

Advice on securing a successful exit from practice life

By Victoria Andrew

Introduction

This advice is aimed primarily at sole practitioners – although some of the content will be relevant to larger practices.

What follows is very much signposting. I cannot cover every eventuality, and, as I make clear in the disclaimer at the end, the content is no substitute for tailored one-to-one advice.

Why me?

- Been there, done that
- Worked on a number of practice sales
- Lessons learnt

So, what do I know about this subject?

I ran successful practice for over 20 years in the London Borough of Bromley. A few years ago, I decided it was time to move on, so I sold the practice.

During the time I was in practice, I also bought and sold blocks of fees.

Today's session covers what I have learnt from my own experience as a practice vendor, and what I have learnt from my clients' experiences.

Outline

- Why you need a succession plan
- Options for passing on your practice
- Maximising practice value: preparing your practice for transfer; presenting the practice for sale.
- Resources available; Questions and answers

Why you need a succession plan

Professional responsibility: don't leave clients in the lurch.

Professional legacy: leave clients with a positive view of chartered accountants.

Benefit from value built up.

As chartered accountants, we do have a professional responsibility not to leave our clients in the lurch. We have a duty to ensure as smooth a transition as possible for them. We need to consider our professional legacy – which includes leaving people with a positive view of our profession. And it would be nice if we – or our heirs – could benefit from the value we have built up in our practices.

Think about it NOW. You have taken the first step by attending this webinar.

Triggering events?

- Illness/declining health
- Death of family member
- Quality of life: spend more time with family; focus on voluntary work/hobbies
- Rewards no longer outweigh the frustrations; changes in filing requirements
- Retirement
- Incapacity (connect plan to LPOA)
- Death (connect plan to will)

In connection with the last two – don't think it won't happen to you – it happened to people I knew! There has been a huge increase in practitioners looking to move on since the start of the pandemic.

In this guidance, I am using the terms succession planning and exit planning interchangeably. As I understand it, exit is about you getting out of your practice, and succession is about who you are going to hand it on to.

Make a plan

So do make some sort of a plan covering all possible scenarios – (there is a proforma in the appendix), and make sure it is consistent with your will and your lasting power of attorney. Some of you may think “I have an alternate” – he or she will deal with it. When did you last have a conversation about the implications of all this with your alternate? Are they still willing to take it on. Who will authorise the bank payments if you cannot?

Too busy to make a plan?

I get it – there are a number of things in my life – like the Lasting Power of Attorney – that I know I need to do. But there is always something more pressing on hand.

For many of you there are endless filing deadlines. Always another client on the phone, or an email to reply to.

But, if you take one thing away from today's webinar, it is this – block out a couple of hours in your diary to think about this, make the plan, type it up, and leave it somewhere where it is easy to find. If necessary, make the appointment with the solicitor and with your alternate.

Options for passing on your practice

Tell clients to go elsewhere

Believe it or not, this does happen. At least make sure that the clients are signposted to “Find a Chartered Accountant,” so they don't fall into the hands of the cowboys. If you are recommending one local firm, do check first that they have capacity to cope with a sudden influx of new clients.

Handover without money changing hands

This also happens. You need to have identified someone who is able and willing to take over – either your alternate or another local practitioner (so there is an overlap with the first option) – or an experienced staff member who either has a practising certificate, or who can obtain one. Why would you choose this option – or the first one – when there is money to be made by selling? Sometimes practitioners just want to get out without the stress of a sale – but in the knowledge that they have left their clients in good hands.

The following options involve money changing hands:

Internal sale

Like the previous option, you will need to have an experienced staff member who either has a practising certificate, or who can obtain one. And like the previous option, it has the advantage that the person taking over the practice is someone the clients already know. And like the first option, you will have had a conversation, followed up with at least a memorandum of understanding, that this is the plan. With an anticipated timeline if it involves your retirement. Does the person have capital? Can they raise a loan? Will you give them a loan?

As I previously mentioned, this presentation is aimed primarily at sole practitioners. If you are in a partnership, one hopes that the plan is written into the partnership agreement – the usual plan is for the remaining partner or partners to purchase the outgoing partner's share for consideration – maybe over a period of time. Have you reviewed your partnership agreement recently? There should be similar provisions in place if the practice operates through a limited company.

