GROWTH STRATEGIES:

MANAGING GROWTH FOR SUCCESSION

INTRODUCTION

Every firm should be developed with view to the ongoing succession and ultimate sale of the business. The great thing about doing this is that you build a strong and profitable business from day one. And when the time comes for you to move on, then you have an asset that is attractive in the market and one for which there should be strong demand.

There are approximately 9,000 public practice firms in Australia, and of these 83% are represented by sole practitioners and two partner firms. There are a large number of small practices delivering similar services to a similar client base. These firms are typical of small business in Australia.

This guide has been designed to provide you with some of the practical tools that will assist you to plan and position your practice so that it is attractive in the marketplace, to have organic growth, and to manage your succession. It is particularly focused on small and medium size practices, although the fundamentals hold true for all.

GROWTH STRATEGIES

It is important to prepare your practice for succession. The better your preparation the better the outcome you should achieve and the smoother the transition. Preparing your practice for succession may take several years, so the planning phase is quite important. Planned succession will always outperform succession as an event. If you do little planning and simply put your practice on to the market then it is likely that you will achieve a lesser outcome than may have been possible.

The main reason why your succession preparation may take several years is to allow sufficient time to enhance the performance and appearance of your practice. One of your objectives with your succession planning is to maximise the financial outcome in the succession. Over time there will be an increase in the number of practices and fee parcels coming on to the market. This being the case, buyers will gravitate to the better quality practices and better pricing will be achieved by the practices who are meeting the performance expectations of the market. It is important to know what those performance expectations are and then to be able to groom your practice as much as possible to meet these expectations. Once you have your numbers right, then you need time – time to prove that the numbers are established and sustainable, rather than a one-year aberration. In most cases a buyer will want to look at performance figures for not less than three years. The better the picture you can paint, the better the outcome you will achieve.

Under performance in key areas of your practice causes succession roadblocks.

These will be the areas a buyer looks at closely to decide whether or not your practice is right for them. Increasingly the market is being educated on what to look for. The public practice business model is a relatively simple one. This does not mean being in public practice is easy but the things that differentiate a strong practice from a weaker one are reasonably easy to identify and measure.

This means that buyers will be looking for key characteristics in a practice. Much of this revolves around the areas of:

- profitability
- liquidity
- efficiency
- growth.

Key influencers of this will be:

- the quality of your client base
- the strength of your systems and procedures
- the quality of your staff
- the depth and breadth of your service range.

Get these areas right and not only are you in a strong position to negotiate your price, but equally importantly you have removed some of the roadblocks that could otherwise exist in a buying decision.

Most practices have areas of under-performance. In some cases, you may be working to improve these, in other cases you simply accept them as being tolerable.

Getting succession ready is about understanding market expectations and then as much as possible positioning your practice so that it rates well in the key areas.

In planning, be mindful that the accounting business model is going through a period of change. A clear strategy for your practice is important. There is no single strategy that is the right one for all practices. Rather you need to have a clear plan of what you want your practice to be and then align your market and resources to your plan.

What the market expects – know the benchmarks

Key to removing any performance roadblocks is to know what the market expects. There have been a reasonable number of benchmarking studies undertaken on the accounting profession. Much of this information is public knowledge or easily accessed with a little research. Given the level of fragmentation in the accounting profession you should be aiming to be well above the average. There is a marked difference in the performance of top quartile firms and the rest. If you are looking to benchmark your performance, always measure against the top quartile. As the number of firms experiencing succession events increases, performance will separate those that are the most attractive opportunities in the market.

The rest of this module is devoted to describing in detail the key areas outlined above that your practice will be assessed on, the benchmarks that currently exist and which tend separate the better performers.

PROFITABILITY

Ask any accountant how they are and you'll generally receive a response that says something about them "being busy", but is this profitable?

Time is our most limited resource and all of us share the desire to be using our time profitably. However, sometimes we get so involved in trying to keep up with client demands that we end up either:

- accepting work we don't have the capacity for
- doing types of work we shouldn't
- rushing to meet deadlines and being inefficient in doing so
- not charging enough for our time
- missing out on leveraging opportunities.

Example:

David is a busy sole practitioner. He is committed to growing his practice as quickly as possible. The practice is busy but David's view is that there is always room for more clients. He never says no to an opportunity for a new client. A group of connected small businesses approach David to act for them to assist with completion of their financial statements on a quarterly basis, end of year accounts and taxation work. David readily accepts the engagement and agrees a fixed fee. When the work starts to come in it is evident that it is poorly organised, source records are incomplete and the clients are always overdue in meeting their compliance deadlines. David's staff don't enjoy doing the work and the clients are resistant to any change. Despite this, he perseveres with the client group because they represent a meaningful fee for the practice. After six months he reviews time spent on the client and realises that he is losing money on the job. His top line revenue has grown but he is sacrificing bottom line profit.

Most of us offer the public a variety of services of differing profitability. Do you know your most profitable types of work and what your ideal mix is?

