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Notes:

“Erroneous assumptions can be disastrous.”

– Peter Drucker

“The significant problems we face cannot be solved at the same level of thinking we were at when we created them.”

– Albert Einstein

CHAPTER 2
FUTURE ACCOUNTING FIRM SERVICE MODEL

Introduction

For the seven decades I have been involved with the profession the first six can be characterised as being ‘more of the same’.

The current decade is seeing more change than ever before – maybe more than in all those previous six decades combined.

Clients are increasing able to use technology to deliver certain results, e.g. complete tax returns or prepare their own accounts.

Government is increasingly requiring, or at least facilitating, online filing while the technology companies are busy delivering Cloud based applications to facilitate that objective. The accountant, in some scenarios is looking like the ‘replaceable’ middleman.

In some countries (e.g. UK and Australia) government is requiring less information. In the UK the government has announced that there will be less need for Tax Returns in the future while cash accounting enables most small businesses to deliver just the top line and bottom line results – not the full profit and loss account or balance sheet

In some countries (e.g. South Africa and Ireland) more regulation has been introduced. But, the regulators infrastructure is considered inadequate at best while the regulation, of course, adds little or no value to clients.

The [UK] history of Institutes reporting on the firm of the future

In 1998 the ICAEW and other Institutes published a 36-page consultation document report entitled, ‘Added-Value Professionals’. This was followed up in January 2003 by a 32 page report entitled, ‘The Profitable and Sustainable’ Practice.

Both reports envisaged the oppathreat of technology and the Internet, the need to move on from being reliant on fees from compliance and to develop a range of other advisory/value-driven services.

How have these reports been received?

I think it is fair to say that the first report was better received in that it was the first one and comprised some challenging material that firms needed to consider. The second report reiterated much that was in the first.

How many firms changed as a result?

I do not know. But these reports probably accelerated the development process for some firms. Larger firms were probably already ahead on many aspects of the report recommendations. What I am certain of is that some firms failed to make changes. It wasn't that they did not try - it was more a case that there was no shortage of compliance work - clients were not queuing at the door for some of the new services that firms were seeking to sell clients.

Lessons learnt

I think the major lesson that has relevance today is that firms succeed when they:

- Bring in a specialist who is dedicated to a particular service, or
- Develop a range of advisory services that can be seen as small step services on from the compliance relationship, that

    Meet a current need, and

    Deliver a ROI – no just alluding to one

Sometimes when I am lecture about developing new services accountants tell me that they, "do this work but don't charge for it." So how to address that issue?

A straightforward approach

Decide what your main 5-10 extension (a range of small step services that are natural follow ones from compliance) services are. Make sure you have the systems (letters, spread sheets etc.) so you can deliver these cost effectively. Create your marketing material (brochure cards/newsletters and so on). Make sure these services feature on your website and in your reception. Determine the price starting point – yes the dreaded - prices from...

Make sure you develop a plan to introduce these to your top 20 clients and introduce them at the outset to:

    Your advocates (banks, solicitors, clients who are happy to refer you and so on)

