Accounting firm mergers and acquisitions

Whether you're looking to buy or sell, here's what firms need to know about today's M&As

White paper

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M&A activity within the accounting profession has significantly changed over the years, fueled by aging firm partners and owners on the cusp of retirement, weak succession planning, and talent shortages. So, what does this mean for today's firms looking to buy or sell?

In years past, firms looking to grow through acquisition typically set their sights on acquiring smaller, traditional compliance firms with solid profitability. Now, however, many firms are more interested in finding the "right fit" and they're being much more selective when looking to make an acquisition. Looking ahead, this buyer's market shows little signs of slowing.

As Terry Putney with **Transition Advisors** explained in the **2022 edition of The Rosenberg Survey**, "Overall, in the M&A world for accounting firms, the level of activity has ramped up significantly. Firms that have a need that an upstream merger or sale can solve have come out from the COVID haze the last two years ready to pursue solutions. Firms looking for growth through M&A continue to use this tried-and-true method of accelerating growth."

He continued, "We have seen firms take to heart the need to diversify their service offerings with an emphasis on non-compliance-based services. CAS (client accounting services) has exploded and is playing a significant role in many firms' offerings as well as a rising in-demand niche for acquiring firms. Firms are facing a lot of challenges with adapting and implementing new technologies. Most of the firms we work with realize they can't be left behind with obsolete technology. The COVID-19 pandemic forced many practices lagging in technology to install and upgrade their IT to remain functioning via a remote workforce."

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Further complicating matters is the fact that M&As can be easily mismanaged. Without proper due diligence, a clear strategy, and open communication, the desired results of an M&A can be difficult to achieve.

In fact, according to collated research and a recent BluWave article, the failure rate for M&As continues to sit between 70% and 90%. Reasons cited for failure include inadequate due diligence, cultural differences, operational differences, regulatory issues, and poor communication.

To help firms succeed and better navigate the paradigm shift in M&A activity, this white paper explores what firms must consider when looking to either buy or sell and provides actionable tips that can be set in motion today.

Looking to sell? Better have curb appeal

When homeowners are looking to put their home on the market, one of the first things they should think about is curb appeal. How attractive is their home when viewed from the street? The same concept applies to firms looking to sell. What is it about your firm that will catch a potential buyer's eye and encourage them to "tour" your firm?

In a buyer's market, it is especially critical that firms looking to sell have curb appeal. How can firms elevate their appeal and attract potential buyers? Let's take a closer look at several strategies.

Differentiate your firm

One way to catch the eye of potential buyers is through differentiation; highlighting what sets your firm apart from the competition. For instance, does your firm focus on a particular vertical or niche?

Firms that have identified niche markets not only enjoy a point of differentiation that could be attractive to a potential buyer, but, in addition, clients will pay a premium for services they believe are geared toward them.

If your firm already focuses on a specific accounting specialization or niche — that's great. However, be certain that your point of differentiation — whatever that may be — is well communicated and showcased.

"I think the biggest thing they need to do is really focus in on 'What is their specialty?' Differentiating themselves from the other hundreds of accounting firms that are a similar size in their area that may also be looking to sell. You need to figure out a way to differentiate yourself, even at that point," said Allen Stahl, Strategic Technology Manager at Thomson Reuters. "Usually, you start out by setting up your website to showcase your specialty areas — things that you know are going to make you look more presentable or are where you have a large level of industry knowledge are two of the key things that I've found are really helpful."

If your firm does not market to a particular niche, perhaps now is a good time to start. Taking a closer look at your current book of business and focusing on your passions can be a great way to begin. For example, perhaps your firm already works with several dental offices, or attorneys, or real estate professionals.

Move beyond compliance

It's no secret that rearview mirror accounting is swiftly falling by the wayside given increased client demands, the commoditization of tax preparation, and a complex regulatory and legislative landscape. To stay relevant in this rapidly shifting environment, a growing number of firms are moving beyond compliance in favor of **higher value, higher margin advisory services**.

