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Can You (and Should You) Buy Or Sell a Law Firm in N.J.?

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For a long time the practice of law was, perhaps, the only profession whose practitioners were prohibited from realizing financial value from a lifetime of hard work. Attorneys who attempted to sell their practices were chided, or, worse, disciplined, and reminded that their clients were not property to be bought and sold. Solo and small-firm attorneys were only allowed to sell their tangible assets when they decided to exit the profession.

In 1990, however, the general negative attitude toward the selling of legal practices changed with the adoption of Model Rule 1.17 by the American Bar Association (ABA), which permitted the sale of law practices and addressed the disparity between succession options available to solo/small and larger firm practitioners.

Why is this relevant today? Because over the next 10 years, the ABA predicts that approximately 400,000 attorneys nationwide will be at retirement age. According to the ABA, there were 1,245,205 attorneys nationwide in 2013, with New Jersey accounting for approximately 41,000.

With one-third of the nation's attorneys projected to retire in the next 10 years, if we assume that New Jersey will track at the national average, the state could expect to have approximately 13,600 attorneys reaching their retirement age over the next 10 years.

Now, what about all those clients? The revenue streams will have to go somewhere.

This might be the perfect time to take advantage of the ability to buy or sell a law practice. Doing so would provide retiring attorneys with additional liquid assets for their retirement while providing new attorneys with an established client base and operating assets.

However, it would be remiss to categorize the winding down of a practice, or preparing to do so, as a consideration only of would-be retirees. Likewise, prospective buyers are not limited to new lawyers, but include a vast number of "refugees" from larger firms, including senior associates and junior partners with upward mobility.

There is a saying, "Lawyers don't retire, they just die at their desks." Although meant to be amusing, the reality of those words is all too worrisome and realistic. Unfortunate

events such as untimely death, illness and disability do happen, and will only increase as the population ages. This is in addition to the current risks of disbarment or removal, or the more favorable "risks" of a potential judgeship, or leaving the practice by choice.

When an attorney is suddenly unable to practice, his duties to his clients do not abruptly end; rather, the attorney, or his estate in certain circumstances, continues to owe clients moral, ethical and legal duties.

Perhaps the attorney is not planning to retire in the next 10 years. However, in addition to developing a crisis plan, the considerations of maximizing the law practice's assets and value, evaluating its total worth, and finding purchasers are issues every attorney should begin to think about and plan for. As Winston Churchill once said, "Let our advance worrying become advance thinking."

Purchasing a law practice can be just as advantageous to newer lawyer purchasers, as to retiring sellers. When purchasing a practice, a newer lawyer is able to hang out his or her shingle with an established client base, a built-in mentor, a trained staff and equipment. Granted, fewer and fewer new lawyers are willing to enter a solo practice, and even fewer may have the financial means to buy a firm outright. Many beginning lawyers might immediately discredit the idea of purchasing a legal practice. But golden opportunities exist for entrepreneurial beginning attorneys, big firm refugees, or other small or solo practitioners wanting to grow their practice areas and client base.

When formulating a succession strategy, attorneys must take into account ethical, moral and legal obligations to their clients. Most importantly, before beginning negotiations with potential buyers, attorneys must be aware of what they are actually permitted to sell as part of their practice

One question many attorneys have during succession planning is what confidential information can and should be provided to a potential purchaser of a practice in light of attorney/client privilege, confidences and secrets. Although the N.J. Rule of Professional Conduct 1.17 – Sale of Law Practice is silent on the matter, the Model RPC 1.17(b) addresses this, providing that notwithstanding attorney/client privilege, the seller may disclose to the prospective buyer information regarding individual clients. There's a bit more guidance from neighboring New York state, where the RPC addresses the disclosure of the identity of the client, financial terms of the attorney-client relationship and more.

Once an attorney has committed to selling his practice and has carefully considered the relevant ethical and professional issues surrounding retirement and cessation from practice, he must take steps to implement his plan and begin the selling process.

Too often, attorneys fail to consider their practice as an asset that could provide income similar to a defined income plan. This sort of thinking can lead to a huge loss of potential retirement-age income. Including the practice as an asset requires practitioners to

undertake succession planning wherein they consider all aspects of the practice. Succession planning should be strategic and well thought-out because a great deal of planning is needed for a successful (and ethical) sale.

Model Rule 1.1 requires sellers to exercise competency in identifying prospective buyers for the practice. Finding a potential buyer requires maximum due diligence, as the seller will be turning over the reins on client matters. The attorney is also giving away the goodwill of his or her name and firm to an unknown practitioner who may very well be a recent law-school graduate. The assistance of an advisor with law firm divestiture experience to evaluate and deliver to the seller potential purchasers can prove invaluable in this process.

Buyers of a law practice must obligate themselves to undertake the representation of all of the clients in a book of business competently and irrespective of whether said clients generate high fees. Here, too, the use of a third-party advisor with law practice transactional experience can prove helpful in identifying, evaluating and conducting due diligence, negotiating and structuring the deal and payment terms. Most importantly, an advisor can help develop and execute a client transition plan, which is critical if the purchase price is dependent upon client retention levels.

It is easy to place a value on real and personal property owned by a practice. However, one of the greatest challenges and also, perhaps, the most critical to selling a firm is the valuation of its goodwill, including name and referral network. This is in addition to its book of business, which is often made up of one-time clients or those whose continued business is dependent on long-standing mutual trust and goodwill, making it difficult to evaluate current and future cash flow. Unfortunately, there is no universally accepted method of valuing a legal practice. Thus, once the seller and purchaser have been identified, the services of valuation experts may be a prudent course of action.

Other necessary requirements in RPC 1.17 to sell a law firm in New Jersey include the seller ceasing to practice in New Jersey, that the entire practice is sold (no cherry picking), written 60-day notice to clients to consent or retrieve their files, and an announcement of the deal published for at least three months in the *New Jersey Law Journal* and *New Jersey Lawyer*. Furthermore, a purchasing attorney is not allowed to increase fees charged clients by reason of the sale.

There has been no better time to buy or sell a law practice in New Jersey, and doing so can be manageable for both parties if strategically planned and appropriately structured. Sellers and buyers must remember to keep the client at the forefront of the transaction, protecting client confidences and confidentiality and conducting due diligence ethically to avoid any conflict of interest.

Nat Wasserstein is the principal of Lindenwood Associates, a strategic development and restructuring firm that helps owners of small to medium sized businesses (including law firms) navigate through times of change, redirection and financial distress.