

**Planning for the Sale and Transitions of a Law Practice Under Rule 1.17
of the Illinois Rules of Professional Conduct in the Event of the Retirement, Death or
Disability of a Sole Practitioner**

By John T. Phipps

GENERAL CONSIDERATIONS

1. Retirement can be planned and orderly. Planning for sudden death or disability is an exercise in contingency planning. There are many contingencies involved in planning the transfer of a law practice and each lawyer's practice creates its own unique planning problems. Retirement involves the same type of planning but allows more time and options rather than forced decisions created by a sudden disastrous traumatic event. There are no definitive answers but better planning and organization will ease the transition, protect the clients, reduce costs and create maximum return for the practice. This article outlines the issues to consider for both retirement planning and sudden post disaster transition. The timetables are based upon sudden events but sales associated with retirement planning involve the same issues and the timetable can be adjusted for the circumstances.

- **Illinois Rules of Professional Conduct Rule 1.17 transfer rules.** Since 2005 Solo practices can be sold in Illinois under the Illinois Rules of Professional Conduct Rule 1.17. Under the current rules, which went into effect January 1, 2010 the transfer requirements have been eased to allow for a quicker more orderly transfer. The current Rule gives a lawyer more flexibility to determine how to dispose of the practice, because the amended Rule removed the time lines for transfer actions. As a result proper planning can shorten the time needed to accomplish some critical tasks in order to more readily protect clients and provide the opportunity to minimize the post transition event expenses, maximize fee and overhead cost recovery, and a bring a greater price for the practice. Notice of the sale must be given regarding the sale. Included in the notice must be a statement that the client's consent will be presumed if the client takes no action or does not object within 90 days of receipt of the notice. However the client can give immediate consent to the transfer or provide instructions about how to handle the client's file. As soon as the client's consent or instructions are received appropriate actions can be completed. A sample notice and consent is included in the appendix.

- **Transition Time Reality.** In planning for a transition it is important to recognize that it will take time and effort to transfer a full time law practice to another lawyer or a law firm which also has a significant work load. The process will not happen overnight and allowance must be made for this reality. At the same time, care must be taken to be able to promptly respond to the needs of the firm clients.

- **Keep the office open.** No matter what happens it is critical that the office be open for at least a short time to cover the transition and meet the client's immediate needs. It is important to identify who will open and manage the office in the event of an emergency especially if the lawyer is unavailable. Clients have needs that must be served in a reasonable manner. Clients are distressed to lose their lawyer. When the phone rings someone needs to answer the client's questions and respond to critical needs and deadlines.

- **Staff.** What you do and how you do it also depends on whether or not you have an office staff. A well trained staff is important in dealing with the issues created by a sudden

emergency.

- **No Staff.** If you do not have a staff to assist, the contingency planning is even more critical because there is no staff to act for you or to follow up on what needs to be done if an unexpected problem occurs. Pre-arranging for a lawyer to cover and manage your cases during the transition becomes especially important. Also, it is important to have someone monitor the phone, mail and email. Good organization, written emergency checklists and plans are essential to provide guidance to whoever covers the office. Case management systems are critical to protect clients, preserve value and avoid problems. Such systems can prevent delay and maximize the practice value.

- **With Staff.** If you have a staff you can work out transition plans using your trained staff to manage the office, ease the transition and protect your clients. Retaining staff is a critical factor in being able to bill for and collect for ongoing work and unbilled fees as well as make a prompt and cost effective transfer. It is important to recognize that it takes time to transfer a thriving practice especially when the acquiring lawyer or law firm already has a good practice. Having your staff available is essential to protect clients, identify deadlines and triage the work so that that the most important work is done on a timely basis. In fact in many law practices the retention of knowledgeable long term assistants and paralegals who can help manage the caseload adds value to the practice. As with the no staff situation, written emergency checklists and plans are important.

- **Prospective Buyers** - What's going on economically in the area and what the climate is like for developing profitable legal work from your practice will greatly affect the sale potential. If possible identify potential buyers and make a contingency continuation or sale agreement with that lawyer or firm. If locating prospective buyer is not possible, at least try to arrange for a lawyer or firm to manage the files and cover the practice during the emergency transition. For example in a disability situation in Champaign County, a lawyer with a juvenile court contract became suddenly disabled so with Court approval a number of lawyers who worked in the juvenile Court area volunteered and took over his cases while he was disabled. There are many different ways to do this so look at your practice and determine a solution that works for you and your practice and then work out contingency plans with potential buyers or transitional lawyers. Even an informal agreement with another lawyer supported by a written continuation plan or checklists can be effective and protect you and your clients.

- **Practice Information** – The buyer will need to review the firm's practice information to determine value and whether or not to buy the practice. This information must be handled on a confidential basis. A form of confidentiality agreement is included in the appendix.

- **Simplify Plan** - Simple works. The contingency plan should have enough detail to be informative and the office should be organized sufficiently for the plan to work. The plan must be easy to understand and flexible enough to work in a highly stressful, short notice situation. That is why checklists are helpful. Most important is to put in place corporate resolutions, powers of attorney and written authorizations to permit prompt action to protect both the practice and the clients when the lawyer is unavailable. The goal is to reduce the transition workload as much as possible.

- **Passwords** – Make sure someone has access to all your passwords. Your plan will not work if your representative cannot access your office files, emails, data stored in the cloud and

backups.

- **Authorizations.** Critical to effective disaster planning is to make sure that the person who will step in for the transition has legal authority to cover and act on behalf of the practice and the lawyer. See the new Illinois Digital Assets Act for guidance on digital asset authorizations.