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Such a shift not only helps firms strengthen client loyalty and enjoy a more consistent revenue stream but also helps firms become more attractive to potential buyers, whose interest in acquiring solely compliance-based practices appears to be waning. In looking at the numbers, it is easy to understand why.

Shifting the conversation away from revenues and into the weeds of margins is a good way to help prospective buyers think about your firm differently.

Consider this: research from the **2023 State of the Tax professionals Report** from Thomson Reuters® Institute showed that 93% of survey respondents said their clients are now looking for some form of advisory services. As for what sort of business advice clients are seeking, 91% said tax strategy was the service clients requested most, followed by business consulting (73%), financial planning (63%), decision-making support (46%), and HR/organizational issues (30%).

"One of the areas that I've found a lot of firms are trying to get into is advisory... but if you can showcase to what degree of advisory your firm is into. There are so many different levels of advisory and there's always this need for a technology advisory partner. If you have some form of technology advice that you can give, or that you participate in with your clients, then it adds an additional layer to what is going to make you more valuable because everybody is looking to get that edge up in the advisory world," Stahl advised.

This does not mean, however, that all solely compliance-based firms looking to sell should immediately pivot and begin offering clients strategic advisory services. It depends on when the firm is looking to sell.

If a firm is looking to sell in a year or more, transitioning to higher value, higher margin advisory services can certainly make the firm more attractive to potential buyers.

On the other hand, firms that are not currently providing clients advisory services and are looking to sell now may want to, instead, turn this factor into an attractive selling point. How? By positioning it in a way that highlights the fact that there's untapped, organic growth potential within the existing client base.

Think beyond pure revenue

Firms looking to sell may want to reconsider how they're talking about the sell and marketing to prospective buyers. What does this mean? Think beyond pure revenue and focus on other metrics.

If firms focused just on revenues alone, they would all look pretty similar on paper. Shifting the conversation away from revenues and into the weeds of margins is a good way to help prospective buyers think about your firm differently. If you can showcase that your profit margins are high and you are doing more with less resources, this could also bode well as you look to market your firm differently," said Stahl.

Added Stahl, "How well you market your firm and help shift the focus from revenues to other areas of how your business operates can be tremendous eye openers for potential buyers."

Reevaluate outdated technology

It is important for firms looking to sell to evaluate their current business practices and, if necessary, implement more efficient operating procedures prior to being evaluated by a potential buyer. This may involve investments in modernizing the firm's tech stack and migrating to **cloud-native solutions**.

As noted in a **2021 article from the Journal of Accountancy**, "Buyers are wary of firms that aren't paperless, aren't on the cloud, or don't have remote-working technology that runs smoothly. They often have these technologies already in place and don't want to go through the hassle of setting it up again."

Obviously, it's not advisable that a firm be in the midst of a technology revamp when being evaluated by a potential buyer. Plus, firms want their books to look good to prospective buyers and those hoping to immediately sell may be hesitant to invest money in implementing new technology. However, those firms looking to sell in a year or more should consider **modernizing legacy systems** to boost appeal.

As Stahl explains, "I have heard time and time again that the cost of change is high for accounting firms. Updating your technology can be tough on not only the budget but the staff as well. Having up-to-date technology can be extremely helpful as it lets the prospective buyers know that your firm has weathered change well and come out the other end successfully. An updated tech stack also benefits the acquiring firm as it typically allows for easier ways of migrating data to and from new systems."

Looking to buy? Ensure your firm is ready

To help ensure success, a firm should do all that it can to learn about the company culture of a firm it is looking to acquire and ensure that both cultures will mesh.

The decision to acquire or merge a firm is not one to be taken lightly. As mentioned earlier, M&As can be easily mismanaged and without proper due diligence, a clear strategy, and open communication, the desired results of an M&A can be difficult to achieve.