The impact of poor profitability should be frightening enough to spur us all into taking immediate action to ensure it doesn't happen to us. Poor profitability will eventually negatively impact everything about your practice. You end up in a downward spiral where things just seem to get worse. Partners and staff often approach the problem by trying to spend even more time at work doing more of the same work which may be only compounding the problem. Funds for new technology and other resources that may assist are limited. Partner, staff morale and motivation suffer, people get sick or leave. Not a pretty scenario.

As accountants, we are very good at quickly determining whether our client's businesses are profitable. However, like many other types of professions some accountants are surprisingly tardy in analysing and keeping on top of their own practice profitability. The golden rule to improving your profitability is that first you must know what your current profitability level is and what drives it.

Driving your practice as a business – the revenue line

Focusing on the business of accounting should never be in conflict with your profession as an accountant. Building a successful business is an essential ingredient to a public practice. At the same time, we recognise that the business focus can be a challenge for a practitioner who is highly focused on client issues. There is a tension between the outworking of your profession, client management and business self-interest. Get the balance right though (and it is possible) and you have a recipe for success.

Let's explore the business development of an accounting practice and take a focus on the revenue line.

Firstly, why the revenue line?

There are a number of fundamental reasons. Certainly, it is a natural place to start and one that has an interest for most of us. Beyond that, however, there is a more compelling reason. And that is for most practices, if they are struggling to achieve bottom line performance, it is because of under-performance at the revenue line. Most accountants tend to get their costs right, although at times we are 'tighter' than we should be from a business perspective. Many firms fail however to get the revenue balance right.

The majority of firms today still operate on a time/cost basis. It has been drilled into us from years past and we are all about hours spent, hours charged. Some firms have broken this shackle and moved to concepts of value billing, premium fees or other models; however, they are in the minority. And often, where it is adopted, it may only be for a part of their work. As a consequence, our revenue results are often driven out of productive capacity (read number of people times their available hours), the charge rates applied, and our workflow efficiency level (read productivity of individuals against available chargeable hours). Mathematically simple, but it can give you a headache working through all of the permutations.

Then if we don't get it right we go through the introspection of analysis around workflow management, productivity levels, staff mix, staff skills, write off levels, client mix etc. Now it is possible to get it right, however, it is a constant vigil and it will often take your focus away from the bigger picture and the bigger opportunity – managing client relationships and being available to take on work opportunities that occur.

There is a wide range of variables across practices and client bases regarding revenue issues for accounting firms.

1. Compliance services delivered on a time cost basis will always create a limiting factor

This is a simple reality for small/medium accounting firms. Basic compliance services are becoming a commodity and there will be continuing downward pressure on price in this area. If this is the extent of your offering, then you will be under ongoing price pressure. Add to this price pressure the challenge of managing workflow throughout the year, staff efficiency on jobs, and simply the unexpected. In this environment the chances of getting your revenue line right is under enormous pressure. Basic compliance services will always be a part of the majority of firms – the issue is, is it the only part?

2. The ability to deliver some specialist services

Irrespective of whether you are a small or large firm there should be scope to deliver some level of specialist service. Being solely a 'GP' practice means no premium in pricing and you are reduced then to playing the numbers game. Take a look at GPs in the medical profession. The only ones who achieve a really healthy return are those with a very high patient throughput. By adding at least one specialist area you open the scope to achieve some revenue premium. Specialisations aren't hard to develop and the opportunities are almost limitless. CGT, GST, valuations, business analytics and advisory, estate planning, succession planning and due diligence work are some examples. Even in a sole practitioner situation there is opportunity to do some of this, particularly with succession planning and estate planning. The baby boomer generational bubble that is flowing through will create enormous opportunities over the next ten years in those two areas. When you do, make sure that you price it correctly. This doesn't get you away from the time/cost framework. It simply puts a better return rate in place.

3. Consider passive income stream opportunities

When you work on a time/cost basis you will only be paid for the hours you work. Add to this a passive income stream and you open up enormous possibilities. Financial planning, risk protection and mortgage facilitation are all services that your clients need. In one area or another over half of the profession already provides these services to their clients. Generally, these areas have the potential to create passive revenue streams. And, the real key is that these are services your clients need and if you were able to provide them in a responsible way then it is likely that they would prefer to 'buy' from you rather than establish another relationship. It is a very practical value add and a way of enhancing the client relationship. Clearly disclosure and management of process are important here. This is an area that is in eye of the regulators at the moment. The Government's response to the Cooper report and the Ripoll report is likely to cause major changes in this area. Subject to these changes, financial services delivered professionally and competently by accountants creates a genuine win/win situation.

4. Productise some of your services

A number of firms have moved into broader areas of service delivery to their clients. This includes areas such as IT, human resources, accounts receivable management, and data processing. Where these can be put into a product format so that the client is buying a 'package' rather than simply time, there is an opportunity to create some revenue leverage. Which products are right for you will depend to some extent on your client base and your areas of expertise or interest.

