

Creating an Attractive, Affordable and Sustainable Ownership Transition Plan

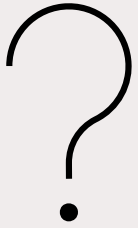
SPEAKERS:

MICHAEL STROGOFF, FAIA

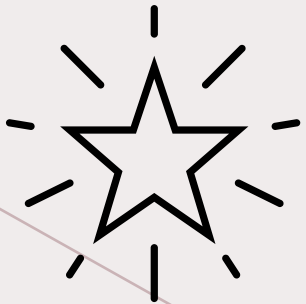
JENNIFER SUZUKI, ATTORNEY



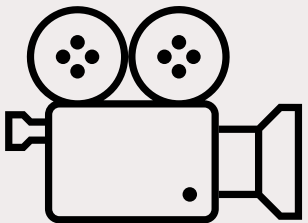
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LEARNING OBJECTIVES



Understand how to develop an ownership transition framework that is attractive, affordable and sustainable



Understand the major challenges that design professional firms face when crafting a transition framework



Learn how an ownership transition framework can balance the professional, financial and legal concerns of buyers and sellers



Understand the pitfalls to avoid when transitioning ownership

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PRESENTERS

MICHAEL STROGOFF, FAIA
OWNER
STROGOFF CONSULTING, INC.

JENNIFER SUZUKI, ATTORNEY
PARTNER
LONG & LEVIT LLP



CREATING AN ATTRACTIVE, AFFORDABLE AND SUSTAINABLE OWNERSHIP TRANSITION PLAN

Presented by:

Jennifer Suzuki, Esq.
Long & Levit, LLP

Michael Strogoff, FAIA
Strogoff Consulting, Inc.

Generously Hosted by:



Agenda

- Overview / Types of Transactions
- Why Consider Ownership?
- Commonly Held Myths
- Criteria for Success
- Potential Concerns to Prospective Owners
- Valuations
- Affordability Levers
- Where to Start
- Legal Documentation
- Questions & Discussion



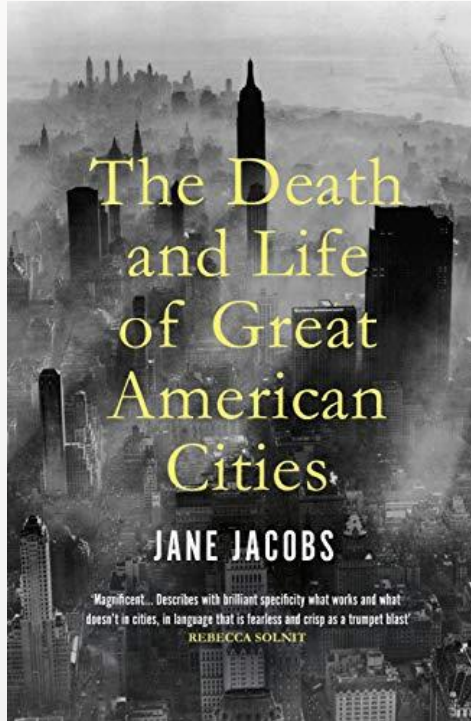
Retirement? I'm going to die at my desk.

Types of Transitions

- Planned Transitions
 - Ownership expansion
 - Gradual redemptions
 - Retirement
- Unplanned Transitions
 - Death
 - Disability
 - Life changes
 - Terminations

Challenges with Internal Transitions

- Number of owners approaching retirement
- Some owners not ready to relinquish control
- Willingness to share information
- Solicitation by competitors and recruiters
- Prospective owners value work|life balance
- Fear of the unknown
- Limited financial resources to invest in a firm
- Requires healthy comfort level with risk



*Firms are living organisms
that continue to evolve.*

Why Transition Planning is Important

- Perpetuates a firm's culture
- Attracts, recognizes and retains key people
- Supports marketing and growth opportunities
- Enables leaders to redefine roles
- Brings additional perspectives to the table
- Facilitates orderly succession planning
- Enables owners to realize value
- Professional liability; insurance
- Life (and death) happens



Let me get this straight. You want me to invest in a design firm?

Why Consider Ownership?

- Opportunity to shape the firm's future
- Professional growth and recognition
- Entrepreneurial path
- More effective marketing platform
- Greater involvement in decision-making
- Access to key financial and operational information
- Potential for increased income
- Long-term investment opportunity

Ownership Transition ~~Myths~~

- Outside acquisitions yield higher returns
- Valuations are only needed when an event happens
- “Fair Market Value” is an objective measure
- Staff will remain forever loyal
- We have plenty of time