- **Powers of Attorney.** Authorizing a named licensed attorney to specifically cover the practice and bank signature authorizations which become effective upon the occurrence of a disabling or other event should be in place to enable the attorney to cover the practice. Sample language for a Power of Attorney is:

This power of attorney shall become effective on the earlier of (a) receipt of written certification from my physician, Dr. _____ or the then primary licensed physician then attending me that I have become incapacitated to such an extent that I am unable to transact ordinary business prudently, (b) the date on which I am adjudicated legally disabled, and (c) or upon receipt of my written statement that I am unable to act or that I authorize this power of attorney to be immediately in effect. Any person dealing with my agent may rely without liability on a photocopy of such written certification. In such event my agent, who is a licensed Illinois attorney, subject to the requirements of the Illinois Code of Professional Responsibility manage my cases and my client matters, shall have all of the powers and authority to act for me in all matters involving my law practice, including, but not limited to, the authority to execute checks, manage and transfer bank accounts, trust accounts and take all necessary or appropriate actions in order to transact any and all of the business of my law practice.

- **Corporation or LLC.** If the practice is a corporation or LLC a contingency plan resolution, similar to the ones in the Appendix can be adopted. This will enable the designated lawyers to continue to operate the office without interruption even when the lawyer dies.

- **Will.** The lawyer should also include a provision in his or her will authorizing a lawyer to be hired and to act for the estate in dealing with the practice. A sample will provision regarding the operation and disposition of the practice is included in the Appendix.

2. **Case management systems.** Case management systems are critical to facilitate a quick and successful transition. These systems provide a computer list of all your cases, current appointments, To Do List with time lines, all deadlines, the people involved and how to contact them. A good case management system can also contain a synopsis of the case and progress notes for immediate reference. Using case management systems can assure timely action in the event of a sudden death or disability as well as add significant value to the practice because of the ease of access to case information. *Amicus, Time Matters, Abacus* and *Case Master* are the most popular computerized case management programs. If you don't have one, pick one and start using it. Case management programs become more valuable and useful as you use them and add information. Most case management programs also have highly sophisticated features that are useful. But the basic features included in the limited editions of these case management programs are enough to provide the necessary information to allow other lawyers and staff members to timely respond to practice needs in the event of a sudden death or disability. You do

not have to use all of a program's features to benefit from the power of a case management program. Even a system developed using Outlook or a similar program can add significant value. Some case management programs can be expensive so a cost benefit analysis is important in determining what works for a practice. In the retirement situation additional transition information and planning data and case management notes can be added to each case to further enhance the practice value. The notes and task lists features can also be refined to add even more value to the practice because they ease the transitions by giving details regarding what has been and should be done with the case.

3. **Checklist for Executor or Representative.** At a minimum, you should have a checklist of items to do in the event of disability or death and have the office organized so your files can be handled expeditiously and your clients protected. The same lists apply to retirement but the time frame expands to fit the situation. The following list can be adapted to your needs.

A. What to do immediately –

Note: It is not disrespectful to start the practice coverage and transition work immediately. It may be difficult to work in such a stressful time but a delay of a few days, or in some cases even hours, can create significant problems and result in lost fees, lost practice value and problems for clients.

1. Get someone appointed or designated to act.
2. Check calendars, docket and "to do" lists to determine urgent items needing to be done. Immediately, contact all clients, opposing parties, Judges and others involved with the urgent items.
3. Take steps to file deadline items prior to the statute of limitations date and appearance date or get extensions, etc.
4. Get continuances and arrange for an attorney to cover cases needing urgent action so clients are not prejudiced and the clients' case can progress on a timely basis.

Note: Remember time and money spend the first few days as well as the first month to ensure a prompt, orderly transition usually results in a quicker practice transfer, a better collection rate on earned and billed fees, higher value received for the practice, lower expenses, happier clients and fewer problems in the sale or transfer of the practice.

B. First week

5. Make staff arrangements to cover the time the office is expected to be open or until a transfer is completed. Normally you will need to ensure health insurance coverage and income for the staff for a sufficient time so the staff will stay until the practice can be transferred or the office closed. In most cases, the retention of an experienced staff makes a difference in how well the transition is completed and the value received. Good longer-term staff members have relationships with clients, know what to do what it is needed and when to do it, so offering incentives for them to continue is appropriate.

6. Notify all remaining clients and other involved parties of the lawyer's

death or disability. See Rule 1.17 regarding notices to client's and client consents. These notices should be sent as soon as possible to start the clock running.

7. To the extent possible, obtain clients' written consents to have a covering attorney work on the file, review confidential matters and cover short term items. If a buyer has been identified, *this is a good time to get clients' to waive notice under Rule 1.17 and sign a written consent. Such consents expedite the transfer and significantly reduce both the time and work needed to transfer the practice.*

8. Triage work and files to establish a timetable for both client and office administration work including, type of work, the attention needed, and the amount of work involved. It is also important to identify who will do the work and the matter's priority. The following timetable fits most situations.

- a) Immediate
- b) First week
- c) First two weeks
- d) First month
- e) First three months (first quarter)
- f) *Include prompt and timely billing as an important part of the triage.*

9. As part of the triage process identify files to be closed along with any remaining work that needs to be completed in order to close the file.

10. If there is unbilled work needed to get paid, these files get priority to help the cash flow.

11. Billing and collection is important because the more bills that can be completed and/or collected during the first two weeks the better. Collection problems will increase exponentially as time passes and the clients are then relying on another lawyer. These problems can be minimized by fee and collection arrangements with both the covering lawyer and lawyers buying the practice. Client(s) want to be served and normally will continue to pay and stay with the new firm if they see their case is being worked on and the work will be quality work done in a timely manner by the new lawyer or law firm.

Under Rule 1.17 if a client's consent is not obtained there is a "not less than 90 days" notice requirement so this notice period needs to be considered in how long to keep the office open. Clients will then have to be notified about how they can contact the practice representatives if the office is to be closed within the 90 day period.

12. The cost of overhead is a part of the fee calculation. Consequently, it is important to make arrangements for allocation of office expenses and the attorney fees with the person or firm taking over the file or files and doing the work after the event.

13. Stop or at least minimize as many ongoing over head expenses as possible, especially *LexisNexis, Westlaw*, library subscriptions and other recurring costs

14. Consider having the Buyer fund some of the overhead expense especially

part of the payroll costs, when the transition lawyer or law firm will be keeping all or a portion of the fees being generated by the transition work.

