

Growth matters

Succession planning

Succession planning is an age old issue for accounting firms, and recent years have brought a new and unique set of challenges which accountants now have to face. In this second series of roundtable discussions for accountants, Macquarie Relationship Banking brought together partners from accounting firms around Australia to discuss these new challenges and practical suggestions for how to address them.

Rob Patterson, management consultant and National Chief Operating Officer of Macpherson & Kelley Lawyers, posed a number of theories to explain the shift in recent years towards partners looking to sell their equity and facing a seemingly smaller market of buyers.

Demand and supply

Rob explored the cycle of demand and supply and how this is contributing to a shift towards an increasing number of sellers and fewer buyers in the accounting industry.

Supply:

In the post World War II years, a significant increase in birth rates led to the emergence of a new generation – the ‘Baby Boomers’. This generation has a longer life expectancy than previous generations and subsequently did not retire at 55 as expected, but are looking to retire now. Many practice owners facing retirement lost value in investments because of the global financial crisis (GFC) which depleted their retirement savings and resulted in them delaying discussions around succession plans or in many cases, not undertaking any succession planning at all.

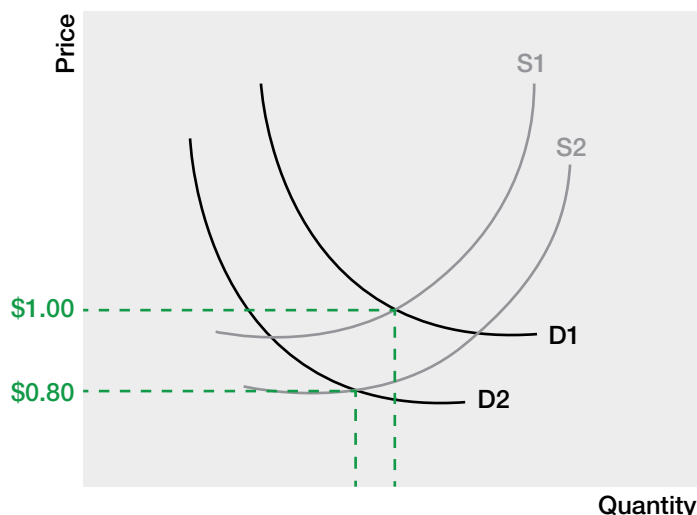
Demand:

Since the 1990s, there has been a global decline in the numbers of students studying accounting. There are various reasons for this, including the increased availability of other business majors, lack of information about the role of accountants in business and public corporate failures linked to poor accounting practice that have tarnished the integrity of the profession.*

Adding to this decline in young people entering the industry, there is a limited number of existing practitioners with the financial capability to buy equity. ‘Generation X’, the generation following the Baby Boomers, married and had children later in life, consequently pushing out the age at which they would have previously looked to fund an equity buy-out.

Many firms cited that layers of career managers, with no view to partnership, are appearing within practices. While these are valuable members of staff, to more junior staff this can seem like an obstacle to their progression, which sometimes forces potential successors out of the firm.

Depicting this shift in demand and supply, are new curves (D2 and S2), indicating a lower price for firms.



Accounting Partner insights

- *“Some accounting graduates have a longer term goal to go back to the family business.”*
- *“Accounting isn’t held in the same esteem as it used to be. We need to get the ‘wow factor’ back.”*
- *“Accounting practices are focusing on their desire to be better business people as opposed to being just professional practitioners. This means a paradigm shift in the way they market, finance and create systems within firms.”*
- *“Several firms we know of have sold to competitors at quite a lot less than the old notion of dollar for dollar.”*
- *“We’ve heard of several smaller, non specialised firms where the sole practitioner had no interest in succession and ultimately could not sell his fees. He simply wound his small firm down.”*
- *“More partners are now considering retirement post the GFC shock.”*

Forms of succession

1. Sale of fees.

This format involves partially selling portions of the practice which can be difficult to do.

2. Merger.

Initially finding the right business to merge with can be difficult. Overcoming cultural differences can be an issue but mergers can succeed if synergies exist, such as a common direction and growth trajectory for the business as well as similar HR practices and employment culture.

3. Sale to an existing partner.

This can be a good option if the existing partner is of the right age demographic but needs to be something that both parties agree on and are passionate about.

4. In-house succession.

This usually involves bringing in a new partner from the senior management team. It is generally regarded as the best option as it is a good way to maximise value, provides continuity for staff and less disruption to clients.

5. Consolidator.

There are currently a few listed entities in the market that buy shares in accounting businesses and whether they retain a passive shareholding or controlling interest in the business, the uptake of this option is likely to increase in the future.

6. Orderly wind-up.

For most practitioners, the idea of wrapping up the business they have built is not a preferred option.