5. Look closely at your charge rate

Most practitioners tend to under charge rather than over charge. If you are looking to reduce your stress levels and 'win' back some of the time that seems to get consumed in your practice, then start to increase your charge rates. Be prepared to lose some business – particularly the unprofitable, the slow payers and the problem clients. They don't add to your business. They simply cause frustrations.

Also look at how you set your charge rates. Historically the profession has set their charge rates either on a cost driven model i.e. a multiple of direct labour cost or they have attempted to the model the market. Both of these methods can work but they also have their limitations. Be prepared to look at value billing and premium pricing models. It is an interesting fact that the majority of firms who score in the top quartile of benchmark studies employ one of these methods for at least a part of their work.

So, there is the top five ways to improve your revenue line. Ask yourself the question – if you could achieve a 10% increase in your revenue line without any increase in your cost structure what would that mean to your business, your bank account and your lifestyle? In the vast majority of cases 10% should be readily achievable.

A more recent area that has emerged in the succession of accounting firms is the question being asked – what does it take to generate the profitability of the firm? The number of hours worked by principals and partners varies significantly. Increasingly the market expects that the firm can deliver reasonable performance results with the partners working not more than 40-50 hours per week. Whilst in some firms it may be common for the partners to work longer hours this should not be a requirement to achieve benchmark performance.

Diagnostic checklist to assess your profitability performance

Measurement	Method of calculation	Benchmark objective	Your result
Revenue per FTE	Gross fees divided by number of full time equivalent personnel, including partners	Aim for > $140K	
Profit after partner salary %	Net operating profit after market-based partner salaries, divided by gross fees	A profit return of 20% on gross revenues is achievable. Where profitability falls below 10% you are likely to have trouble funding growth or seasonal variations	
Revenue efficiency	Measurement of time charged against budget. For staff with no administrative responsibilities you should be looking for a 75-80% efficiency rate on a standard week. The efficiency rate will be scaled down where there are administrative duties	Can be measured on a firm productivity basis, based on the budget you have created. All employees should have productivity budgets	

Key costs to revenue %	Labour cost (including allowance for principal or partners salary) to gross revenue Overhead costs to gross revenue	50-58% 22-28%	
Average fee per client	Gross fees divided by total number of client groups	Will vary depending on your market segment. An average below $1,000 will place pressures on you. Ideal position > $3k	
Average fee per tax return	Gross fees divided by number of tax returns lodged	Will vary based on the practice and work type being undertaken. The objective is to drive the average number upwards	
Fee structure partner down	Should be calculated on a partner down basis, using the partner rate as a benchmark from which to calculate a charge rate for other employees	Will vary based on location, market segment and type of work undertaken. As a guide, a manager could be 80% of the partner rate and a senior 60%	
Hours worked by principals and partners	Average working hours required of principals per week	Average hours within 40-50 hours per week	

Download a Profit Improvement Workpaper.

Profit strategies checklist to address under performance

Much of the focus here needs to be at the revenue line or improving practice efficiency. Most accounting practices do not have issues with excess operating costs. Cost control is normally in place. It is more likely that profit is being influenced by a lack of revenue or workflow management efficiency. The following list represents the key strategies most likely to increase practice profitability. In a number of cases there is a range of ways to implement these strategies.

Strategy	Expected impact	Timeframe for effect	Other impacts
Increase charge rates and review charge rate setting model	Increase should flow straight through to the bottom line	Immediate	May cause some resistance from fee sensitive clients. The majority of clients have some fee elasticity
Cross sell more services within your client base	Should increase average revenue per client, with profit return reasonably constant	Normally 3-6 months to see flow through effect	Will require more resources and an active sales process

Introduce new premium services e.g. financial planning, succession planning	Existing client base should provide your initial market. May also attract some new clients. Should increase revenue with higher profit margin from the premium service	Normally 6-12 months to see flow through effect	Will require additional skill sets, more resources and an active sales process
Reduce write off levels	Will increase your revenue capacity, either allowing you to take on more work or to complete the same amount of work with fewer people	Immediate impact on capacity. Will normally take 3-6 months to realise flow through results	Should reduce workflow frustration and improve overall practice morale
Acquire new target clients	Your target clients should be the most profitable for your practice. New target clients should enhance your client mix and increase practice profitability	Normally within 3 months of new client acquisition	Target clients tend to buy more services and provide more interesting work
Refine your client base	Getting rid of problem clients will improve overall practice efficiency and open up capacity to take on new clients or do more for your better clients	Normally 6-12 months to see flow through effect	Will reduce frustration levels within the practice that are caused by problem clients
Increase the marketing focus of your practice. Professionals need to sell	A stronger focus on marketing will produce more work, leading to increased revenues and profits	Normally within 3 months	May require some marketing budget. Will increase the energy of the practice

Changing the profit profile of your firm

Improving your profitability does not need to come from a single radical change in your practice. Change can come in small steps, with a low impact on clients and minimal intrusion into the operations of the practice. Consider the impact on profitability if you:

- increased your fees by 3%
- reduced your write-off level by 2%
- cross-sold one additional service to 10% of your clients.

