CREATING VALUE FOR YOUR FIRM THROUGH STRATEGIC ALLIANCES

Shimmerman Penn LLP
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Presentation by:

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Our AED Industry Group

Dedicated team serving the industry for 20+ years.
Educational programs, webinars and events.
Conference presentations at OAA, IIDEX, SDA Canada.
Assisted the OAA in drafting proposed changes to the Architects Act in 2010.

Key areas of focus include:
• Structuring new business partnerships
• Understanding common industry valuation methodologies
• Creating succession plans for organic growth
• Financial benchmarking using key industry metrics
• Designing creative compensation strategies
Creating Value for Your Firm
Through Strategic Alliances

• Strategic Planning for Growth
• Building Value
• Short Term vs. Long Term Strategies
• Managing Risk
• Corporate Ownership Structures
Creating Value Through Strategic Alliances
Strategic Planning for Growth

- Status Quo (maintenance)
- Partnering & Joint Ventures
- Organic growth (internal succession)
- Multi-Disciplinary firm
- Mergers and Acquisitions
Creating Value Through Strategic Alliances
Strategic Planning for Growth

Marketplace Is Changing

• Develop new services and specialties in-house
• Leverage a broader based firm
• Collaboration among firms to win projects
• Business opportunities in new markets
• Access to talent, technologies, services
• Access to outside investors
Creating Value Through Strategic Alliances
Strategic Planning for Growth

Financial Assessment

- Budgeting the cost of achieving objectives
  - Obtaining resources
  - Marketing initiatives
- Analyzing Contribution & Profitability
  - New businesses / segments
  - Profit sharing and compensation
- Valuation: Purchase and Sale
  - Ownership interests (internal)
  - Businesses (external)
Creating Value Through Strategic Alliances
Building Value

General Principles

• Understanding the “value” of your business – what it’s worth
• Planning for growth – what is the purpose of the valuation
  – Internal succession
  – Mergers and acquisitions
  – Sale of the firm
• Potential of the firm to fund its internal succession
Creating Value Through Strategic Alliances
Building Value

Methodology and Formula for Landscape Architecture Firms

• Combination of Book Value and Earnings
• “Value” = Book Value + Goodwill
• Goodwill based on a “Multiple of Earnings” formula
Creating Value Through Strategic Alliances
Building Value

Goodwill: The Business Advantage
• Reputation
• Clients and retention
• Specialization
• Technical skills
• Firm management
• Probability the business advantage will continue
• Potential of increased profitability
• Professional staff team, retention
• Transferability of Goodwill
Creating Value Through Strategic Alliances
Building Value

Focus on improving the 2 components of value

– Book Value
  • using financial metrics to improve the quality of the firm’s assets
  • improving project profitability and staff efficiency

– Goodwill:
  • Quantitative: focus on the quality of earnings
  • Qualitative: increasing the value of “goodwill”
Creating Value Through Strategic Alliances
Short Term vs. Long Term Strategies

SHORT TERM STRATEGIES

- Not necessary to commit to building internal resources (e.g. staffing, premises, computers and IT)
- Opportunity to get to know other professionals, companies
- Opportunity to test new markets, services
- Develop a new service in-house
- Collaboration for a specific project
Creating Value Through Strategic Alliances
Short Term vs. Long Term Strategies

SHORT TERM STRATEGIES

• Develop new services internally
• Use of sub-contractors or sub-consultants
• Project joint venture
  – Participants remain as separate entities
  – Joint Venture Agreement for the project
  – Accounting and administrative responsibilities
  – Financing for working capital
  – Sharing revenues and expenses
Creating Value Through Strategic Alliances
Short Term vs. Long Term Strategies

LONG TERM STRATEGIES

• More complex business arrangements
• Ownership and valuation of businesses
• Financing for long-term growth
• Need for higher level strategic planning
  – Due diligence process
  – Internal vs. external development
  – Mergers and acquisitions
  – Commitment of resources
  – Remuneration of senior management
  – Business plan for 1-3 years
LONG TERM STRATEGIES: MERGERS AND ACQUISITIONS

Benefits
• Synergies
• Economies of scale
• Acquisition of specializations
• Access to key professionals
• Increased market share

Planning
• Prepare your business – assess resources
• Search for partners / targets
• Valuation of the businesses
• Combining business cultures
Creating Value Through Strategic Alliances
Managing Risk

OWNERSHIP STRUCTURES – TAILORED SOLUTIONS

• Financial Risk
  – Business operations and cash flows
  – External financing requirements and covenants
  – Investment of capital by owners

• Liability Risk
  – Professional Liability
  – Commercial and Other Liability
  – Insurance

• Business Risk
  – Ownership Agreements (long-term arrangements)
  – Participation Agreements (short term projects, eg. JV’s)
Creating Value Through Strategic Alliances
Corporate Structure

- Architecture firm starts outdoor furniture business
- Takes on a business partner
- Liability risk is segregated
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Corporate Structure

- Combination of 3 firms
- Plan to expand into larger contracts
- Each partner corporation retains separate ownership
- Partnership earnings allocated per agreement
Creating Value Through Strategic Alliances
Corporate Structure

- Combination of architecture and design firms
- Liability risk is segregated
- Remuneration by way of salary/bonus/dividends
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Corporate Structure

Architect 1
Holdco 1

Non-Architect 3
Holdco 3

Architect 2
Holdco 2

Architect Firm

Family Trust

Holdco 1
Holdco 2
Holdco 3

Architect Firm
Architect Firm

Firm earns $100,000

After tax earnings = $84,500

Firm pays dividend to Holdco of $84,500 – no tax

Holdco pays dividend to shareholder of $60,000

Holdco pays Trust dividend of $24,500

Dividends paid to beneficiaries. If no other income, dividend will be tax free

Family Trust

Architect

Holdco 1

Architect Firm

Firm earns $100,000

After tax earnings = $84,500
Creating Value for Your Firm Through Strategic Alliances

SUMMARY

• Strategic Planning for Growth
• Building Value
• Short Term vs. Long Term Strategies
• Managing Risk
• Corporate Ownership Structures
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