    All your new clients

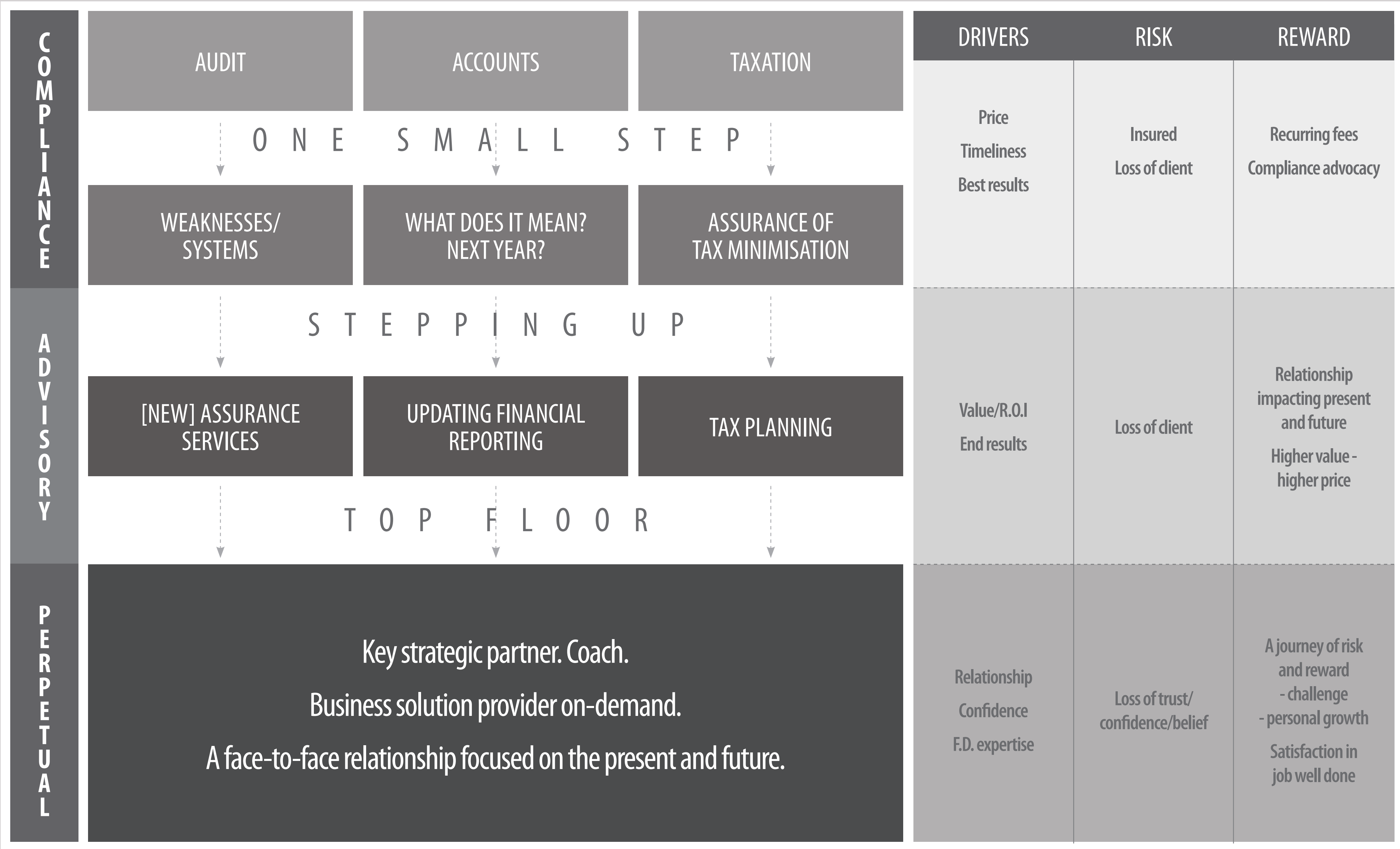
Finally make sure your staff know about your [extended] services and look for opportunities to refer leads to you. Some of these services should also be ones that your staff can get involved with – in identifying which services clients need and maybe also in the delivery of these services.

Notes:

"Here is the prime condition of success: Concentrate your energy, thought and capital exclusively upon the business in which you are engaged. Having begun on one line, resolve to fight it out on that line, to lead in it, adopt every improvement, have the best machinery, and know the most about it."

- Andrew Carnegie

FUTURE ACCOUNTING FIRM **SERVICE MODEL**



Notes:

CHAPTER 3
TRENDS, BENCHMARKING AND INSIGHTS

Let's look at [some] trends in the profession

The basis for this material is surveys published in the USA by Mike and Kelly Platt of Inside Public Accounting. These surveys are based on responses by more than 500 firms from firms of all sizes. For the purposes of providing information that will be of value I have included benchmarks that I consider apply to firms with revenues of between £1 and £15 million.

But before we progress, a reminder that this is one business (aka as a profession) where there are very few standards in performance.

All references are made on the basis that the survey results are always presented and interpreted on an apples for apples basis – so the impact of mergers does not distort the results.

1 Organic revenue growth

What firms are achieving? On average firms currently grow thereabouts to 5 per cent with a range from 5% with very few firms achieving somewhere in the 30% region while about 15% of firms turned in negative performance.

Trends? Growth rates have marginally increased over the past few years.

Key questions:

1. What have you achieved in the last five years – net of inflation?
2. What could you realistically stretch to achieve in the next 12 months?
3. This should involve stretch. What does this look like? What has to be done to achieve that growth rate?

2 Revenue per chargeable hour

What is your revenue per chargeable hour?

Revenue per charge hour formula:

$$\frac{\text{Net fees}}{\text{Charge hours}}$$

An increasing number of firms are now earning fees from services that are not necessarily measured by the chargeable hour. These include services such as wealth management fees, M&A success fees and computer sales with these accounting for maybe as much as 10% of fee income.

Notes:

"There's no benchmark for how life's "supposed" to happen. There is no ideal world for you to wait around for. The world is always just what it is now, it's up to you how you respond to it."