The targets set here are quite modest. They do, however, provide a stepping stone to enhanced profitability.

LIQUIDITY

Profitability is great in any business. But talk to any insolvency practitioner and they'll give you some tragic war stories of profitable businesses that fell over because they ran out of cash. So while it is essential for your long-term well-being that your business remains at a good level of profitability, it is also critical that you are managing your short-term liquidity to ensure you can stay in business.

Your combined debtors and work in progress represent the 'lock up' of the firm. This is an area that the profession has focused on over recent years. The better performing firms now manage their lock up in less than 70 days on average.

Get the work, do the work, bill the work and collect the money. Sounds simple doesn't it, but sometimes it just doesn't happen as easily as this.

Collecting fees is an area that many practices struggle with. Debtors can get out of control and industry benchmarks indicate that average debtors within the profession represent 60 to 90 days of annual fees. Not a good advertisement for the people who advise business.

Collecting the money is an area that some practices struggle with and it is due in part to the close relationship we have with our clients and the difficulty we have in asking for money from the client. At times, the client may also exploit this relationship and when funds are tight the accountant is one of the last to be paid. I don't think you would disagree if I suggest the accountant should be the first to be paid given our role as trusted business advisor.

Example:

Roberto and Josh, university friends, both go into practice around the same time, establishing sole practitioner firms. Over a three-year period they both grow their fee base to $500,000. Roberto takes a fairly relaxed approach with client payments and at the end of the three years his average debtor days is 70 days i.e. just over $105,000 (GST inclusive). Josh has adopted a stricter debtor management approach and his average debtor days are 40 i.e. just over $60,000 (GST inclusive). Roberto and Josh compare notes on how their practices are performing. For Roberto, the higher debtor days has meant:

- *he has needed bank funding for the additional $45,000 working capital*
- *he is absorbing the interest cost against his profits*
- *he has had a higher level of bad debts than Josh*
- *as his practice is growing his clients expect continuity of these trading terms, which will place further pressure on his working capital.*

Introducing a credit policy immediately within your practice may be difficult and unpopular for a number of reasons. Firstly, how do you approach your large clients who are unable to pay on your new credit terms, but who you cannot afford to lose as a client? Secondly, how do you transition your clients (who are accustomed to pay between 60-90 days) to meeting your new credit terms? We suggest the new credit policy be implemented in a staged process.

1. For those clients paying on 90-day terms, negotiate them back to 60 days.
2. For clients who have always paid 60 days, these should be brought back to 30 days.
3. Continue this staged process until all clients are paying within your new trading terms.
4. Communicate the credit policy to existing clients at every opportunity you can, such as newsletters, correspondence where appropriate or to the extent of re-issuing an engagement letter.

For new clients a credit policy is not difficult to introduce, as it will be explained in the engagement letter. Or, preferably, if you can outline your trading terms as early as possible, the initial meeting would be a great opportunity to do this. By setting clear expectations at the start you give yourself the very best opportunity to get client payment behaviour right from the beginning. It is always harder to change existing habits than to establish new ones.

Equally important is your management of work in progress. You should be managing your work so that it is billed progressively or on completion of work segments. Regular billing will drive down your work in progress and improve your liquidity position.

Diagnostic checklist to assess your liquidity performance

Measurement	Method of calculation	Benchmark objective	Your result
Liquidity debtors days	Debtors outstanding at month end dividend by annual revenue, then multiplied by 365	Average for the profession 60 days. You should be aiming for less than 45 days	
Liquidity WIP days	Work in progress at month end divided by annual revenue, then multiplied by 365	Again, average for the profession is 60 days. You should be aiming for less than 30 days	

Liquidity strategies checklist to address under performance

Improving practice liquidity normally comes through an integrated approach. Whilst one strategy in isolation will have some effect it is the implementation of a range of strategies that will produce optimal results. The following list represents the key strategies most likely to increase practice liquidity. In a number of cases there is a range of ways to implement these strategies.

Strategy	Expected impact	Timeframe for effect	Other impacts
Explain your payment terms in your engagement letter	Establishes expectations with client from commencement	Should flow on from initial billing period	May require a follow up process to implement the payment terms required
Quantify fees in advance	Removes uncertainty and allows clients to raise the fee issue in advance of work being undertaken	Should reduce any delay in payment due to a query on the quantum of the bill	A risk of write-off if you under quote the job
Bill regularly	Progress billing will lower your WIP exposure and accelerate your cash cycle	Should show within 90 days	Requires up-to-date WIP information and discipline to bill work out a monthly basis
Bill as near as possible to the conclusion of work segment	Allows clients to relate the bill to the work completed	Normally 30-60 days	Standard procedure should be to bill work out at conclusion or agreed milestone events
Where practical present the account to the client	A percentage of clients will pay immediately	Within 30 days	Typically reduces debtor days by a minimum 15 days
Provide payment alternatives e.g. credit card, EFT etc.	Greater flexibility in payment methods will accelerate the payment cycle	30-60 days	Requires alternate payment facilities to be in place