When looking to make an acquisition, one of the first things firms must do is have a clear understanding of why such a move makes sense. What are they solving for and why? Firms that begin their M&A journey with a clear understanding of their goals and vision are better poised for success. That being said, understanding the "why" is just one of several factors that a firm must consider when looking to buy. Let's take a closer look.

Evaluate corporate cultures

It is imperative that firms not underestimate the importance of corporate culture. Bringing together two groups of people that have different ways of working and different personalities can prove challenging, to say the least. A failure to recognize cultural differences when assessing a potential deal can be detrimental.

As noted in the KPMG report, **Talent flight: Overlooked risks during M&A**, "Culture is almost always a key to integration success, but its intangible nature makes it difficult to account for during due diligence and integration. KPMG research shows that when M&A deals fail to meet targets, the most likely reason by far is a lack of buy-in among execution teams across the organization."

To help ensure success, a firm should do all that it can to learn about the company culture of a firm it is looking to acquire and ensure that both cultures will mesh. It is also important to recognize that, during a time of transition, a change in company culture will likely occur.

In fact, Culture Amp, an employee experience platform, suggested that there are three common ways to begin developing a company culture post-M&A:

- Choose one culture to be carried on
- Create a new culture that combines the best from both companies
- Create a completely new culture

Regardless of which path a firm chooses, establishing a good communication plan before the deal is finalized, and carrying that plan on throughout the process, is critical. As noted by Culture Amp, firms may also want to conduct a post-M&A employee survey as another way to keep the lines of communication open and to demonstrate to staff that their feedback is important.

Where will people fit in?

In some firms, especially smaller firms, employees wear many hats. They might be doing tax and accounting work; they might be doing tax, accounting, and some admin work; they might be doing some assurance work with audits; or they might just be doing it all. This differs from larger firms, where employees might be focused on a particular service line. Given this, firms need to figure out where people are going to fit within the new organization.

"People are [often] wearing lots of different hats at the firm so understanding whether or not there's a potential opportunity to bridge them into your current processes with what they are doing now or take a little bit of a different approach and ensure that you are being mindful that too much change can really become a problem," said Stahl. "Because change management has its own impact on the amount of people who are willing to stick through that entire buying and acquiring process."

Navigate change management

Nothing will send shockwaves like telling staff that their firm is about to be acquired or it will be acquiring another practice. They may immediately begin to wonder if their job is at risk and stress over what other changes may be in store. That's why it is important to effectively navigate change management.

Keeping staff engaged and immersed in the changes will help them better understand why the changes are taking place while arming them with the knowledge to contribute and help the united firm on its path to success. Failure to do so means that people may become disgruntled, lose focus, or simply leave their job all together to work for another practice.

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"If you can come into an acquisition and bring to the table the benefits that both sides are going to gain, the employee and staff-level folks will respect that transparency," said Stahl. "If you can share that prior to really changing anything then they can gain a better understanding of how their lives might be easier or better. Just bridging that gap and setting the right expectation is hugely instrumental in the front of making that transition a success."

As outlined in an **article from Foley & Lardner LLP**, there are specific strategies that can help to ensure a successful integration, including:

- **Cultural due diligence:** When you are conducting your due diligence, you should also conduct a thorough cultural assessment. This can help to identify potential challenges and opportunities and should inform decision-making throughout the integration process.
- **Leadership alignment:** Make sure you have an open dialogue and collaboration between leaders from both organizations from the start. By doing this, you can align strategic objectives, values, and management styles. Encourage leaders to act as role models for cultural integration and openly communicate the benefits of the merger to employees.
- **Communication and employee engagement:** During a merger or acquisition, communication with employees is key. Without it, rumors start, and panic can set in. Develop a robust communication plan that keeps employees informed about integration progress, addresses concerns, and highlights the shared vision and values. Encourage employee participation in cross-functional teams and integration initiatives to foster collaboration and a sense of ownership.
- **Cultural integration roadmap:** Create a structured integration plan that outlines specific steps and milestones for cultural integration. This roadmap should include activities such as cultural training, cross-cultural workshops, and initiatives that promote cultural exchange and understanding.