– Isaac Marion, *Warm Bodies*

Key questions:

1. What have you achieved in the last five years?
2. What could you realistically achieve?
3. How often will you monitor this performance?
4. What services do you or are you able to develop that are not based on the chargeable hour?

3 Revenue per employee

Of all the metrics that can be tracked, this is one that I think is of particular importance. Some metrics can, at best, be ambiguous, and at worst downright misleading. For example, revenue per partner – how are non-equity partners accounted for? Revenue per professional can also be defined differently by different firms. Are para-professionals included? Partners?

A good approach, applied consistently looks at the number of full time employees (FTE) on the basis of defining FTEs as including fee earning staff including partners, paraprofessionals and part-time staff (calculated based on the proportion of their time compared to a full week).

The revenue per employee will typically depend on your countries economy and firm salaries. Some of the primary factors affecting this metric include

- Reduced fees due to client pressure for lower fees
- Partners' willingness to demand what is perceived by the firm as a fair and economic fee
- Market place competiveness, for example in the area of proposals
- Staffing for growth

4 The shrinking profit margin

Remember the days of one third, one third, one third? That is one third of revenue was accounted for by salary, one third overhead and one third was profit. For most firms those margins are now consigned to history.

- What is your margin?
- What are you doing to increase it?

This is referred to again in 7 below.

5 HR costs as a percentage of the top line

Staff costs have increased including the cost of salary, benefits, training (time and money), holidays and 'bank' holidays.

Firms in some countries report that staff performance is the biggest issue they face.

Worryingly, many firms are now reporting staff costs approaching and sometimes breaching the 50% barrier. Include a market-based salary for partners and how does your cost of salaries compare with gross revenues?

Notes:

What did this look like five years ago? Importantly, what can you do to improve profitability and reduce the cost of salaries?

What are your HR costs? The percentage of HR to gross fees must be monitored and any upward trend reversed. There is no way your firm's profits will increase unless this happens.

6 IT cost as a percentage of the top line

This has increased dramatically with technology companies typically charging for software based on a per seat cost. Hardware and software require constant updates and along with that the cost of training and developing competencies.

More about this later.

7 Fee resistance

Clients are more fee resistant. More could be said here but that is reserved for another time.

So what are your current fee trends? What is your margin? All the benchmarking reports I have seen include graphs with margin showing a downward trend. These trends still show the most profitable firms generating a profit margin of 33% but firms in the lower range are reporting an average margin in the 25% region.

Key questions:

1. What has been your profit margin over the last 5 years?
2. What does your strategic plan envisage?
3. What does the new norm for profit margin look like?

8 Net income per equity partner

When the global financial crisis struck in 2008 it did not take too long for firms to start saying goodbye to staff that were considered surplus to requirements. This exiting of resources also extended to partners with some who were close to retirement taking the decision, maybe with more than a little help, to vacate their desks while others were simply shown the door. The consequences? In many cases net income per equity partner increased.

How has this happened while clients have remained price conscious? How has this happened when many firms report struggling to find the right talent? There is, of course, more than one reason and reasons will vary from one firm to another. Factors include:

- Gaining more clients than have been lost
- Merging and gaining the advantages of lower overhead per unit of revenue
- Developing niche and non traditional services

What should net income per partner look like? I have seen this vary from as little as £7,000 for a [full time, 3000+ hours p.a. sole practitioner] to £500,000 average for a 10 partner firm.

Notes:

What is your country's average pay? Multiply this by 5.5 as your first benchmark comparison with your own performance. Certainly your profits should exceed that.

9 Time on

When I first became involved in consulting time on (chargeable hours) for partners looked like 1200 hours in the USA and about the same in the UK.

Drift. How times have changed.

Today in some countries time on has drifted south to less than 900 while in the UK partners average thereabouts to 850.

I sometimes tell the story of one client firm whose managing partner (900+ chargeable) instructed me to consult with the firm. One of my briefs was to coach a partner whose performance had reduced to 450 charge hours a year. During my coaching time I managed to help him nudge his hours moving in the right direction, albeit only by a small increment. After consulting for three years we agreed the firm had made significant advances and they were now on the right path. Some three years on I met up with the managing partner and during the course of our conversation I mentioned that I was telling this one story about the partner who only accounted for 450 client hours. He smiled and said, "Yes, I know, but let me ask you to guess how many hours he is doing now." My guess was wrong – time on is now down to 350.

10 Non equity partners (aka salaried partners)

The traditional model of automatically making an upcoming manager is, I think, long since dead in the water. For firm profitability to be sustainable there is going to have to be a further shift which most likely will look like one equity partner to one non equity partner.