External Sale (or merger)

In reality, something may be presented as a merger to the outside world and to clients, when it is really a sale. I have come across very few actual mergers. External sale is the option I shall focus on in the following slides.

Piecemeal sale (“block of fees”) versus all in one go

Looking back, I sometimes wish I had done this instead of all in one go. It may suit those practitioners who want to wind down gradually – but it definitely needs a plan. When you “slice and dice” your client list – which I'll talk about on the next slide, it makes it easier to identify a block of clients who all have the same characteristic – maybe they are all one type of work, or all in the same location, or all have the same type of regulation, or they are all clients where you don't do all the work yourself – much of it is done by staff or subcontractors. If you can downsize your practice costs in proportion to the reduction in fee income, this may be a suitable option.

Pay a manager or outsource the admin

I have never come across these options in real life, but that is not to say they won't be suitable for you or won't work. At the risk of stating the obvious to a bunch of chartered accountants, you will need to crunch the numbers to see if these options will work for you financially.

What are you actually selling? Just fees/goodwill or whole practice?

There is an ICAEW help-sheet on buying and selling fees, which I have provided a link to in the resources section at the end. This includes buying or selling all the fees in the practice. It says:

“Purchasing fees is not actually buying clients – clients have the right to choose their accountants. What is being bought is a right to an introduction and recommendation, and the chance to sell a

service to specific clients including information about the client and the services that they may require.”

If you are selling all your goodwill in one go, you may also need to consider transferring other aspects of the practice, such as staff, premises, goodwill, furniture & equipment, and software licences.

Maximising Practice value

Work out what you have got

This means you need to analyse your client list by age (decades is enough), location (1st half of postcode), business structure, business sector, fee size (GRF: identify 10 largest clients by fee), technology.

There is a proforma in the appendix. Ideally you would have CRM software that will do this for you – otherwise it’s an Excel spreadsheet. The goal is to have a client list you can sort by category. The edited highlights can then be used for marketing.

You may also want to do an internal Practice Assurance review at this stage, if you haven’t done one, or had a review recently. Better to find and address any weaknesses at this stage – rather than when you get to Due Diligence!

There are two major factors affecting value:

Average age of clients

If your practice has a large proportion of older clients, some buyers will try to use this as a lever to reduce asking price. So you can pre-empt that by considering it at an early stage, then pointing out that the asking price reflects this. The same applies to:-

Technology

This is not about what software you use in your own practice. There is a high probability that a buyer will not be using the same. That shouldn’t be a major problem and can be addressed during sale negotiations. What is important to a lot of buyers now is what method clients use for their own record-keeping.

Pricing

- Based on GRF
- Ignore one-off assignments
- Normal range 0.9 GRF to 1.1 GRF
- Lower % for full payment up front
- Higher % for payment in instalments (later instalments reduced if clients are lost)
- Normal instalments 33%; 33%; 33%
- I asked for (and got) 50%; 25%; 25% on 1.1

The default basis for pricing the goodwill of a practice or block of fees is still GRF – Gross Recurring Fees. This will be taken from the client list and normally based on the last invoice or invoices for 12 months’ services. Any one-off assignments are excluded from the list.

I have heard of other bases being used, for example, past or anticipated turnover, past or anticipated profits.

To those of you who have already done a “back of an envelope” calculation and think they can clear £100,000 for a £100,000 turnover practice – I usually say “halve it.” I’ll return to this later on.

I was given a lecture by one potential buyer along the lines that I shouldn’t ask for 50% upfront with two subsequent instalments of 25% each – because the “standard” contract was three instalments of one-third each. I didn’t go with that buyer – because I got what I asked for elsewhere. There is no “standard contract”. It is whatever is acceptable to both the buyer and seller.

Finding and meeting potential buyers

Using a broker

Most charge commission to seller – a few charge commission to buyer instead. They may charge extra for mailout. From a mailout to 300, I received 4 expressions of interest.