15. Arrange for all tax payments and tax return filings to be done on a timely basis or get appropriate extensions.

16. Minimizing overhead is critical to a profitable and successful transition.

C. First two weeks

17. All required Rule 1.17 9- day client notices and other notices need to be sent promptly, but to the extent possible should be sent by at least by the end of first two weeks.

18. Begin arrangements to close or transfer office.

19. Cover all necessary work.

20. Follow up on undone items.

21. Work on bills and collecting fees.

22. Complete arrangement regarding leases, etc.

23. Arrange for storage of office and closed files. Consider file destruction possibilities.

24. Cancel all remaining unneeded subscriptions and expenses.

25. Arrange for tail and transition malpractice insurance for the office staff and estate.

26. Adjust other insurance coverage to meet the new circumstances.

27. Send all rebills that are in process.

28. Consider what to do with websites and lawyer listings such as Martindale-Hubble, West, LinkedIn, Facebook or other lists.

29. Complete substitution of attorney of record, registered agent and other items where a new attorney of record is necessary.

D. End of first month

- Make final decisions regarding sale, transfer or closing the office.
- Make final decisions regarding the transfer of remaining files and any remaining notice requirements.

- Complete arrangements regarding the closing or transfer of the office.
- Triage accounts receivable for collection efforts and write off doubtful collections.

- Make sure all unbilled work on each file has either been billed or fee sharing and collection arrangements have been completed with the lawyer taking over the file.
- Make sure all follow up bills have been sent and all other bills have been sent and put in the rebilling cycle or process. Billing and rebilling tend to get low priority with all the client work involved but must not be overlooked because the collected fees are assets and can help fund the transition and pay current bills.

E. End of first quarter

- Office transition work should normally be completed and the office should be basically closed or transferred to the buyer. However, there may be reasons to keep the actual office or a substitute office open longer.
- Make sure all tax filings and payments are done timely.
- Complete collection of fees if possible.
- Arrange for and schedule completion of all tax returns.
- Wrap up all items remaining regarding Rule 1.17 Notices and arrange for necessary court orders regarding transfers for clients that cannot be given notice or who have not provided direction or objected to the transfer.
- Arrange for mail forwarding. Retaining or transferring a long time post office box may be appropriate to ensure the purchasing lawyer or firm and/or the lawyer or his or her estate receive ongoing correspondence and transfer value.
- Final closing on the sale must, under Rule 1.17, be after the expiration date for the last 90-day notice that has been given. However, if it appears that all clients have consented the sale could close earlier. Also, there does not appear to be any limitation on the ability to close the sale as the transition progresses for those parts of the practice where consents have been obtained during the interim period between the retirement, death or disability of the lawyer and the final closing. With the signed consents it is possible to transfer those client files as soon as client consent is obtained. Quickly processing and transferring files will reduce the transition workload because the office no longer has to deal with those files or matters.

F. End of six months

- Make appropriate tax filings
- Make final collection efforts and normally write off all but those files that do not have specific payment agreements because of the cost of collection.
- Complete all unfinished file transfers.
- Complete all file storage matters relating to the practice information and client files. Make contact arrangements for clients to be able to access older closed files. Make sure original documents, especially wills, deeds and other important documents have been returned to clients.

G. End of first year

- Final tax filings should be completed or scheduled.
- Everything should be completed except payment of client fees that have been agreed to be paid in installments over an extended time.

H. Unique items, other activities and deadlines. In every office there are unique items. These need to be identified as soon as possible and dealt with. They can be things

such as sports ticket seating plans, travel accident insurance, airline and hotel points, airline tickets, guaranteed or prepaid hotel reservations and prepaid CLE courses or other prepaid services or contracts. Many of these may have significant value or in the case of such things as guaranteed room reservations can create unnecessary expenses if not timely cancelled. Preplanning and checking accounting records and calendars will ensure that such items are not overlooked. For example, in my office I have files in my case management program for each reward or prepaid program with the account number, contact information, and details. We show all guaranteed hotel reservations in the calendar on the appropriate date and the hotel file so we have an easy way to verify what reservations are guaranteed so they can be cancelled.

VALUATION

3. Valuation of Practice. The value of a law practice is based upon a prediction of the future based on facts presently in hand. There is no “right” way to value a practice because each practice is unique and each buyer is unique.

- What the selling lawyer wants to obtain is an acceptable return on the practice and its tangible assets including work in progress and stream of future business.

- The buyer wants value for the investment.

- Work-in-progress - evaluate the amount of the expected fees for finishing the current client work will generate. In most offices the value of the amount of work still to be completed on its case files is of significant value because of the amount of fees the current work will generate until the file is closed.

- Practice Information – The buyer will need time to evaluate the firm’s practice information and financial data. In an emergency transfer situation having good computer records for three to five years supported by tax returns readily available is important.

- Overhead relates to profitability. Controlling overhead expenses during the transition is a significant issue. Shifting overhead costs to a buyer is of great value to the selling practice because of the amount of money that can be saved. Overhead shifting or allocation should be done when the overhead relates to the fees being produced by the work being transferred which is generating or should generate fees for the buyer. *Overhead allocation is a frequently overlooked issue.* Depending on the file, when the buyer is benefiting from the seller’s overhead’s contribution to the fees, this portion of the overhead expense should be allocated to and paid by the Buyer.

- The value obtained and how a sale or transfer works is different for each lawyer and each practice. This uncertainty and the fact each transfer has its own considerations makes it difficult to value a practice. As a result the determination of the practice’s value is usually a combination of several different valuation methods.

- Time is a critical factor for both the lawyer and client. The more time that passes after a sudden transition event, the less the practice is worth. Also, the amount of immediate demands for service and case review process can create a cost/benefit problem for a purchasing lawyer or

firm. If the immediate demands of dealing with the practice are time consuming and burdensome for a busy lawyer the likelihood is that a potential buyer will walk away. It then comes down to what a willing buyer is willing to pay in a distress situation. The reason good organization and a good staff can be of great value is because the burden of the extra transition work can be greatly reduced and does not fall totally on the purchasing lawyer and his or her staff. In most cases the Seller's staff can complete much of the transition work in order to ease the burden on the purchasing lawyer or law firm as well as generate considerable fees. This is why overhead allocation is important and these costs should be part of the fees generated by the purchaser. Good staff adds value.