Where are we at now? I do not have the answer to that for the UK but in the USA 66% of reporting firms have non-equity partners. Typically non eqs. do not have the same capital requirement or the same levels of risk. However their time on and contribution is within reach of the equity partners. Their net income is maybe half that of the equity partners – maybe even less.

11 Where do new partners come from?

Typically 60% are promoted from the firm's talent pool and 40% are lateral hires from another firm.

12 Partner reviews

Typically only 50% of firms have a partner review process. So, you have reviews for all staff but when someone reaches the Holy Grail the review process defaults to partner meetings and maybe MP coaching?

13 What is the average age of the partner group?

Accountancy Institutes in the USA, UK and South Africa all report and have concerns that so far as practice is concerned this is an ageing profession. Your next partner decision – will this reduce your firm's average age?

14 What are the primary service sectors?

After auditing, accounting and tax services firms derive income from a range of other services. The following represent service specialisations that account for the 20% of firm revenue derived from non-compliance work.

Business valuations	0.5-1.6%
Business advisory services	1.6-5%
Computer consulting	0.6 – 4%
Fee based financial services	0.5 -3.4%
Commission based financial service	0.1 -3%
Health care	0.1-2.5%
Litigation support	0.3-2.2%
M&A	0.1-0.8%
Employee benefit admin	0.1-1%
HR consulting	0.1-0.5%
Other	2.5-11.8%

15 Lock up

Debtor average days	55
WIP average days	25
Total lock up	80 days

16 Percentage of billing rates compared to equity partners

Equity partners	100%
Salaried partners	95%
Profession staff with 9+ years of experience	70%
Professional staff with 6-8 years of experience	55%
Professional staff with 3-5 years experience	45%
Professional staff with 0-2 years experience	35%
Para professionals	30%

This guide might help you review our staff charge rates.

17 Utilisation

Auditing and accounting	1300-1500
Taxation	1300-1400
Firmwide	66-72%

18 Staff hours

Professional staff hours	1900-2100
Professional staff hours billable	68-88%
Average charge hours – non-professional staff	200

19 Charge hours per professional staff

0-2 years experience	1350-1500
3-5 years experience	1500-1700
6-8 years experience	1400-1500
9+ years of experience	1200-1500
Paraprofessionals	1200-1400
Other staff	900-1400

Notes:

"The secret of leadership is simple: Do what you believe in. Paint a picture of the future. Go there. People will follow."

– Seth Godin, *Tribes: We Need You to Lead Us* commitment from your team is a vital (but often overlooked) ingredient to good branding.

Notes:

PS – A firm that commits to investing in the future

The accountancy profession does not have a reputation for being at the leading edge of innovation. But as noted above – there are plenty of opportunities to innovate.

Many accountants I know do not have a business plan as such – their definition of a business plan is a budget!

Notes:

Internal environment

- Financial position – Capex. Lock up. Profitability
- Organisational structure – Equity. Non equity. Departmental.
- Growth trends – what is historical. What is achievable. Realistic
- Pricing position
- Capacity. What does stretch look like? Improving timeliness.

Analysis of strengths, weaknesses, (both internal) threats and opportunities (both external)

Drilling down into specifics – ensuring that they are all joined up

Marketing, Sales, Production, Innovation, Human Resources, Finances, Administration.

Where do we wish to go?

What should we assume?

- Economic growth
- Compliance services - growing, stable or in decline
- Competitors – those in geographic proximity. Cloud based
- Technology – what investment is required. Training
- Access to funding
- Access to talent

A Mission Statement is important

- Begin with the end in mind
- Ensure it is compelling and inspiring
- Focuses on the benefits your people derive from the organisation
- Eliminates conflict and channel resources
- Are not goals; but about the on-going direction
- Is not financial
- Is not focussed on quality of service
- Not carved in stone, but also not changed on a whim

How do we get there?

Identify Key Result areas

Establish goals by Key Result area

Establish SMART goals

Specific

Measurable

Achievable

Realistic

Time based (or could be trackable)

Notes:

“A man must be big enough to admit his mistakes, smart enough to profit from them, and strong enough to correct them.”

– John C. Maxwell

4. Look at your current client lost – what are your cross-serving opportunities – i.e. where are you underserving clients?
5. Establish a marketing budget – recommend not less than 3% of gross income
6. Develop incentives for new and share business

Incentive Plans

1. What is the philosophy behind your remuneration / profit sharing plan?
2. Are there adequate incentives for gaining new business?
3. Are there consequences for not maintaining the business of clients?
4. Are there processes for enabling staff and partners to identify further client-service opportunities?
5. Are there reward schemes in place that motivate and reward accordingly?
6. Are your plans creating the desired behaviour?