Other ways of finding a buyer

You may wish to try other methods first, before appointing a broker:

- a) Approaching a fellow practitioner, whom you know to be in the market for acquisition. This approach may be through a mutual contact – e.g. a fellow professional.
 - b) Asking your Area Society or Town Group administrator to do a mailout on your behalf.
- Would you also like a handholding service? Will a broker do this for you? (ask before you sign up with them).
 - If there is more than one potential buyer, organise a meeting day – you in one place – potential buyers come to you - suggest meetings at 2 hour intervals.
 - Maintaining confidentiality; once expressions of interest received, ask potential buyers to sign a confidentiality agreement – ideally before they know your identity as the seller (if you are not using a broker, you can use another intermediary). This is very important: if clients get wind too early on in the process, they are likely to get nervous.

Talking to potential buyers

The first meeting is mostly a “get to know you” chat and may include the buyer asking the seller how much involvement they are looking for after the sale, and at what rate. As the seller, you should ask buyers what their plans are over the next 5 years; you may be surprised at some of the answers, and that may influence your decision if you receive more than one offer. I have noticed more recently, particularly where a vendor has found their own potential buyer without going through a broker, that these early stage chats are more likely to be done by emails and video-calls. The aim of these meetings is to end up with an offer – subject to contract – either at the meeting itself, or within about a week.

Do you actually need a broker?

I always imagined that they had a database full of acquisitive firms of chartered accountants and would just call them when instructed by a practice vendor. That wasn’t how it worked in my case. The broker sent out 300 “on spec” letters to practices in my area, for which I was charged for the

postage. These letters did not identify my practice – but didn't stop a recipient guessing, and mentioning it in front of one of my biggest clients! So much for respecting confidentiality.

Doing this size of mailout yourself is harder work than you might think: going through the relevant directories for a specific location, picking out likely practices, checking every website to ensure they are regulated, and for cultural fit with the vendor's practice.

I did appreciate the advice I received from my broker (I didn't use a handholding service) on 2 points:

- Selling a practice is as stressful as selling a property (possibly more stressful!)
- A sale is more likely to go through if you can be flexible during negotiations.

Pre-Contract

This next bit can be quite stressful. For me, it took about 4 months, and covered all the discussions from accepting an offer "subject to contract" up to the contract being signed, including due diligence.

- Discussions with buyer: based on "heads of agreement" (see appendix) – roughly the same clauses that you might expect to see in final contract.
- Resolution of possible sticking points (e.g. staff; clawback; seller's consultancy agreement)
- Due diligence: buyers may ask to see a sample of client files as well as practice accounts, tax returns and VAT returns, statements for the practice bank account, records of last practice assurance review, and PII records. Some buyers do no due diligence! Vendors should also do due diligence (e.g. does the buyer have the funds? will they have the resources to service the additional clients? Is the buyer a good fit for your clients?)
- Before the due diligence exercise, it may be time for buyer & seller to sign a further confidentiality agreement (if this was not covered in the first one). The buyer is about to be given access to client details. ICAEW guidance is that we should follow the Code of Ethics on this. There is also the question of GDPR. But remember what I said before about clients getting nervous if they get wind of what is going on too soon? There may be a couple of ways to approach this: the first is to ensure that your engagement letters cover the possibility of practice sale or restructuring as an example of when 3rd parties might have access to client files. You may need to beef up the wording of standard pro-forma engagement letters. The other is to leave the due diligence visit until as late as possible before the contract is signed. This will mean there are only a few days between having to get a client's permission for the buyer to view their file, and the letter going out to all clients informing them of the sale.
- Legal drafting of contract: by a solicitor experienced in practice sales. By this stage, there should be a straw man based on the "heads of agreement" for the solicitor to work from.

For me, there was a lot of toing and froing about staff, based on who would transfer under TUPE and who would be offered redundancy.

There were also a lot of discussions about the calculation of clawback. This is the amount by which the second and third instalments would be reduced for the loss of clients after the sale.

From Contract to Completion

- Letter from seller to clients advising them of the transfer; this could be presented as a “merger” if the seller is staying on board as a consultant. Wording of letter normally by agreement between buyer and seller. At this stage (unless already done) the clients should be informed that their details will be handed over to the buyer – and given the chance to say no.
- Dealing with clients’ concerns; some will contact the seller seeking reassurance, and time for this should be factored into the plan.
- Planning handover of software & data and handover of any physical files
- Finalising legal matters with employees

The length of this period can vary (for me it was 2 weeks) and is by mutual agreement. It may well be planned to accommodate ongoing work commitments.