4. Timing. Complete the transfer as soon as possible. One must get the lawyer who is going to buy the practice or the office assets involved as soon as possible. Clients will see this and the prompt attention to their matters will help both the retention of clients and the collection of fees. Getting clients to quickly waive notice and approve the immediate transfer of the file is an important part of the transfer process because it reduces delays and protects the client. The transfer rules facilitate the prompt transfer of files with the client's consent.

5. Allocation of transition expenses and fees. Questions as to the amount that can be charged for fees and how to allocate the fees and expenses after death or disability are important issues. Office expenses mount as time passes. The monthly overhead can be expensive even for solo firms. There are problems recouping the office expense during the period after death or disability, so time is of the essence. There is an immediate need to either close the office as soon as possible or preferably get another lawyer to take over all or part of the office expense as part of the transition process.

In many transfers, especially emergency transfers created by sudden death or disability the parties fail to allocate the office expense as part of fee allocation or have the lawyer taking over the file assume the case related expenses and overhead. A reasonable allocation of the office expense that is part of the work on the file in the file transfer process is a factor to consider. In most cases the office staff and associates will contribute valuable work to the file as part of the transfer and this cost should be factored in as a benefit for the firm taking over the practice and paid for as part of the sale. Value billing can be factored in the division of fees on the file transfer. Remember, the graph of gratitude and appreciation of the value of all the work done falls dramatically as time passes so time is of the essence in collecting fees. Each case is unique and the case's value must be individually determined in most cases. A good example of this type of consideration is the difference in value of similar personal injury cases between one that has just been accepted and one that is ready for trial.

6. List of Items that can be identified, valued and transferred:

- a. Cash - sometimes seed money or transition funds will need to be advanced to ensure the success of the transfer.
- b. Furniture.
- c. Fixtures.
- d. Equipment - computers, photocopy machines, printers, fax machine, etc. including lease values.

e. Office Supplies.

f. Law Library - With *Westlaw*, *Lexis*, *IICLE Smart Books*, etc. most of our law libraries of books are now of little value. Subscriptions at discounted rates can usually be transferred and have value. Otherwise terminate the service and seek refunds.

g. Real Estate or Leasehold interest - Where the office is located may have location value and favorable leases also can improve the price.

h. Advertising in place - Finish contract and renewal. Websites have value. What's the identity value of prior advertising and listings that can be transferred or assumed?

i. Telephone numbers - especially if identifiable, well known for a long time or part of an advertising plan or directory.

j. Proprietary computer software - The case management systems, case systems, computer files of office and practice forms such as *Hot Docs*, which provide the ability to produce work quickly, are of great value particularly to newer lawyers. Adaptations of other software also have value and this need to be factored in. In many offices, the firms form and brief files are worth a lot considering the costs of commercial form books and the adaptations required to use them in the local practice area. These proprietary items can be leveraged for profit, especially such items as a good *Hot Docs* or an office forms library, because they are fill in blank forms systems that have value especially for first time users. Also, the value of having a file in electronic form has great value because this will ease the transition and reduce the purchasers' work because of the ready access to case file data and the reduced need to consult the paper file for current case information.

k. Fees and billing information.

l. Accounts receivable - factor costs of collection. This is a benefit to the estate if the collection of accounts receivable can be transferred because it saves collection costs as well as enhances recovery of fees for both the buyer and seller. Clients tend to pay the replacement lawyer first and outstanding bills can be included in the process.

m. Costs advanced and work in progress which is significantly completed or entirely completed but not yet billed as a receivable.

n. Trust accounts - need to be dealt with correctly and correctly accounted to the client involved.

o. Insurance policies may be transferred to the buyer or canceled for a refund.

7. **Good will of the practice** - is the going concern value of the practice and the prospect of future business. Typically, it includes the following:

a. Staff. The trained and experienced "in place" staff especially those who know the clients and can produce billable work are great value as part of the practice and for

retention of clients.

b. Cash flow generated by the annual fee billings and collections in relation to the nature and type of work involved. Normally, a three to five-year average will be used to even out the process and determine the average fee collection per year.

c. Use of tangible office assets such as computers and forms and legal systems in place and how the use of these assets can be leveraged for profit. Also, the replacement cost savings may be a factor because of the time and expense that will be saved by not having to recreate office systems and computer data.

d. Prospective work and current client files in progress. In many offices, the files in progress will be enough to generate substantial fees without any new business. The expected fees for completing the work in progress can justify a significant business generation credit or fee. Ongoing high fee generating clients add value. The amount of cash flow that can be generated by the firm's clients and current work in progress is another important aspect of this valuation factor. The amount of advance fee deposits or "evergreen" fee deposit agreements may also make the practice more attractive because they avoid collection problems.

e. Office organization and productivity. This is very subjective but some offices are more efficient and effective and are able to generate significant fees because of the productivity. What you are selling is really an intangible so the extent such office productivity can be transferred will add significant value. Staff is an important part of the productivity. The more the practice can be transferred on a "turnkey" basis the better the value especially those practices with a good cash flow and highly productive staff. In addition, the more productive the purchasing lawyer is the better the value because she or he will be able to generate more fees from the purchase.

f. Closed files for reference and repeat business - wills, real estate, corporate files, etc.

g. How much work and time is needed to complete the transition. Here again, a well-organized office with a good case management system and experienced staff in place should bring a premium by facilitating a prompt transfer. The more the transfer can be a turnkey operation and quickly generate cash flow for the buyer, the higher the value. Even when there is not a lot to sell in many offices there is work to be finished. As a result, in such cases a fee allocation agreement can be negotiated to finish the work so those fees are not lost.

h. The value of the name and the expectation of continued client business. This is the intangible value that is hard to define but to the extent it can be transferred it adds significant value to the practice.

i. Location and Phone Number. Clients get used to going to the longtime office location so staying in the same location with the same phone number may be an additional value.