Consider fixed fees for some work	Clients often relate better to packaged services for a set price. Normally tied to a regular monthly or quarterly payment	30-60 days	Need to develop skills in quoting on a package of services. Generally needs to be accompanied by a strong engagement letter
Invoices should state payment terms and provide EFT details	Will remind clients of payment terms and encourage EFT payment	30-60 days	EFT payment is normally the lowest cost method of managing payments
Follow up debts systematically and frequently	Slow paying clients will pay faster when there is a systematic follow up process	Within 90 days	Will identify and reduce potential bad debts
Consider the fee issue in your client selection criteria	Some potential clients may be rejected on the basis of the payment risk	Progressive	Should result in a better quality client base

Below are procedures to implement a credit policy within your practice.

Credit policy

The first step is to have a documented credit policy. The credit policy will include trading terms and a follow up procedure when payment has not been received within agreed trading terms. A simple rule is to have some form of follow up every seven days. If your trading terms are 14 days from end of month then the follow up procedure starts at 21 days after the end of the month. We suggest the following procedure:

1. Send a letter to all clients who have not paid within 21 days explaining your terms of trade and asking for payment within seven days. Ask that if there are any problems with the account they should contact the credit manager immediately.
2. If payment has not been received by the 28th day, the client should be contacted by phone. If the first letter failed to produce results, it is this call that will generate action. Make notes of what was agreed with the client.
3. From your phone call with the client, if payment was agreed within seven days and had not been received by the following week, then a final letter should be sent requesting immediate payment or the account will be sent to the debt collectors. This letter generally produces a result.
4. The final step is to send the account to the debt collector if there has been no response from the client. The partner responsible for the client is advised first in case there are reasons why the client should not be put in the hands of the debt collection agency. Our experience is that clients who reach this stage are those whom we don’t want to retain and will likely leave after the debt collector steps in.

Some tips to assist in the collection process:

Repayment plans

If the client on the phone says they are having a cash flow problem, then agree on a repayment plan. Ask for weekly payments until the debt is repaid over say a period of one to three months. Send a letter to the client confirming the arrangement and closely monitor payments.

Financing

If the debt is relatively large (say over $10,000), the amount could be financed by financial institutions who specialise in this area of funding professional fees. You receive the funds up front and the client repays the debt over a period of no more than 10 months with interest and an administration charge. The downside to this arrangement is the accountant guarantees the repayment of the amount as no security is taken by the finance institution. This means if the client defaults, you take over repayment of the debt.

Fixed fees

Setting up fixed fee arrangements with clients, having agreed amounts automatically credited to your bank account every month, improves cash flow and saves the administration time of collecting money. The key to fixed fee arrangements is to ensure that you have clear terms on what the agreed fee covers. Where you are not clear on this you run the risk that the client will expect all and every piece of work you complete for them during a year to be within the fixed fee agreement. Where you are using fixed fees, agree in writing the work that is covered. Be specific and state in the engagement letter that you will identify any work that is not covered under the fee agreement in advance of commencing it. Then make sure that you do.

Communicate the policy

A policy is not worth much if no one is aware of it. The policy should be communicated as follows.

- The engagement letter is an important document to communicate your trading terms as the client signs the letter agreeing to the terms.
- The trading terms should be clearly indicated on every invoice and statement sent to the client. Also be clear if the trading terms are from the invoice date or end of the month. Even better, state a date when the invoice is due and payable.
- Don't forget your team. The people responsible for following up clients should be crystal clear on the credit policy. Similarly your professional team must understand the firm's credit policy. I would even ask the professional team to check if there are any amount owing by the client greater than 30 days prior to commencing new work for that client. If the client is finding it difficult paying existing accounts, they are unlikely to afford any new work. Partner clearance is required in cases like this.
- The credit policy should be communicated to clients during all follow up letters and phone calls.

Implement the policy

This is the most difficult step. It is important to select the right people for the job. Your administration team will most likely do the follow up and reporting to the administration partner(s). The follow up and reporting must be weekly. The types of reports provided to the partner include:

- a debtors trial balance
- a schedule of clients who have received follow up phone calls and their response
- a schedule of clients who have been sent a second letter
- a schedule of clients who will be put in the hands of the debt collection agency
- total collections for the week and month compared to budget.

The important point here is to have weekly meetings of less than one hour to ensure the credit policy is being implemented.

The credit policy explained above should ensure your firm is the first to be paid by your clients. Alternatively, those clients who have a problem with paying for your services within agreed trading terms are likely to leave.

Download a liquidity improvement workpaper.

GROWTH

If you are not growing, then you'll be going backwards. All accountancy practices need new work, if only to replace old work that may be declining for very good reasons. If you have an ageing client base, then it is likely that over time some of your clients will need fewer services. Even where you retain the client the fee profile may reduce.