There were several practical matters to arrange: see the checklist in the appendix.

What happens after the sale?

This is based on my personal experience: there is a checklist in the appendix.

I spent a few days working in the buyer’s office and then went on holiday for ten days. That may have been a mistake! I was trying to put some distance between me & the buyers & let the clients get used to the idea, but there were a lot of queries.

I was supposed to have a consultancy agreement which had been discussed in the pre-contract negotiations. Although I produced a draft, it was never signed by the buying firm. That wasn’t too big a problem, as I am still doing consultancy for them over five years later, and they have always paid me the rate we originally agreed.

Would I do it again?

Most definitely yes, because I had reached a stage where something had to happen. The way I was operating was not sustainable for me personally.

What went right for me?

The sale actually went through in a reasonably short time. From receiving the broker’s flyer to completion was about six months. I would say that is at the lower end of what is possible. I do not regret selling to the firm I did; I still believe that it was right to go for a young, technology-savvy firm – it was the right thing for the clients - even if not all of them appreciated it at the time.

What went wrong for me?

The biggest thing was the amount of clients lost.

Retention after two years was 65%; the target was 90%! The 35% lost was roughly equally split between the 1st year & the 2nd year.

In the appendix, I have included some figures. These are not the actual numbers, but show the same proportions between the asking price, the actual price received after all clawback had been deducted, and the net figure received after all expenses of sale. The final net figure I received was 54% of the original asking price. Remember what I said earlier about having a back-of-an-envelope calculation, and me saying to halve it?!

Reasons for clients leaving fell into three categories:

- Firstly, some clients did not give the new firm a chance. Some of them had been thinking of leaving but the transfer prompted them to act. Many of these clients were based outside London & decided to find a more local accountant. Many of the clients who left at this stage disliked the fact that they could no longer expect a personal service from me.
- Secondly, service by the buying firm was sometimes poor. Despite reassurances that they had the resources to service the additional clients, they had staffing issues during this period, and some new staff were recruited but did not work out. I spent a great deal of my unpaid “handover time” trying to repair damage done by these staff - only for the clients to leave anyway!
- Finally, there were the usual reasons for leaving – for example, the death of a client or the sale or closure of a business.

Another issue was that the partners of the buying firm did not provide me with quarterly updates of clients lost & reasons why (per the contract). I had to chase for this. In addition, they did not instigate the process of calculating the twelve-month and twenty-four month payments; I had to drive this process and both payments were late. The contract did provide for interest, but I didn't claim this, in the interests of maintaining good relations.

Finally, I spent a huge amount of unanticipated, unpaid “handover time” after the sale. Much of this time was spent briefing the partners and staff on particular clients. I wish I had kept a record of this unpaid time but that would have required more effort & focus to maintain!

During the three months between completion and the end of January, I personally cleared all the remaining work-in-progress, for which I billed the buying firm one-third of what they charged to clients. This wasn't envisaged at the discussion stage, and not in the contract; it was done by mutual agreement. I also did some tax returns & accounts from scratch because I was familiar with the software and it was the busy period. Again, I charged the buying firm one-third of the client fee.

During those first three months, I worked five or more days a week, but over the past five years, my involvement with the clients has decreased significantly, although I am still doing one-off assignments for the buying firm.

What would I do differently?

There were some things I might do differently if I were doing this again:

- I might have done the sale in tranches (piecemeal sale). On the other hand, it wasn't right for me at the time; I just wanted out!
- I would have reduced the amount of hand-holding given to clients before I put the practice on the market. It was not easy to wean clients off home visits and personal service. There is a difference between a client-centred practice and a system-centred practice – and I didn't fully appreciate that.

- I would have negotiated a sale price of 0.8 or 0.75 x GRF with no clawback. That would have meant a lower contract price but ultimately more money in the bank.
- I would have set an upper limit on unpaid handover time.
- And finally, I would not have given one of my employees a choice between TUPE and redundancy.

Final thoughts

As I said earlier, when I was talking about alligators, I'd like you to take away one thing:– block out a couple of hours in your diary to make the plan, type it up, and leave it somewhere where it is easy to find. If necessary, make the appointment with your solicitor and with your alternate.