8. Valuation Problems. Determining value depends on the practice's profitability. A buyer will want to look at all of the financial information. Profit and loss statements, balance sheets, work-in-progress, aged accounts receivable statements, tax returns and supporting

documents are the starting points in determining value. The basic ways to determine value are: the book value method, fair market value, and income or cash flow method. Sometimes with other types of professional practices, accountants use a ratio of one and a half times annual income. They do not have a rule of thumb for law practices because, at this point in Illinois, we still do not have an experience record to look at for guidance. Medical practices, for example, are valued between 0.4 to 1.0 x annual gross receipts but law offices are so unique that there is no one size fits all formula because in most practices the clients and work are so different. The more fees the practice is expected to generate for the buyer the greater the value.

- The value will also depend on how much repeat business is expected, the nature of the practice, the number of clients, number of files, the transferability of client relationships and the fees that can be expected to be earned from the work transferred, as well as the fees that will be received for completing the current work-in-progress. If there is a lot of repeat business expected, the estimated return will be higher so the value increases. The problem is that the practice of law is changing. Clients are having problems paying for legal services and are going *pro se* more often and competitors such as www.legalzoom.com are providing challenges. These trends also affect value.

- If you do not have a good estimate for repeat business, another approach is the excess earnings approach. This method computes the additional earnings a buyer can expect to generate from the practice above the normal return expected for a new lawyer starting practice or an established firm adding the business from the purchased practice. For example, can the purchaser expect to gross two to four times more fees from buying a practice rather than starting a practice from scratch? This is particularly important in smaller counties with few lawyers because purchasing a "book of business" from an existing practice can make the difference between a young lawyer making a reasonable living and starving.

- Excess earnings tries to get the investment return value of the practice as opposed to the fair market value and usually involves comparing five years income statements and figuring out how much extra income the practice will generate for the buyer to determine the worth of the practice. It is doubtful that such a method is used very often because of the personal nature of most small practices. It does however; give some indication as to how a buyer may view the practice because the purchaser must make a cost/benefit analysis as to the amount paid for the practice. *Note: Do not forget to include the value of direct lawyer benefits from such expenses as medical insurance coverage, pension plans, leased vehicles, car insurance, travel costs and other personal "business" costs that the office pays for the lawyer as part of the "actual" earnings. One important value of a solo practice is the ability to have the office pay for certain types of expenses and save taxes. The value of "benefits" to the lawyer need to be factored in when determining value because such benefits are real income items and many benefit items can be transferred to a buyer.*

- Goodwill is the differential advantage for the practice. It is the ability to do better than the competition by reason of skill, reputation, location, or special talent or other qualifications. This is really a problem because many solo practitioners have a personal following and it is hard to determine a goodwill value for this type of personal practice and how much of that will transfer. This problem is illustrated by the fact that the value of an established phone number in a small or medium size county can be worth a lot while a phone number in a larger city may have no special value at all.

- Tentative future cash flow approach - Cash is king so how much cash flow will this practice generate for the Buyer. How much work is there to complete and how much new work will the practice generate. Value is then based upon the estimated cash flow and what it is worth to the buyer to generate the extra cash flow. This is analogous to the business generation credit many larger firms use to allocate the value of the business generation for the firm.

There does not seem to be any consistency, but all considering all three methods provide some help in making a valuation decision. All three should be considered in arriving at the value of the practice. Value is essentially a compromise so the different approaches offer guidance in arriving at a value decision.

- Solo and small firm law practices in different states are offered for sale at various prices on the internet. Some of them have very low and some very high sale price numbers. It's hard to determine what is the pricing method used and how the very high numbers are determined. Reviewing what is available on the internet may offer some guidance in arriving at a value for an Illinois solo practice.

- Professional appraisals - These can be important but can be expensive. The problem with appraisals is they tend to rely on the practice numbers and may not include important intangible considerations. Qualified experts who actually look at all aspects of the practice in arriving at the value may be helpful but tend to be expensive. However, in many areas getting full value is not possible because the market is limited and the delay created by the time necessary to develop a full appraisal can significantly diminish value.

- Basically it all comes down to what a willing buyer will pay a willing seller to get the specific intact practice based upon the kind and amount of estimated benefit the buyer expects to obtain. One deceased solo practitioner had a practice with a staff of six generated a large gross per year. Two or three lawyers could have bought his practice together and made each six figure incomes per year because of the staff and systems in place and the limited number of lawyers in the area. Because at that time a sale was prohibited, no value was obtained and the clients were not served by the process. Under current rules such a well organized office would minimize the transition expenses and get maximum value on the fees for the files being transferred because it would be a virtual turnkey practice. What is necessary to maximize value and reduce transfer costs includes planning and organization. *In the end, however, finding a buyer who is both willing and can pay full value is the most difficult part of the sale. The better the organization of the office and the planning, the quicker a purchaser can start earning fees from the practice. Immediate generation of fees is the key to a good sale price for the practice.*

- The market for practice sales is continuing to be challenged because of the large education debt load that many new lawyers have. They cannot afford to buy a practice at a reasonable price. This is shifting the sales of law practices to existing firms who are better able to pay for the value of the practice. Depending on the circumstances creative financing arrangements may still work for new lawyers but many young lawyers can't handle the extra cash demand.

- Finally how is the purchase price being paid. Cash sales are becoming rare for many reasons especially economic. Paying a percentage down for the tangible assets with a fixed amount or percentage payment as fees are collected seems to be becoming the norm especially in smaller counties. Down payments especially for the tangible assets also seems to be the norm as

well. The payment plan can also affect the price because of the practical limits on what the purchaser can afford can limit the purchase price on the other side. Payments generated as the practice develops can increase the price especially in the second or later years as the practice becomes more established with the new lawyer.