It is also important to keep in mind that the firm being acquired may currently be under several software licensing agreements, and those agreements are likely contracted out for a certain period of time.

The technology factor

When looking to acquire a firm, effective due diligence must include evaluating the technology of the target firm and ensuring technology alignment.

In Stahl's previous role working with the top 100 accounting firms, he witnessed many mergers that struggled due to lack of upfront involvement from the technology teams providing realistic expectations to the rest of the firm as to when and how quickly their technology softwares would be joined together.

For starters, it's important to keep in mind that technology conversions take time. This could be anywhere from three months to a year. Too often firms underestimate the amount of time it will take, so setting expectations and allowing as much time as possible to make a conversion successful will prove beneficial.

"Everyone wants their data to be converted yesterday and that's just not realistic. And so you have to sit back and set some better expectations so that you give yourself time to work through whatever kinks there are because every software has a different way of getting at the data and it's never easy," said Stahl. "What you can hope for is that the technology that you're having come out of your acquiring firm has an easy way of exporting the data into whatever other tools. If you can get the data into some form, Excel format or original native data formats, then you are in a way better position than if your system has a proprietary code-based extract that doesn't allow you get it into any of those formats."

Stahl, who noted that ironing out workflow processes can often prove to be the most challenging and time-consuming aspect, said firms may want to consider taking a phased approach to technology conversions, especially given the various contending deadlines that firms face (i.e., tax deadlines, audit deadlines, etc.).

It is also important to keep in mind that the firm being acquired may currently be under several software licensing agreements, and those agreements are likely contracted out for a certain period of time. Knowing and understanding how long those agreements are in place for will help the acquiring firm better understand when they can successfully convert, and it can help avoid potential overlaps with respect to their own licenses and the doubling of licensing fees.

Conclusion

In today's business environment, it is perhaps more important than ever that firms do their due diligence, develop a clear strategy, and keep the lines of communication open to help ensure a successful M&A.

This involves making sure that the two firms are a good strategic fit, understanding the corporate cultures of both practices, navigating change management, and ensuring technology alignment.

The good news is that firms don't have to embark on their M&A journey alone. By turning to a trusted solutions provider like **Thomson Reuters**, who can assist with technology conversions and process consulting to improve firm efficiencies, firms on both sides of the M&A equation can be confident they are on the path to success.

Recommended products

Practice Forward

Grow your accounting practice and become a next-generation firm with high-value advisory services. Thomson Reuters **Practice Forward** allows you to take a critical look at your operations and create the big-picture strategy you need to drive your firm's profitability and success.

SurePrep

This **1040 automation technology** is widely used in the market today for both staff collaboration with clients, data gathering, OCR, client portals, and more. This up-to-date technology lends itself to being consider tax agnostic meaning it will help any firms acquisition go much smoother while keeping the staff processes the same.

Cloud Audit Suite

The preferred end-to-end continuum of AI-enabled audit applications, the Thomson Reuters **Cloud Audit Suite** enables real-time digital collaboration between audit teams and clients.

Tax and Accounting APIs

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Professional Services

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The world of mergers and acquisitions is a complex one, where strategic planning and effective communication play pivotal roles in determining success. As businesses continue to evolve, M&A activities will remain a key driver of growth and transformation. Whether you are a large tax and accounting firm looking to expand your reach or a smaller practice exploring opportunities, the lessons shared in our white paper emphasize the importance of meticulous planning and a holistic approach.

Don't miss this chance to gain a deeper understanding of how to position your firm for sustainable growth and success in the ever-changing landscape of the accounting industry. Click below to learn more and unlock the potential of your M&A endeavors:

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