

## Architecture Firm Ownership Transitions

By Ed Hord, FAIA, 2014 Chair, AIA Trust &  
Ann Casso, Hon. AIA, Executive Director, AIA Trust

The slowly improving economy has led to an increasing pace of mergers and acquisitions among architecture firms. In addition, 'baby boomer' firm owners now considering retirement also fuel various ownership transitions. Privately owned architecture firms in today's consolidating, competitive environment face numerous hurdles when considering traditional internal ownership transitions and leadership succession programs. To help AIA members through these types of transitions, the AIA Trust commissioned George Christodoulo, head of a national law practice serving design professionals as both buyers and sellers in mergers and acquisitions, to author a white paper on: "Selling, Merging or Closing Your Practice? An Overview of the Many Processes and Factors to Consider When Choosing a Course of Action" to help members determine their own best course of action.

The performance of architecture firms since the 2008 recession has inhibited the capability of younger owners to finance their purchase of shares, delaying typical paths for leadership succession. The market turnaround in recent years may increase the likelihood of successful internal transitions, since an infusion of profits is necessary to finance the purchase of shares from older leaders, while allowing adequate capital to operate and grow. It remains vital that the next generation of architects have the inclination and entrepreneurial business instincts to lead a firm.

Recently an architectural firm based in Baltimore, Maryland began the search for another firm with which to merge or to purchase in order to expand their geographic reach and insulate the firm from regional economic swings. The Baltimore firm was looking for a firm with a similar culture and values as well as one that was structured for future success. At first, a great number of firms looked interesting as they were both successful and well-run. The firm leaders who were in their 60's were looking to retire with a good financial payout to fund their retirement. With further investigation, it was apparent that many of these firms had not developed the next generation of rainmakers and leaders, so that when the current leaders left, there would be no one remaining who could lead the firm or retain current clients and bring in new ones.

There is a lesson here: running a firm that is successful and profitable is not enough. If one wants to create real value in a firm that could in later years fund a founder's retirement, then great attention needs to be paid to the development and retention of the next generation of leaders. This is essential for either an internal transfer of a firm or for a firm merger or sale. Employees should be recruited and retained who have the potential to take the firm into the next generation. Employee attributes to look for:

- Creative
- Ambitious
- Able to take over the management of key clients and land new ones
- Financially savvy
- Honorable.

Promising future leaders will need to be mentored and groomed for leadership. As the current firm principal, you will need to spend time and money on helping them to develop the skills needed for success. You will need to let them manage existing clients and support them in finding new clients. There are hazards here. Once you spend years mentoring and training ambitious, bright young people and handing over the management of the firm's clients, how do you keep them from taking those clients and starting their own firm? It is very important to make sure that you compensate them well, give them early ownership, and have them share in the financial success of the firm. They also need to understand the value that comes from the resume and client base of their current firm.

If an internal transition isn't feasible, there may be good reasons for an external purchase of an architecture firm, including a higher valuation of the firm by outside purchasers and clients who want to minimize the number of joint ventures, firms, and sub-consultants on projects. There are numerous courses of action that may be considered with an external purchase since it is a complex process. A description of the alternatives, along with charts clarifying the parties involved, are included in the AIA Trust white paper.

Whether internally changing the ownership of a firm, dealing with an external buyer, or merging architecture firms, the Trust white paper addresses the practice and business issues that will ultimately determine success or failure. These factors include whether the firms have compatible cultures, how the firm will be named, professional liability insurance, personal

property of seller shareholders, tax ramifications, the retention and future employment of the seller's employees, and the communications plan and branding strategy as they relate to the public and to the firm's clients.

Also outlined are the steps involved and factors to consider should the decision be made to close the firm. A firm closure isn't as simple as it may sound. Beyond the obvious downside of ending a business and terminating employee jobs, disadvantages can include lower net proceeds to the owners, and unresolved outstanding debt and current property leases.

The final decision of whether to sell, merge, or close a firm will not only affect the financial return to the owners, but the employment of staff, and the firm's culture. There is no right answer to how each firm's leadership should best evolve over time; only options to be weighed with the circumstances and priorities of the firm's owners. Change is inevitable, and potential consequences underscore the importance of being prepared for it. Understanding the various approaches and possible outcomes can help guide firm principals to chart the best path to their future.

Read the AIA Trust White Paper: [Selling, Merging, or Closing Your Practice? An Overview of the Many Processes and Factors to Consider When Choosing a Course of Action](#)

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*Ed Hord, FAIA, is a founder and senior principal of Hord Coplan Macht (HCM), a 200-person architecture and landscape architecture firm with offices in Baltimore, Denver and Alexandria, VA. Ann Casso, Honorary AIA, serves as the Executive Director of the AIA Trust.*

*The AIA Trust evaluates, selects, and monitors member benefit programs that meet the Institute's high standards of quality and value and serves as a risk management resource for AIA members. Article first published July 2015, [\*Practice Management Digest\*](#).*