ETHICAL ISSUES ON THE SALE

1. Protect Clients. The most obvious problem is that you are required to protect your clients' interest and confidences. There are multiple ways that the lawyer's estate can deal with protecting clients. Good planning will protect the clients and especially when it is done in a way that the clients understand and appreciate. Rule 1.17 provides that client consent must be given before client specific information can be disclosed to a purchasing attorney so it is important to get such consent as soon as possible. In fact, getting such consent in the engagement agreement is becoming more common. Clients appreciate the care you have given to protect their interests.

2. Conflicts. Any substitute, transition, or purchasing attorney needs to make sure that there are no conflicts with working with or purchasing the existing clients' files. If a conflict may exist then the parties must take whatever action that necessary to avoid the conflict. Case management systems can be checked to quickly identify such potential conflict problems and these files can then be segregated and dealt with separately.

3. Confidentiality. Client confidences are important and care needs to be taken to ensure that clients give timely permission to allow other lawyers to access to the client's files. These issues are very difficult but the rules deal in terms of minimum time periods for giving notices to clients before consent is presumed. In most cases waiting that long will be detrimental to the client. Active contact with the client can make it possible to immediately obtain the necessary permissions and waivers to permit another lawyer to review the confidential file and take any appropriate action. There is a requirement to mail a notice but no requirement for you to wait for the client to respond. Planning will make it possible to be proactive in contacting the clients and getting the necessary consents to permit the covering or transfer lawyer to work on the clients cases in a timely manner. Most clients will welcome and appreciate the proactive approach. As indicated above the client's consent for a covering or substitute lawyer can be part of the engagement agreement.

4. Client communications and confidentiality. What is the status of the contact between the lawyer and clients, both active and inactive? Confidentiality extends to the lawyer's staff who can assist with the transfer by dealing with the clients. In many cases a client's consent to access and/or transfer a file and waiver of notice can be obtained quickly, as well as consent to have the covering lawyer or transfer lawyer service the file. A good staff knows the clients and can be a valuable asset in arranging needed consents and a prompt transfer of the files or transfer of the practice. A good staff can also create enhanced goodwill with the clients if they are hired to continue even on an interim basis.

5. Preemptive Client consent in Fee Agreements. Consider incorporating clients' consents into your retainer agreements and retention letters to permit another attorney to work on their files and review confidential information in the event of your unavailability, illness, death or disability. It could be as simple as:

Unavailability of Attorney/Client's Consent to Temporary Substitute Attorney/Limited Confidentiality Waiver. In the event attorney is unavailable or becomes ill, disabled or dies

unexpectedly, client consents to another lawyer, chosen by attorney or attorney's legal representative, appearing for the attorney and to the extent necessary reviewing the file and handling the file until attorney becomes available or a successor attorney is either approved by or chosen by client. For this limited purpose, client waives confidentiality and consents to the other lawyer's appearance and access to clients' file for the purpose of taking appropriate action to protect clients' interests and reviewing and receiving the file as a possible successor attorney. To the extent possible, attorney will discuss with client the need for the other attorney and identify the other attorney, prior to having the substitute attorney temporarily act for or appear for the primary attorney and the client or reviewing the file.

6. Limited Liability. One of the major practice rule changes is the limited liability rule. Supreme Court Rule 722 gives Illinois lawyers the ability to have a limited liability practice and increases the ability to do some planning, especially for disability situations. This will enable solo practitioners to merge with another limited liability practice or partner with a limited liability practice so that if the lawyer wants to retire, he or she can do so without the potential partnership liability problems. Such entities can limit the overall personal liability on the transition to the malpractice insurance coverage. Partnership liability has been one of the disadvantages of such transfer arrangements in the past, because all partners share liability for creating a partnership debts and liabilities. Now these limited liability entities are becoming a preferred method of transfer between a lawyer seeking to retire and a buyer because they can be used to facilitate a transitional working relationship between the parties prior to the actual transfer.

- While it doesn't solve the problem of the true solo who suddenly becomes disabled or dies, because of the limitations on liability provisions of Supreme Court Rule 722, limited liability entities provide good planning alternatives, especially where there is enough time before retirement, death or total disability to make the necessary arrangements. Likewise, if the lawyer has a professional corporation or limited liability company he or she may perform a practice merger. There may be some adverse tax consequences, but these limited liability mergers offer transfer possibilities that should be considered especially with estates or sudden disability.

7. Fee Splitting and Overhead Payments. A problem in wrapping up a practice is the value of systems and having people in place to carry on the business. Previously, in some cases, the offices closed very rapidly, the files were distributed and no real thought was given to selling the systems or the ability for the office to continue to serve clients and generate income during the interim before the practice was transferred, distributed or closed. Client's' cases need to be served by the staff and a lawyer. A lawyer using the office staff and overhead during a transition needs to pay for that overhead. Otherwise, it becomes a cost to the disabled or deceased lawyer's estate. Overhead expense should be paid for by the lawyer who is actually benefitting from the use of the overhead. If a lawyer is using the transferring lawyers overhead to generate fees, these fees should be used to pay the associated overhead.

- In cases where there is ongoing overhead and services are actually being performed by the office staff for clients, transfer provisions need to provide that the new lawyer or transferee pay for or reimburse the estate for its share of the overhead and the cost of the work performed. Payment of or reimbursement for expenses and use of overhead is not fee splitting. It is part of the cost of generating the fee and is nothing different than the overhead that existed as part of producing the work before the death or disability. The lawyer obtaining the practice, or even just the file, should pay those expenses during the transition that are part of the overhead used in doing the work in order to protect clients or generate fees after the death or disability of the lawyer.

8. **Receiverships.** Under the Supreme Court Rules, there can be a lawyer appointed to act as a receiver. This is not a good way to deal with a practice, because a receivership is slow and cumbersome and the receiver is normally not paid. A receiver should be avoided if at all possible because a receivership is the last resort and is normally used only when a law practice is in a hopeless mess.

9. **Existing client-attorney of record issues.** A quick check should be made to see that a substitution of attorney is made very quickly in each litigated case in order to protect clients and avoid a default order. The same applies to corporation registered agent designation. The transfer rules presume consent if no objection is made or client action taken 90 days after notice to the client but a lot of solo practitioners' files require immediate contact with the client so that work can continue to be done immediately. This is important and most of the time the lawyer's staff who are familiar with the clients can deal with these issues. Again, this should be part of a new or transfer lawyers overhead that the estate should recover or have the new lawyer pay because beneficial work for the client is normally being done in addition to or as part of the transfer.