The Basic Ingredients

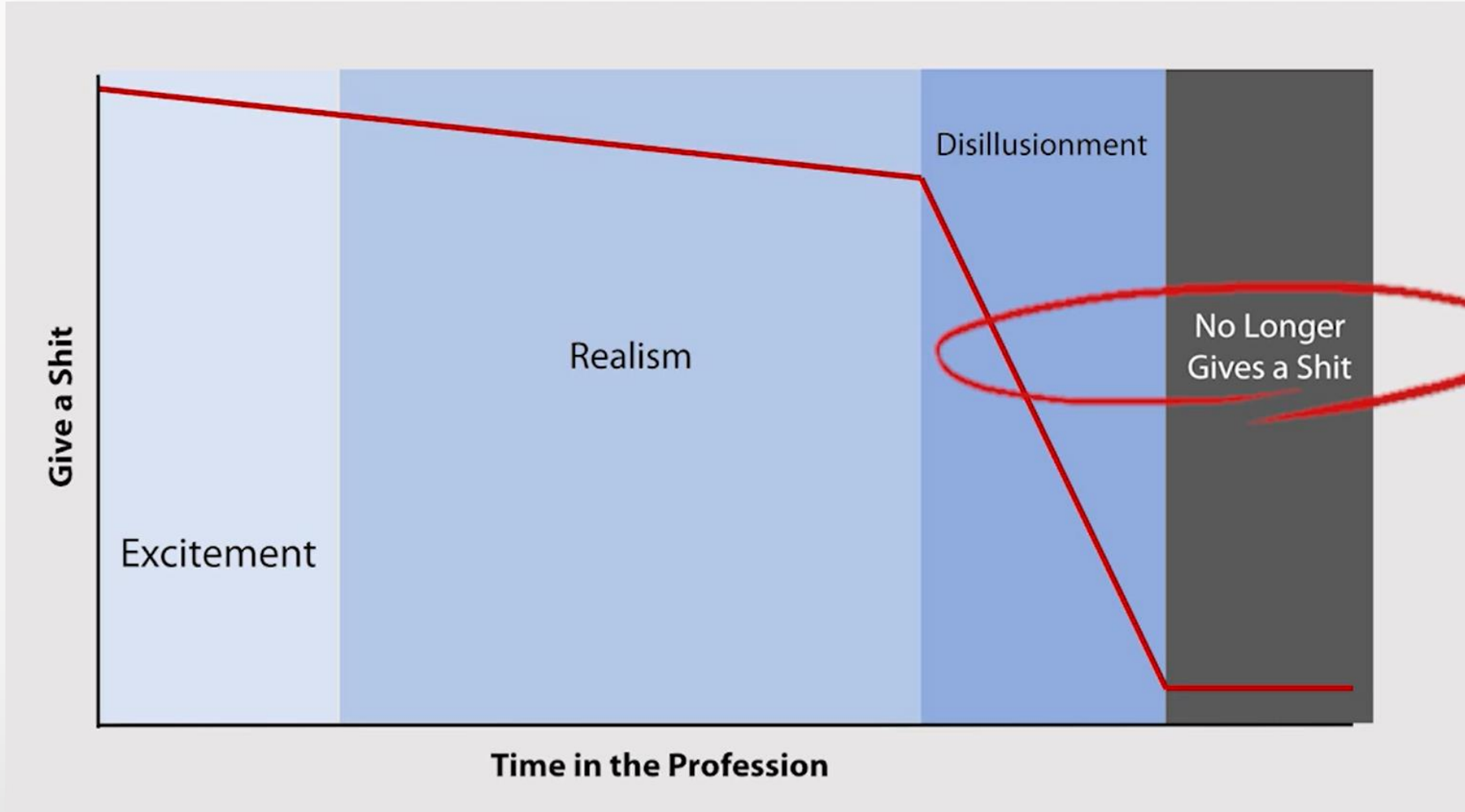
- ✓ Consistent profitability
- ✓ Qualified and interested leaders
- ✓ Time



Will 5 out of 7 work?

Among the Criteria for Ownership

- **Shared values** and belief in the **firm's vision**
- **Trust, integrity, discretion** and sound judgment
- Ability to think **strategically** about the future
- A **mindset** that what is best for the firm takes precedence over what is best for any single individual
- Strong **interpersonal skills** and commitment to engage in **constructive communication**
- Tolerance for and **willingness to assume appropriate risks**



Criteria for Success

- Willing **buyers** and willing **sellers**
- Demonstrate that ownership yields an **upside** and **benefits** beyond that enjoyed by employees
- Sharing in the **profits**
- Identify **ownership criteria** and **expectations**
- **Relinquish** control
- Must be **attractive** and **affordable**
- Develop a **roadmap**