Resources available

ICAEW website:

Some of the following items on [Running your practice](#) under the Practice Resources section may be particularly helpful:

- In the first section on Key Resources and Support, there's a subsection on [Practice Help-sheets](#): especially Arrangements of Alternates, [Buying and Selling Fees](#), [Changes in the Composition of a Firm](#), [Practice Assurance Compliance Review](#), [UK GDPR – Client Files](#)
 - Scroll down to the section on Managing Risk: there's a section entitled [Arrangements to cover the Incapacity or Death of a Sole Practitioner](#)
 - Scroll down further to the section on [Exit Routes and Succession Planning](#) and see if any of the articles are of interest.
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Skeleton Practice Exit/Succession Plan

Aims: choose which apply to you; add any which apply and are not included here.

- Ethical duty to ensure continuity of care for clients
- Remove a source of stress for you
- Reduce stress for those who have to handle your affairs if you are indisposed.
- Have a plan that works for you financially.

Options: highlight those which you are most likely to go for yourself if retiring.

And if someone else is doing this as attorney or executor – which are they most likely to choose?

- Tell clients to go elsewhere – simple retirement/cessation.
- Handover without money changing hands– if there is someone suitable to take over
- Internal sale – if there is someone suitable to take over
- External sale. Will need to find a buyer; think about maximising value
- Merger: often boils down to a sale (although it may be presented to others as a merger); true mergers are unusual
- Pay someone to manage the practice & continue to take the profits. Will this work financially? And from a regulatory point of view?
- Outsource the admin. (but you will still have to do the client work)
- Piecemeal sale / downsizing (“blocks of fees”). Remove categories of work one at a time. Can you reduce costs proportionately at the same time?

Allow 6-12 months for the whole process.

Have a conversation with your alternate.

Review will, LPOA and (if appropriate) partnership agreement.

Interim plan. Think about how you (or your attorney or executor) will run the practice whilst the handover process is going on.

Proforma Client Analysis List

If this is being sent to potential buyers, client codes should be used instead of actual names. If you don't use client codes, find some other method of anonymising the clients, such that you can still identify them yourself. If this list is for internal use only, the client names can be left in. This proforma is available in Excel format on request millcove1912@gmail.com

The clients can then be sorted easily into different categories. In an ideal world, you would have CRM software that would do this for you – or could at least export the data into a csv or Excel file. When you get to the Due Diligence stage, you can add AML columns for:- year started acting, ID risk, reason for ID risk rating, ID up-to-date (Y/N).

XYZ & Co Chartered Accountants

Date 23/06/2022

Client Analysis

Updated

Client Name	Fee (GRF)	Location	Age	Business	Business	Client
	(Excl VAT)			Sector	Structure	Tech
Mouse, Mr M	£500	BR6	48	Rental	Personal Tax	Excel
ABC Garage Ltd	£2,000	SE1	56	Vehicle Repair	Ltd Company	Xero

Heads of Agreement Checklist

Matters to be dealt with in pre-contract discussions, and to form the basis of clauses in the final sale contract. This list is not exhaustive.

- Formal names and addresses of parties (buyer and seller)
- Planned date for buyer's due diligence visit
- Planned date of contract and completion
- What is being transferred: goodwill (list of clients + GRF in appendix); office equipment; software & data; physical files; employees; premises.
- Price and basis of calculation. Timing & method of payment(s)
- Interest on delayed payments; remedy for buyer if seller doesn't pay up by a specified date
- Clawback
- Supplier contracts
- Debtors; creditors; WiP; bank balance?
- Seller's run-off PII
- Restraint of trade - seller and seller's staff: check employees' and subcontractors' contracts
- Efforts by buyer to maximise income post completion: timely invoicing; recovery efforts; standards of client service
- Buyer to notify seller at regular intervals of complaints, client losses, reasons for client losses
- Seller's consultancy role with buyer's practice – probably the subject of a separate contract, but will be included in pre-contract discussions
- Wording of client letter A (sent by seller to clients after contract & before completion)
- Wording of client letter B (sent by buyer on date of completion or on specified date thereafter)
- Subcontractors: will the buyer be taking them on?
- Employees: will the buyer be taking them on? (more likely if they have a relationship with the clients). Redundancy or TUPE?
- Will the buyer have sufficient staff and partner time to get to know and service new clients?
- Premises: less of an issue if seller practices from own home, but does buyer have sufficiently large premises from which to service an expanded practice? Is the seller tied into a lease? Some buyers will run seller's premises as a satellite office until the end of the lease. What if seller owns office premises?