10. **Client files/Client's consent.** The client files follow the client. Determining immediately with who gets the file and what is done, requires contacting the client. In most solo practices, a lawyer deals with a limited number of active clients and if he or she has worked out some arrangement on what to do, a client can approve the plan very quickly and the law office can continue running in ways that are beneficial to the clients, the lawyer's estate and the new lawyer.

11. **Overhead Cost Problems.** In some of the transitions that I have seen, a major problem has occurred because the estate of the deceased lawyer and the potential transfer lawyer do not spend enough time at the beginning to resolve the ethical issues about fees, costs and expenses allocations. If they quickly work out those kinds of issues as to who will pay for each expense and how much additional reimbursement the deceased lawyer's estate will get for transition overhead expenses, both can profit from the transition. Pre-event planning helps but, post-event agreements defining each party's responsibilities and overhead obligations are critical. As part of the planning process consideration should be given to having enough life insurance and overhead disability insurance to cover in full at least three months of overhead for the operation of the office during the transition. Cash flow problems are normal and if cash is a problem the insurance proceeds gives the buyer a better negotiation position because such cash can reduce the distress situation created by deficit operations.

12. **Trust Accounts, unearned fees, etc.** Problems can occur with unearned fees, trust funds, and other held assets that belong to clients. Look for whatever harm is foreseeable in each file and promptly take care of dealing with that file to avoid problems and protect the client. Many clients will be cooperative in making arrangements with regard to unearned fees and trust account balances. A problem-solving approach works and enhances value for the client and the lawyer because the clients do not have to worry about what happened to their funds.

13. **Staff Knowledge.** One of the biggest assets of a lawyer who has an office staff is the staff's knowledge about the client files and matters. Staff members are subject to the same ethical rules that governed the lawyer with respect to confidential information. The staff can or should be able to produce quality legal work, review files for triage actions, return confidential information to clients, screen for conflicts and get necessary consents.

14. **Mandatory File Review.** All active files must be looked at and reviewed as soon as possible to avoid the inadvertent missing of deadlines, statute of limitations or other concerns that might be considered. Such review will protect against the inadvertent failure to act, and help

to avoid the unintended breach of client confidences. Depending on the case, a review could cause a breach of confidences but the damages to clients regarding possible breaches of confidence may be less than if the file is not promptly reviewed and a problem avoided. It is a judgment call. Case management systems are the best protection against overlooking items and deadlines as well as confidences being breached by disclosure to an opposing party. Client lists in case management systems can be used to check for conflicts with a potential a successor lawyer to avoid improper disclosure. Good case management lists and experienced staff who are familiar with the clients and cases can shorten the review and triage process. Triage to determine the urgency of cases and staging the review process is necessary to give priority to the most pressing and profitable matters. Depending on the type of practice, the case review process can be very time consuming and burdensome. Better organization and good case management systems will ease the process.

15. Foreseeable Prejudice to Client Must be Avoided. It is important to make sure that no foreseeable prejudice to the client is allowed to occur.

16. Buyer Competency. A significant problem that the lawyer or estate faces is the competency of the buyer. While the seller or seller's estate is not a guarantor, there is an ethical requirement that the seller or seller's estate make a reasonable investigation of the purchaser's competence and honesty.

17. Client Expectations/Misrepresentation Claims. Care must be taken to ensure that there is no misrepresentation or unreasonable client expectations issues. A lot of solo lawyers carry too much information in their head and this can be a problem with clients and buyers because of a client's claims that the lawyer "said he or she would do something" or guaranteed a certain result. This can be troublesome so the better the files can be documented; the less chance there is for post event problems when the lawyer is not available to respond. In taking over a file it is important that either the transferring lawyer or the purchaser or preferably both quickly determine what the client wants and whether or not client expectation issues exist. Simply asking the necessary information about the client's expectations and what the client understood the lawyer was doing can quickly indicate whether or not that such issues need to be dealt with. Remember clients who want or expect certain results have a tendency to ascribe miraculous powers to the disabled or dead lawyer and such expectations tend to increase the more time passes if not confronted promptly.

18. Malpractice Tail Insurance. Malpractice insurance is one problem to be considered. The best thing to do is to cover all of the buying and selling lawyers with "tail insurance" which, while expensive, can allow the estate to be closed or the retired lawyer to have peace of mind.

19. Covenants not to Compete. In Illinois covenants not to compete are not allowed. Rule 1.17 covers lawyers "who cease to engage in the private practice of law in all or part of Illinois" due to seven enumerated events. There is no time limit so the contract involving retirement of a lawyer needs to deal with these issues in retirement situations.

20. Original Documents. Care must be taken to protect clients' original documents such as wills, deeds, contracts, etc. The better practice is to not keep a client's wills and other original documents. Originals should be copied and the originals should then be returned to the client.

21. Payment. How is the sale to be paid for? This will largely depend on the buyer's resources and ability to pay. Normally, the more cash that can be received in the beginning, the better the transition. A large debt service obligation can kill a lot of installment transactions and there is always the potential problem of timely payments. The payment structure must comply with the Illinois Code of Professional Responsibility.

PLANNING ITEMS

One of the most important things to do is to have basic estate and practice information readily available to your family and executor if you die or become disabled. These include the following:

- A. Funeral instructions
- B. People and organizations to contact. This is important because most lawyers have many contacts in case management systems, computerized address books or contacts software so it is important to prioritize whom to call first.
 - 1) Personal
 - 2) Advisors
 - 3) Business
 - 4) Professional organizations
 - 5) Clients
 - 6) Others
- C. List of Advisors
- D. Location of wills and important documents.
- E. Life insurance, disability insurance, other policies.
- F. Directions and a checklist for taking immediate action to protect clients and the practice.
- G. List of potential people that would be involved in selling and buying the practice and statement of what arrangements have been agreed to or should be considered.
- H. Office and personal financial information and at least five years of tax returns should be immediately available
- I. A time line list of items to be taken care of and what and when each item should be done.
- J. File destruction plan. In most offices, a number closed files can be destroyed rather than stored. In our offices, we make sure all original documents are returned prior to closing in order to minimize the potential destruction of original documents.

