lawyer a percentage of the fees generated by other lawyers' work done on behalf of clients formerly handled principally by the retiring lawyer.

The formula should provide incentives for both Sara and the lawyers on the receiving end of the client transition to cooperate with one another. That can sometimes be a challenge for both the law firm and the retiring lawyer. Firms understandably prefer formulas that emphasize a percentage of future fees expected to be generated; retiring lawyers will usually want something more fixed.

Of Counsel—Different Firm. Now let's suppose Sara's law firm offers her an "of counsel" agreement that in her mind undervalues the book of business that she could transfer to others at the firm. Depending upon the portability of her book, she might want to consider going "of counsel" somewhere else. Most law firms, small and large, are willing to talk to 30-, 40-, or 50-something-year-old partners with a book of business who are thinking of switching firms. Smart law firms will similarly want to talk to a 62-year-old partner with a well-thought-out client-transition plan. That plan would include a description of the lawyer's key clients,2 a history of fees billed and collected, hours worked, and an indication of how many years and how many hours each year the attorney plans to work.

This "of counsel" arrangement with a different firm can be a viable option for a lawyer in any size firm, including solo practitioners. Solos and small-firm owners who want to relinquish the duties of running the business of their practice may find the arrangement especially attractive. While some may label the transaction as merely switching firms or a merger, it is in reality an acquisition, but one where the retiring lawyer does not receive cash for the practice. Instead, the lawyer negotiates a compensation package with the acquiring firm, following the same parameters noted above for lawyers who become "of counsel" at their original firm.

Changing law firms in an "of counsel" role is easier said than done. As would be true any time a lawyer wants to leave one law firm for another, the lawyer needs to "shop" the practice to other firms; the market may not be as robust or predictable as one hopes. Furthermore, switching firms can be problematic for all of the familiar reasons, including conflicts, culture, and governance. Most importantly, there are no guarantees that one's book of business will follow to the new firm.

Those who are thinking of moving their practice elsewhere need to be aware that their firm's retirement plan may restrict their ability to practice law while receiving retirement benefits. Although Rule 5.6 of the Minnesota Rules of Professional Conduct prohibits noncompete agreements for lawyers because they limit clients' freedom to choose their attorneys, the rule specifically exempts agreements "concerning benefits upon retirement." The ABA has recently opined that as long as a lawyer is genuinely retiring, a law firm may impose geographic, temporal, or subject matter restrictions on the departing lawyer's practice, or prohibit the lawyer from practicing law entirely, as a condition of receiving the retirement benefits.3

Selling Your Law Practice

Now what if Sara was a solo practitioner or the majority owner of a small law firm? Although ethically proscribed for years, a relatively new exit strategy can be to sell the practice and turn good will into cash.4 The lawyer's client base, the referral network, the law firm's name and reputation, the

firm's phone number, the firm's web domain name—all of these intangibles have value which can form the basis for a selling price.

Even when the ethics rules prohibited the outright sale of one's practice, smart lawyers would seek out potential "successors" and devise a partnership or other contractual arrangement of shared overhead expenses and revenue that enabled the retiring owner to extract the good will value of the practice during the last years of practicing. Under the "successor" model, after a negotiated time frame, the entire practice would then be owned by the "successor."

As a practical matter, whether one sells a practice or finds a successor, the issues that need to be addressed by the retiring lawyer are virtually identical. The only significant distinction between the two is the nature of the legal documentation required to close the deal. Both scenarios offer many advantages. Employees of the practice, if any, can frequently be retained. Someone else becomes responsible for old client files. And the lawyer avoids the problems of dying at her desk, including the burden on heirs of winding up the practice, determining whether any active matters remain, and returning client files.

What problems will Sara likely face? First, she will have to find a buyer. One can do that by advertising, networking, or utilizing the services of a consultant. Likely buyers include:

• Refugees from large firms who are seeking a career change for reasons of lifestyle, inability to make partner, layoff, or conflicts;
• Insiders—minority shareholders or associates who would benefit from being able to retain the firm's name, staff, presence in the marketplace, etc.; and
• Recent graduates "hanging out a shingle."

Buyers are motivated because in theory they can obtain:

• An existing book of business;
• Good will;
• Ability to grow their practice faster; and
• Operating systems and staff in place with known costs and an existing track record.