A Few Specific Action Pointers

1. Create firm-wide reassurance that the factors affecting profit sharing are accurately and fairly computed.
2. Reward staff monthly – maybe with a quarterly adjustment
3. Evaluate whether your reward and recognition systems are having the intended effect

Continuous Marketing

It has oft been observed that the marketing budget is one of the earliest casualties in financially challenging times while in an upturn the marketing spend is perhaps regarded as an affordable luxury.

Marketing is like the supply of gas or electricity. It is (apart from black outs) continuously available. Marketing is an investment in the future success of the business. It is never to be regarded as optional – it is just as essential as your staff or their investment in training. It is about ensuring that the firm has a continuous pipeline of desirable clients.

Investing in marketing is an essential business pursuit.

Just as entrepreneurship has at its heart adapting and positioning the business for the future, so marketing has at its heart delivering a continuous supply of new business opportunities.

“But we gain clients from referrals.”

Yes, and rightly so. But research demonstrates that while 90% + of clients are happy to recommend 90%+ of clients also say they have never been asked to recommend.

Notes:

9 Credit/debit card costs

In 1992 I was consulting with Jerry Atkinson who was the founder and the then managing partner of Atkinsons, Albuquerque, NM, USA. He showed me a marketing card that was introducing a new service enabling clients to pay by card. While clients can pay by direct debit or cheque it is good to enable clients to pay by whatever means they find appropriate. Dentists accept payment by card –usually within 5 minutes of the end of treatment.

Many firms are now accepting payment by card. Have you checked as to whether you could reduce the cost of the initial merchant cost?

10 Guarding against theft [of time]

While theft may not be something you regard as an issue the theft of time can be.

Recently, my wife visited our hairdresser (a former client of my practice and one with the reputation of being the best hair salon in Bristol). The owner was more than a little annoyed because the barber who does my hair had taken time off for his grandmother's funeral and advised he was not planning to return until the New Year. As this was around Christmas he was fully booked and the salon owners were left cancelling some appointments and having to hire in another barber over this busy period. In another instance I have a client who has a number of problems with staff being off unwell on a regularly occurring basis and even staff who were supposed to be on courses who had decided to 'skip' the course.

One of the primary issues arising from this is that other staff know what is going on and are watching how you respond.

Do you hold a back to work interview when staff have been unwell for more than, say, two days? While you do not wish to encourage staff to return to work until fully recovered neither do you wish the sick leave to last longer than appropriate.

While on the subject of theft the same principal applies to the write up of time sheets. Staff should know that recording time accursedly is essential. Charging time that has not been spent is, potentially, unfair to the client whose costs sheets bears the unspent time. Not recording time, especially if it out of normal hours time is unfair to staff – even though their motive well be not to be unfair to the client. Eventually this could become a habit with a number of possible knock-on effects.

Interestingly, it is often the firm owners who are in first and out last and yet have time sheets that only reflect a standard working week. This can establish an unhealthy culture of expectancy – a situation, which some people tell me, is a feature of some of the big accountancy firms they have worked for.

11 Idle assets

Do you have any assets lying around that are no longer being used? If so they are taking up space while they are gathering dust. Could you dispose of these either by donating them to charity or by selling on sites such as gum tree/eBay?

Notes:

CHAPTER 13
OUR PARTNER PERFORMANCE MODEL

I was first introduced to the Partner Performance model by Dave Cottle (my co-author of Clients 4Life) who had first seen this when studying the Weiner Worksheet, developed by Ron Weiner of New York. I find this provides valuable insight into the core model of how you can look at an accounting firm and the keys to how you can take management decisions that improve firm profitability. So often management material is adopted by many and I wish to give credit where it is due.

In Double Your Income we engage with the LUBRM model from the perspective of an individual firm owner.

The four types of management activity

Our firm revenues are derived from our productivity (doing the work) and our pricing (the amount we charge).

Our net income is the revenue, less the cost of earning that revenue (cost management), less the write downs taken (client management).

Therefore, in generating a profit firms engage in four types of management activity:

1. Productivity
2. Pricing
3. Cost management
4. Client management

These four management activities combine and provide five keys that influence the quantum of the bottom line.

The five keys to firm profitability

Long term keys:

1. Leverage (L)
2. Margin (M)

Short term keys:

3. Billing rate (B)
4. Utilisation (U)
5. Realisation (R)