The market also expects to see revenue growth. An emerging trend in the profession is the challenge of being able to deliver organic growth on a systemic basis. Much of the reported growth in firms is growth by acquisition. There is nothing wrong with this and it can strategically make sense. However, it is no substitute for organic growth. Firms that can demonstrate an ability to deliver organic growth on a systemic basis are far more valuable. These firms have inherent value built into their future. They also present a lower risk profile in the event of loss of clients or work.

As a guide growth should be not less than 10% per annum. This should be a mix of both price growth and real growth. But all growth is not good - especially unplanned, unexpected or haphazard growth. This type of growth can impose severe strains and pressures on a practice resulting in:

- reduced servicing of existing clients
- greater risk exposure from poor quality work
- potentially damaging your firm's reputation and negatively affecting your referral strategies
- overloading yourself and staff members resulting in reduced performance or, at worst, resignations
- greatly reduced efficiency and hence profitability
- increased strain on liquidity.

Like profitability, we need to know the numbers before we can hope to manage and improve them. Hence we need some simple and effective systems to record and monitor our growth. We also need to plan for growth, setting targets for what type and how much growth we want and how we intend to achieve this.

Different practices will need differing levels of growth at different stages in their life. In a stable practice only minimal growth may be needed. However, a practice with succession issues and looking to bring in younger owners to pay out the older exiting owners may have fairly high growth demands.

Long term sustainable growth requires comprehensive planning, good systems, focus and persistence by the principals of the practice.

Planning for growth

When you are planning the future growth of your practice you must remain pragmatic. Rush into business growth and you risk damaging your existing client base, reputation, and above all your bottom line.

So what elements should you be thinking about when planning for next year's growth and what are some common pitfalls of practices that grow too quickly?

What sort of growth?

The first issue you need to consider is which path of growth would best suit your firm and will most efficiently lead you to the outcome you wish to achieve. Will you seek expansion through attracting more clients to your firm or through encouraging a greater level of fees from your existing clients?

You could, of course, decide to do both, but each will require a different strategy.

Growth through increased clients

This must be a targeted approach and not just growth for growth's sake. Lots of people talk about client targeting, but few do it well.

Most importantly, you must sit down and identify your target client. Be specific. Are you looking to work with small businesses or is your practice wishing to expand into the larger end of town? Where are your ideal clients located? Are they in the same suburb as you or are they geographically diverse?

Specialisation might be the stream of growth for you. You might have built up considerable experience dealing with businesses in a particular sector and expanding further into this industry might be the most effective way to go. Alternatively, you might be experiencing a drop off in your industry of specialisation and may decide to market further afield.

In implementing a growth strategy, you should look closely at the external promotion of your firm. Are you going to take a shotgun approach or are you going to tackle it in a targeted way?

Targeted growth and having a target client profile will generally produce the most effective form of growth for your practice. It also allows you to refine your practice client base over time. The majority of firms have taken on clients over time who are probably not the ideal client for the firm. Taking an increasingly targeted approach to new clients allows you to improve your client mix over time. Clients that meet your target client profile will generally be:

- more profitable for the firm
- provide greater professional satisfaction
- deliver sustainable growth
- the best deployment of your resources.

Perhaps the most simple, but most forgotten technique, is to utilise your existing networks. Talk with your existing clients. Referrals are one of the most simple and effective ways to grow your client base. The majority of firms will say that client referrals produce the highest number of new clients, however, the majority of firms do not have an active client referral process in place. For most firms this is a passive outcome. Imagine what might happen if you took a more active approach to generating client referrals?

Client seminars are a great low-cost way to showcase your firm and the services you offer. In order to achieve the best results in attracting new business, your audience should be made up of a mix of clients and non-clients.

Growth through increased fees per clients

The first step with this growth strategy is to compare what services you are currently providing with what services your clients are actually using.

It might be that the particular services you are offering are no longer suitable for your target group. You might decide to expand a well-utilised area of your business, offering your clients additional value-added services. You might also decide to increase your service offerings, adding to your compliance capabilities with business consulting, financial planning or IT support.

Alternatively, your growth might be stunted by ignorance. Your existing clients might simply not be aware of all the services you offer. Make sure you continue to educate your clients along their own growth cycle as to the range of expertise and service you can provide. The simplest way to do this is to have an Area of Operation document detailing the services provided by your firm. Every accountant in your office should have a copy of this document and it should be standard procedure to walk your new clients through your service range.

Increasing your fees per client should also include a reasonable level of price growth. Don't get stuck in the rut of maintaining the same charges year in, year out. Your costs are increasing, so to should your prices. Where your fees are correctly set, then annual price growth of 3-4% will only keep pace with inflation.

Pitfalls of growing too quickly

So, you have decided how you are going to grow your practice but before you rush into things there are a few issues you must consider.

1. *Do you have the capacity to grow?*

Having identified your target client, it is important to determine whether you have the capacity to care for them. You don't want to find yourself in the situation where new clients are walking in the front door and existing clients are heading out the door.