Assuming Sara can find a buyer, she will next need to reach agreement with the successor on a partnership, value, or other form of contractual arrangement, including a payout schedule. There are no hard and fast rules. Much like selling a home, selling a practice ultimately requires a determination of what someone is likely willing to pay. The most significant factor in trying to value a practice is assessing the book of business. That includes:

• Business that continues from existing clients;
• New matters from former clients that come to the firm; and
• New matters that come to the firm simply based on the seller's reputation.

It should come as no surprise that the value of one's book is largely dependent upon the practice area and type of clientele. For example, if you are retiring from an estate-planning practice, chances are good that the heirs of clients whose wills you drafted will turn to your successor to probate the estate. If you have provided employment law advice to a variety of small business owners and work with your successor lawyer to transition such clients, many will remain rather than search for new employment law counsel after you are no longer around. Contrast that with the practice of a

prominent criminal defense lawyer. Here, transferring any good will is extremely problematic; the good will may be too personal in nature.

Enter the number crunchers. Some parties emphasize current earnings to support a value; others look to the expected earnings. Still, others use a market- or asset-based approach. Both buyers and sellers should consider the impact on value of economic trends in the practice area and the competition, as well as the tax consequences of the practice transfer. Whatever approach is taken, once the practice is valued, the payout of the purchase price or other agreed upon arrangement can be structured over a period of several years, providing an income stream to the retiring lawyer and allowing the buyer to stretch out the payments enough to make a living in those first few years of the transition.

One difficulty of selling an active practice is how to allow the buyer to conduct a due diligence inspection of the quality of the existing client matters without breaching client confidentiality. As a threshold matter, individual files may not be sold; Rule 1.17 requires that the “entire practice” be sold, save for conflicts files or matter in which the buyer would not be competent.5 Similarly, Rule 1.17 addresses confidentiality only in the context of the client’s failure to respond to a notice from the lawyer that the entire practice has been sold and that the client’s file will be transferred.6 But in the negotiation phase, a buyer cannot be permitted to casually peruse client files to determine their value. Instead, selling lawyers may have to make lists and summaries of client matters for inspection of the buyers. Those lists may also need to be incorporated by reference into the sales agreement, so that the buyer has some recourse if the seller misrepresented the merits of the matters.

Plan Your Retirement

John Kennedy once remarked that “the time to put on a new roof is when the sun is shining.” All of the retirement strategies discussed in this article require time—time to determine the best strategy and then time to implement it. Transferring client relationships and one’s caseload requires effort; it will not just happen overnight. The bare minimum amount of time required is probably one year. And depending upon the pace at which the retiring partner wants to wind down, the complete transfer may last as long as five to seven years. In any event, if you intend to retire, it is time well-spent to ensure that you can spend well during retirement. #

Notes

1 American Bar Association, Formal Op. 90-357 (May 10, 1990).

2 As with any lateral transfer, the moving lawyer must maintain client confidentiality, which may require, in the early stages of negotiation, descriptions of the lawyer’s clients without immediate disclosure of their identities.

3 ABA Formal Opinion 06-444, “Permissibility of Restrictive Covenants in Lawyer Agreements Concerning Benefits Upon Retirement” (Sept. 13, 2006).

4 *See* Minnesota Rules of Professional Conduct, Rule 1.17.

5 *See* Rule 1.17(c).

6 *See* Rule 1.17(e). If the client does not respond to the notice, the client is deemed to have waived confidentiality for purposes of transferring the file to a new lawyer.

Roy S. Ginsburg *is an attorney coach who has helped numerous lawyers nationwide achieve practice development goals and career satisfaction. While maintaining his private practice of law on behalf of a select group of clients, Roy has coached a variety of lawyers on how to best plan for their retirement and is a frequent CLE speaker. Bar associations and law firms all across the country have sponsored*

Roy's programs, which are designed to help lawyers create successful and satisfying careers.

***Eric T. Cooperstein** has a solo practice devoted to ethics consulting and representation, a product of his work as a former senior assistant director of the Office of Lawyers Professional Responsibility. Eric defends lawyers against ethics complaints, provides advice and expert opinions, and represents lawyers in fee disputes and law firm break-ups. He is also a qualified neutral and a frequent writer and speaker on ethics and law practice issues. Eric will serve as secretary of the Hennepin County Bar Association beginning July 1, 2010.*

The authors acknowledge with thanks the contributions of Pete Peterson, an attorney with the law firm of Maxfield Peterson, P.C. of Grand Junction, CO, who helped in development of this article.