22. Contingency Operations Notebook. It is a good idea to have a contingent

operation or emergency notebook which includes information about the lawyer's various insurance policies and investments, a list of clients and written instructions on what to do in certain emergency situations along with checklists and sample letters, notices and forms and location of passwords. In addition, notes, observations and suggestions can be included. Even handwritten instructions or checklists will work. Most solo practitioners are not that organized, but at least having all these items together in a notebook, or a designated file drawer or safe can be a major help. A plan needs to be as effective and complete as appropriate. You don't get extra credit for making it look pretty but the better and more complete the information the more workable the plan.

23. Simple works. Most solo practitioners won't do nor do they have the time or inclination to do extensive disaster planning because their current workload and the work already piled up doesn't allow time to do so. Most lawyers don't take the time to either plan or organize their personal matters. In my office, I have my tax returns and the files for all my investments in one file drawer in the safe. The insurance and bank accounts are in another file drawer in the safe. All of the financial information, billing time slips and case management information are on my computers with weekly backup in the office, at home and our full computer system is backed up with Carbonite on the cloud. My accountant has a monthly backup of the financial information. I have a good staff. All of the client information, appointment schedules, To Do Lists and deadlines are entered in our *Amicus* Case Management System. The information is all there and readily accessible so that it can be reviewed and dealt with in a timely manner. It may not be perfect but the clients are protected. Anyone using a post disaster checklist can promptly locate all of the information they need to protect my clients and take effective action on behalf of my clients. What we do is simple but the information and documents are there and can be accessed so that timely action can be taken. I hope to have time to do better. But what I have is available for timely use and will work.

MAJOR ISSUES TO CONSIDER

1. What work and filings are due with all of the cases
2. Immediately review all new files opened in the thirty days before the death or disability because of the enhanced possibility that all items have not been properly docketed and the file opening procedures may not have been completed.
3. Client and file index
4. Cash flow, expenses and staff requirements
5. Your trust accounts
6. What to do with pending files
7. Billing for unbilled work and the collection of accounts receivable
8. What to do with the old files. Current destruction of closed unnecessary files will save time and money for storage costs. A current destruction plan can save a lot of trouble and expense because it informs the staff and buyer as to what files can be immediately destroyed and guidance as to how long to store the remaining files.

9. Tail insurance

10. Prior Partnerships - The problem is that in two partner firms upon the death or disability of one partner, the surviving lawyer immediately becomes a solo practitioner. If there is no new partnership, the surviving partner will then have to sell her or his own practice under Rule 1.17 if she or he wants to retire, becomes disabled or dies. In these situations check for any partnership agreement for the prior firm. If there is no written agreement then the partnership was legally dissolved and partnership statutes and all of the above considerations apply in winding up the partnership. If there was a partnership agreement then that agreement will govern the partnership matters and affect how the surviving practice is sold under Rule 1.17.

RESOURCES

While there are a number of published articles, the two book resources I know that are available are *Selling Your Law Practice: The Profitable Exit Strategy. Including the Fundamentals of Closing a Law Practice* by Edward Poll and *The Lawyer's Guide to Succession Planning: A Project Management Approach for Successful Law Firm Transitions and Exits* by John W. Olmstead.

Selling Your Law Practice: The Profitable Exit Strategy. Including the Fundamentals of Closing a Law Practice by Edward Poll is published by LawBiz Management Company (a division of Edward Poll & Associates, Inc.), 421 Howland Canal, Venice, California 90291. \$489.00. www.lawbiz.com It is comprehensive and contains sample agreements, checklists, financial worksheets and other necessary forms that cover all aspects of a practice sale. It is a quick start comprehensive plan with a CD of all forms. Using Ed Poll's plan should save a large amount of time and provide additional value on the sale well beyond the price of the book itself. Some sale offers may include an hour consultation with the author.

The Lawyer's Guide to Succession Planning: A Project Management Approach for Successful Law Firm Transitions and Exits by John W. Olmstead is published by ABA Book Publishing, 321 N. Clark Street, Chicago, Illinois 60654. Published on August 1, 2016. \$125.95. www.shop.americanbar.org. John is a frequent contributor to ISBA publications.

CONCLUSION

There is no right answer for every situation. Each practice is different and each one needs to be dealt with based upon what is required for that practice. After more than ten years, we still don't have a lot of experience selling solo practices in Illinois and the market is changing because of the economy and new lawyer education debt. It is clear that case management systems will help in the transition and maximize value. Good planning and practice organization protects clients and saves money, time and effort. Hopefully, because of the Illinois Supreme Court's 2010 change of the rules to make the sale of a solo practice easier, solo practitioners can get the value for their practices that they have spent a lifetime building as well as provide for an orderly transition of their offices so that their clients are protected and will continue to be well served. The rule provides the opportunity for a successful transfer but good planning is important to get the best return. It does not have to be fancy but it needs to be informative. To paraphrase General George S. Patton, a good plan well executed now, is much better than a perfect plan that is never quite finished.

About the Author:

John T. Phipps is engaged in the general practice of law in Champaign, IL as John T. Phipps Law Offices, P.C. His primary emphasis is in the areas of family law, general civil litigation, real estate, probate and business law. He is a past chair of the ISBA General Practice, Solo and Small Firm Section Council, Co-Editor of the Section's newsletter (17 years), and member of the ISBA Assembly. He was also the Chair of the ISBA Practice Transfer Committee and the Electronic Research Committee which lead to the adoption of FastCase as a member benefit for the ISBA. He is a Laureate of the ISBA Academy of Illinois Lawyers. He also has served as Chair the ISBA Senior Lawyers Section Council and is co-editor of the Section's newsletter and is on the ISBA Amicus Committee.

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