This capacity has to be at the partner level. It is typically the most senior people who are the busiest in an accounting practice. These are the people who are under the pressure, often work the longest hours and sometimes simply don't have the time to do all the things they would like to do, let alone those that they should be doing. If this is the case in your firm, how can you expect to attract and service new clients? The key is to create capacity at the top level. You might decide to have at least one full time equivalent in excess of current requirements to allow sufficient time for managing client relationships. You should not waste this additional capacity but make use of it by driving the work vertically down your firm.

2. *Ensure quality control*

Make sure you don't get too busy too quickly. You must have systems in place to ensure the growth process is as smooth as possible. Make sure your procedures and working papers are in order. With growth comes a greater need for delegation and a heightened importance on systemised operation.

3. *Can you afford to grow?*

Do you have sufficient working capital to match your desired growth? Most practices can cope with growth from a profitability point of view, but many have problems in the liquidity area. Have you considered the time lag between taking on additional work and actually seeing the money in your bank account? Fees can be tied up for up to four months so your capital must be flexible enough to allow for this delay. You should also consider additional costs associated with staff increases and marketing efforts.

4. *Avoid discounting*

Perhaps the most ineffective growth strategy comes with offering discounted fees. Discounting for professional service is a lazy marketing strategy and one that is sure to come back and bite you. You may find yourself in a spiralling price war that you cannot afford to sustain. The client who comes to you on the basis of a discounted fee will leave you for the very same reason.

5. *Don't forget your existing clients*

It is important to ensure you have systems in place that allow you to keep in touch with existing clients. You might be working towards targeting a different end of the market, but you cannot afford to alienate existing clients in the short term. Keeping in contact might be as simple as distribution of a regular newsletter or a phone call.

Growing your practice

Implementing an effective growth strategy is now more important than ever before. Our baby boomers are middle-aged and with a typical practice's clients being plus or minus ten years in age of the practitioner, more and more clients will be approaching retirement or exit stage.

This fact can have a major impact on the ongoing value of your practice when looking at your succession planning or exiting of older partners. Hence targeting your growth efforts at the appropriate client age levels can be beneficial to the value of your practice.

Example:

Helen has been in practice for 25 years. She has a mature client base with the majority of her clients aged between 50 and 70 years of age. Over recent years she has noticed that a number of her clients have retired or have sold their business in anticipation of their retirement. Whilst her client numbers have remained reasonably stable her fee base has contracted as a number of her clients have reduced services needed. Helen realises that this trend is likely to continue and is keen to arrest the contraction in her fee base. Thinking about her client base and their emerging needs Helen upskills herself in estate planning strategies. She adds estate planning to her suite of services and starts to promote the availability of this service to her clients. Over a 12-month period she notices that an increasing number of her clients are seeking estate planning services and the fees from this work are now offsetting other fee losses. By understanding her client base and their changing needs, Helen has been able to position her practice to continue to assist those clients and in the process grow a sustainable revenue stream for the firm.

If you do not target your growth strategy well enough you risk filling up your client base with poor quality clients – those that cannot afford to pay, stress cases and those that are simply a drain on your resources.

It is crucial to understand the source of your desired growth. You must match your practice's needs with where you want your clients to come from. Don't let your firm get in to the position where they take on anyone. Ensure you have a clear definition of your target client and you will have a greater chance of avoiding inefficient management.

There is no definitive answer to practice growth. Time spent examining your practice's structure and projected goals are the only way to go. Make sure you have a strategic plan in place that is supported by a clear marketing plan.

Download a Growth improvement workpaper.

Diagnostic checklist to assess your performance

Measurement	Method of calculation	Benchmark objective	Your result
12 month moving average on fees	Immediate past 12 months gross fees divided by 12 and updated on a monthly basis to create a trend line	There is no absolute benchmark for this. The trend line should be consistent with your growth strategy. Generally, your growth trend should be in excess of 10% per annum	
Client turnover rate	Number of client attrition's divided by average client numbers for the year	There is no absolute benchmark here as it will depend on your strategic plan. Normally you would look for an attrition rate < 3%	
Client addition rate	Number of client additions divided by average client numbers for the year	There is no absolute benchmark. It will be depend on your growth strategy and the basis for that growth. Results should be consistent with your plan	

Growth strategies checklist to address under performance

Growth strategies can generally be separated between internal and external growth strategies. Most firms need to have a mix of internal and external strategies. You need to be developing new clients, but also maximising the value delivered to, and being received from, existing clients.