Ownership Roadmap

Effective Date	Current Owner 1		Current Owner 2		Current Owner 3		Future Owner 1		Future Owner 2		Future Owner 3		Future Owner 4		Shares Outstanding
	%	Shares	%	Shares	%	Shares	%	Shares	%	Shares	%	Shares	%	Shares	
As of December 31, 2023	60.0%	600	20.0%	200	20.0%	200	0.0%	-	0.0%	-	0.0%	-	0.0%	-	1,000
Year 1 - January 1, 2024	47.6%	500	19.0%	200	23.8%	250	4.8%	50	4.8%	50	0.0%	-	0.0%	-	1,050
Year 2 - January 1, 2025	40.0%	400	20.0%	200	30.0%	300	5.0%	50	5.0%	50	0.0%	-	0.0%	-	1,000
Year 3 - January 1, 2026	30.0%	300	20.0%	200	30.0%	300	10.0%	100	10.0%	100	0.0%	-	0.0%	-	1,000
Year 4 - January 1, 2027	20.0%	200	20.0%	200	35.0%	350	10.0%	100	10.0%	100	5.0%	50	0.0%	-	1,000
Year 5 - January 1, 2028	5.0%	50	20.0%	200	40.0%	400	15.0%	150	15.0%	150	5.0%	50	0.0%	-	1,000
Year 6 - January 1, 2029	0.0%	-	20.0%	200	40.0%	400	15.0%	150	15.0%	150	10.0%	100	0.0%	-	1,000
Year 7 - January 1, 2030	0.0%	-	10.0%	100	40.0%	400	15.0%	150	15.0%	150	10.0%	100	10.0%	100	1,000
Year 8 - January 1, 2031	0.0%	-	10.0%	100	40.0%	400	15.0%	150	15.0%	150	10.0%	100	10.0%	100	1,000
Year 9 - January 1, 2032	0.0%	-	0.0%	-	50.0%	500	15.0%	150	15.0%	150	10.0%	100	10.0%	100	1,000
Year 10 - January 1, 2033	0.0%	-	0.0%	-	50.0%	500	15.0%	150	15.0%	150	10.0%	100	10.0%	100	1,000



Potential Concerns of Prospective Owners

- Liability arising from **status as shareholder** or **officer** and **director**
- **New liabilities**, such as:
 - Assuming responsible control
 - Signing and stamping
 - Personal guarantees
- **Governance / minority lack of control**



But I invested the best years of my life!

Valuations

- Must be **affordable**
- Consists of **tangible** and **intangible value**
- Reflects likelihood of **future profitability**
- **Clearly prescribed**
- Represents a **default value**
- **Risk Factors:**
 - Reliance on Key Personnel Discount
 - Key Client Discount
 - Lack of Marketability Discount
 - Minority Control Discounts
 - Other Risk Factors



Can I pay for that with bitcoin?

Affordability Levers

- Net worth retained or allocated to current owners
- Offer in increments
- Valuation amount
- Downpayment
- Discount or subsidy on initial purchase
- Salary increases
- Financing and payment terms
- Relief valves

Projected Annual Cash Flow for Incoming Owner A (Accrual-Based)

Fiscal Year	Stock Purchase Price (Including any Discount)	A. Down Payments/ Cash Purchases	B. Initial Base Salary Increase (after taxes)	C. Annual Primary Loan Payments	D. Annual Ownership Distributions (after taxes)	E. Ownership Distributions Applied as Additional Loan Payments	F. Annual Net Cash Flow (Not including salary and discretionary bonuses, if any)	G. Cumulative Net Cash Flow	Ownership Value and %	Less: Notes Payable	Net Ownership Value
2024	50,966	(10,000)	6,900	(5,200)	16,006	(9,279)	(1,573)	(1,573)	63,700 5%	(28,068)	35,632
2025	-	-	6,900	(5,200)	16,848	(9,767)	8,781	7,209	72,800 5%	(14,101)	58,699
2026	81,855	-	6,900	(12,000)	35,449	(20,550)	9,799	17,007	163,700 10%	(67,131)	96,569
2027	90,957	-	6,900	(19,600)	55,905	(32,409)	10,796	27,804	272,900 16%	(112,243)	160,657
2028	150,117	-	6,900	(32,400)	88,121	(51,085)	11,536	39,340	450,400 23%	(189,151)	261,249
2029	87,375	-	6,900	(34,400)	135,759	(78,701)	29,558	68,898	578,900 28%	(173,843)	405,057
2030	-	-	6,900	(34,400)	141,189	(81,849)	31,840	100,739	584,300 28%	(63,397)	520,903
2031	-	-	6,900	(25,800)	146,837	(38,715)	89,222	189,961	589,900 28%	-	589,900
2032	-	-	6,900	-	152,710	-	159,610	349,571	595,600 28%	-	595,600
2033	-	-	6,900	-	157,292	-	164,192	513,763	607,512 28%	-	607,512
	461,270	(10,000)	69,000	(169,000)	946,117	(322,354)	513,763				

Where to Start

- Pathways to ownership
 - Leadership ladders
 - Training and mentoring
 - Increasing levels of responsibility
- Roadmap
- Valuation
- Initial discussions with prospective owners
- Advisory team
- Term Sheet

Legal Documentation

- Stock (or Unit) Purchase Agreement
- Redemption Agreement (if applicable)
- Promissory Note and Pledge Agreement, as needed
- Buy-Sell Agreement (sometimes part of Shareholder or Operating Agreement)
- Updates to Articles of Incorporation and Bylaws, as needed

Questions & Discussion



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Michael Strogoff, FAIA
Strogoff Consulting, Inc.
StrogoffConsulting.com
Michael@StrogoffConsulting.com
415.383.7011



Jennifer Suzuki, Esq.
Long & Levit, LLP
longlevit.com
JSuzuki@longlevit.com
415.438-4442