- Storage of archive files
-

Post-contract, pre-completion checklist

Some can wait until after completion if done promptly

Does not include matters related to office premises

- Letter from seller to clients informing them of the transfer.
- Provide seller bank details to buyer (for payment due on completion)
- Arrange transfer of accounts/tax software (transfer licences to purchaser?)
- Arrange transfer of digital client data (accounts, tax returns, working papers, contact details)
- Notify ICAEW (no longer running a practice; change address from office to home or buyer's office)
- Notify all suppliers & other membership organisations (ceasing trading; change address to home if continuing arrangement)
- Arrange change of agent details with HMRC: may be easier to keep separate agent account & just change firm name and address, rather than trying to merge with buyer's agent account
- Notify HMRC – own tax & NI – probably just change address from office to home.
- Notify P I insurance company & arrange run-off.
- Clear and bill as much WIP as possible (depending on what is in sale contract)
- Dispose of branded stationery, brochures & merchandise
- Cancel or transfer SOs & DDs.
- Arrange for website to be taken down; e-mails diverted; phone diverted
- Issue termination letters to subcontractors (even if continuing to work for merged practice); may be one month before completion depending on their contract.
- Order moving boxes for files (if any hard copy); arrange staff member to pack them; book removal van to move boxes of files + filing cabinets on completion day.
- Finalise legal matters with employees – if redundancy, give them draft settlement agreement for them to seek independent legal advice (vendor has to pay costs – up to a limit). Calculate accrued holiday pay; final payroll returns & P45s.
- Notify HMRC re end of PAYE scheme: final returns.
- Letters from buyer to clients introducing themselves. Clients must consent to the change, which should be covered by them signing new engagement letters.

Post completion checklist

Does not include matters related to office premises

- Anything not done on previous list
- Check 1st instalment in bank
- Agree final amount of broker or adviser invoice and pay.
- Calculate and list debtors & WIP at completion date; WIP list to buyer.
- Consultancy work for buyer:
 - “handover time” (should have set limit before contract)
 - billable work + WIP at completion date (depends on agreement with buyer).

- Keep a record of paid and unpaid time – review regularly (maybe when invoicing)
 - Agree invoicing arrangements (date, rate & frequency) with the buyer for your work
 - Own accounts & tax to completion date. Tax return to include Capital Gains Tax pages?
 - Chase debtors at completion date.
 - Close business bank account when all debtors received.
 - Clear out office.
 - Keep a record of paid and unpaid time – review regularly (maybe when invoicing)
 - Monitor clients leaving and reason (with input from buyer)
 - You may have to be proactive about instigating process of calculating 2nd and 3rd instalments – put in your diary.
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Asking Price; Contract Price; Clawback

*These are not actual figures, but are pro-rata based on theoretical turnover figure.
Costs do not include additional postage, phone & loss of chargeable time!*

Turnover year ended 31-3-16	£105,031
Turnover period ended 4-11-16 (7 months or 218 days)	£52,486
GRF at meeting day	£100,430
Asking price	£110,473
GRF at contract date	£95,502
Contract price	£105,050 (just under 1.1 x GRF)

GRF at completion + 2 years £62,419 Client retention at 2 years 65.4%

Total received in 3 instalments (after deducting clawback) **£68,991** (1.1 x £62,419 + £330 commission on fees paid to buyer by clients subsequently lost)

Associated Costs Total: **£9,089**

These are not actual figures, but are pro-rata based on theoretical turnover figure.

Not included: additional postage, phone & loss of chargeable time!

Solicitors re sale contract and consultancy agreement	£3,960
Employees (termination; PiLoN; accrued holiday pay)	£3,310
Solicitors re termination of employees	£924
Broker: postage £254 (No broker's commission payable by seller)	
ICAEW course on exiting from practice:	£211
Meeting costs (room hire; mileage; parking)	£217
Removal firm + archive boxes	£213

Original Asking Price £110,473

Amount Received Less Costs £59,902 = 54% of asking price!

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