In-house succession

Enabling partner buy-in from your existing management team allows for maximum value for the exiting partner and reduces disruption to the business, its clients and staff. In order to best facilitate in-house succession, there are a number of factors to consider.

<h3>HR management</h3> <ul style="list-style-type: none">– Start discussions with staff early, even at the recruitment stage, outlining your long term plans for the practice.– Develop clear and transparent career plans that outline how staff can progress within the firm. Set clear KPIs and expectations.– Identify talent within the firm; let key performers know they are valued, develop a skills matrix that identifies strengths and areas for leadership development.– Hold regular reviews with staff, ideally quarterly, but half yearly at a minimum. Encourage managers to have open, honest discussions with staff and address their training needs.– Establish a culture of autonomy and accountability.	<h3>Embrace diversity; Gen X and Gen Y</h3> <p>Gen Y has a reputation for preferring shorter tenures in an organisation. However, evidence suggests that Gen Y will prove loyal if presented with the right circumstances. You can provide this by:</p> <ul style="list-style-type: none">– Giving regular feedback.– Ensuring there are learning opportunities and diversity at work.– Creating a work/life balance and flexible working culture in your office.– Encouraging corporate social responsibility – research indicates Gen Y is interested in this aspect of the organisations for which they work.** <h4>Accounting Partner insights on Gen Y</h4> <ul style="list-style-type: none">– <i>“They’re not the same as us, but that doesn’t mean they can’t be successful. It’ll just be different. Like is attracted to like and they’re likely to win clients differently to how we did.”</i>– <i>“Make buying into the practice more attractive by promoting diversity, work/life balance, corporate responsibility and involving family in work functions.”</i>
<h3>Embrace diversity; encourage a gender friendly environment</h3> <p>While there are now greater numbers of female accounting graduates than males and women make up 50 per cent or more of the staffing mix in firms, there is a dramatic difference at partnership level, with women comprising only 18 per cent of all equity partners at the Big Four firms.***</p> <ul style="list-style-type: none">– Actively discourage gender bias in your firm.– Embrace neutral networking opportunities where everyone can network and feel comfortable.– Endeavour to provide a diverse group of role models for staff.	<h3>Facilitating finance</h3> <p>The capacity of individuals to fund an equity buy-out has changed over the last number of years. The GFC, fluctuating property prices and changing demographics have all impacted this capacity. For example, twenty years ago a potential successor in their mid thirties generally had equity built up in their home. This is no longer the case and purchasing even 20 per cent of a practice can be expensive and often beyond the means for incoming owners to source themselves. There is reluctance towards vendor finance; it can require a long repayment period and can create inequality in the boardroom. Partners are increasingly keen for buyers to secure their own finance. This makes all partners equal in the boardroom, rather than one partner being in debt to others.</p> <p>The cents in the dollar way of valuing Accounting practices is being seen less and there is now a move towards valuing a firm on a future maintainable earnings basis.</p>

Suggestions from accounting firms

- **Entry and exit price** Representatives from larger firms suggest the better model for succession and buy-in is a lower entry and exit price. One of the firms who attended had a 20c entry and exit price averaged over two years.
 - **Gifting** A unique solution was described in one of the sessions which saw one partner gifting a percentage of the practice to staff after three to five years, then giving key staff an option to buy after this period.
 - **Options for loyalty** A similar structure offered the Senior Associates a 50 per cent option in the partnership which is exercised in five years on satisfaction of a number of key hurdles. This has the benefits of tying the Senior Associate to the firm and driving growth in the partnership.
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Conclusion

When it comes to succession - start planning now.

1. Think about the likely forms of succession and what best suits your firm. Identify three to four people or firms that you believe would be interested in buying equity in your firm. If you haven't already started to discuss potential arrangements with these parties, now is the time to make sure they are aware of this!
2. Enhance your practice; you can't just get by anymore.
3. Think about your retirement; what will you need and what do you want?
4. Talk about succession from a very early stage with quality staff. If you have career senior managers who have no desire of becoming equity partners, consider sharing this fact as it's possible that the more junior staff will assume a roadblock to partnership exists.

We would like to thank our roundtable participants for their candidness during the roundtable discussions and the insights they brought to their respective groups. Succession planning will always be important to accounting firms and is a key area of focus for Macquarie Relationship Banking.

We want to help our accounting clients empower the next generation of leaders to buy into accounting practices by regularly working with partnerships to determine how to structure, plan and fund the release of equity to existing partners or the admission of new partners.

Please talk with your local Relationship Manager to enjoy a distinctly different banking experience.

macquarie.com.au/accounting

* Akbrecht & Sack, Accounting Education: Charting the Course through a perilous future, 2000.

** Maree Mattner, Generation Y and the rise of the interactive and online HR, HC Online, 3 February 2011.

***Public Accounting Report: Women continue to advance into leadership at largest firms, 15 June 2010.

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