Strategy	Expected impact	Timeframe for effect	Other impacts
Identify the growth capacity within your firm	Develops an understanding of whether you can expect to achieve growth or whether you need to put additional capacity in place	Within 30 days	Will identify resource requirements
Increase your service range	Provides additional service areas for your existing clients to purchase	Will normally show results within 90 days of implementation	Increases in service range normally require additional resources
Increase client utilisation of existing services	Your existing clients will purchase additional services. Should increase average fee spend per client	Will normally show results within 90 days of implementation	Will require additional resources but cost of acquisition of business will decrease
Increase charge rates	Should grow revenue and profit line	Immediate	May cause some client sensitivity depending on the level of increase

Identify the characteristics of your target client and then focus on acquiring these types of clients	Should provide a greater focus on the type of client you would prefer to be working with	A longer-term strategy. Make take 1-2 years to see the impact	May cause you to categorise your clients and also identify existing clients who add little or no value to the firm
Have specific new client acquisition objectives e.g. we will acquire 5 new 'A' class clients over the next 6 weeks	Specific targets cause a much greater focus on achieving the outcome and marketing plans have to be more tightly developed	Normally 6-12 months	Should elevate the marketing focus of the firm
All partners and senior managers to actively cultivate professional networks	Should increase and produce a flow of referral work	Within 3-6 months of network being established	Likely to lead to referral of non-target as well as target clients

CLIENT MIX

The client mix of a practice will vary significantly depending on the nature of the practice. The typical general business services practice will have a client mix including:

- small to medium businesses
- contractors and self employed
- private individuals and investors
- non-profit organisations.

The majority of firms grow their client base at random. As clients are referred to or approach the firm they are taken on as clients. This often means that after a number of years the firm has a substantial client spread. This spread can be of assistance to the practice in reducing its risk exposure and providing a broad range of work that allows the firm to bring on and develop staff from junior to senior levels.

In the early years of a practice almost any client mix is manageable. As the practice matures, however, the client mix will have a significant impact on practice profitability and the ability of the practice to continue to grow. Risk positions begin to develop when you don't have control over your client mix and your client numbers increase with a heavy skewing of client numbers to lower end work. This can often be most easily identified by measuring the average fee per client of the practice. Where the number drops below $1000, this tends to indicate that the practice requires high volume throughput moving at the extreme to a factory production line.

High volume, low value work can be profitable. And certainly, there is no risk of client dependence by the practice. The most common problems caused by such work are:

- fees tend to be at a lower level and part of the market may be price sensitive
- the principal or partner will be stretched quite thinly across the client base
- typically resource capacity will experience seasonal peaks and lows
- ability to take on higher level clients with significant work and time demands is limited
- good quality staff will become bored by the lack of challenge from more complex work
- profitability is often at the lower end of the profit range.

The relationship between your client mix and the average fee per client is an important one. The average partner cannot manage much more than $1.5 million in fees. Certainly in larger firms there are partners who manage well in excess of this and even in some smaller firms you find cases of principals or partners who are managing well in excess of $1 million in fees. However, if we look at the main stream of small to medium size firms the average partner is managing between $400k and $900K in fees. As soon as you have identified your average fee per client you will be able to identify how many clients you can realistically manage. The typical partner will not be able to manage more than 250 clients. This number will be influenced by the average client fee.

As you look at your client mix, the more it is skewed towards a volume of lower end work – the lower the total value of fees you will be able to manage, and the less capacity you will have to take on larger assignments.

To assist in understanding and managing their client mix some firms categorise their clients as A, B, C or D grade clients. These ratings will be based on variables such as fees charged, size of the client, number of services consumed and satisfaction in working with clients. This type of system simply provides an easy to see picture of what the client mix looks like and the emerging trends.

The main objective with your client mix should be to be in control of it, and to understand the effect of the number of clients you manage and the average fee per client. With this information you can design your business strategy to pursue the client mix you are after, rather than simply accepting whatever comes.

Example:

Julie and Andrew are partners in a suburban accounting firm. Andrew specialises in business services and taxation work and Julie specialises in SMSF compliance and administration work. The partners have agreed to grow the firm through Andrew bringing on as many new business service clients as possible with the intent that Julie will care for their SMSF requirements. They expect that the majority of their clients will be SMEs and high net worth individuals. As the practice grows Andrew is introduced to a network of clients who work for the government and are keen property investors with rental property portfolios. The firm experiences significant growth through these new clients and they are taking up an increasing amount of Andrew's time. At year end, Julie and Andrew meet to review the progress of the firm. They notice that Andrew is under significant work pressure whereas Julie has seen growth in her business area almost stop. This drop in growth is matched to the reduction in the level of referral work that is coming from Andrew. Whilst not by design, they realise that the change in activity has not been consistent with their business strategy and has slowed the overall growth of the firm.

Download a Client mix improvement workpaper.

Diagnostic checklist to assess your performance

Test method	Method of calculation	Benchmark objective	Your result	Test indicators
Average fee per client	Divide gross fees of the practice by your total number of clients	Will vary depending on your market segment. An average below $1,000 will place pressures on you. Ideal position is > $3k		
Client dependence	Identify top 5 clients by fees and then calculate their fee as a percentage of total fees	No one client > 8% of gross fees and top 5 clients < 30% of gross fees		

Industry or sector dependence	Calculate client fees by industry or sector group as a percentage of gross fees	No one sector should represent more than 30% of gross fees		
Number of clients per partner	Measure number of clients being managed by each partner	For the normal business services general practice client numbers should not exceed 250 per partner. Will reduce significantly based on average fee per client		
Where a client rating system is used, the relative proportion of each group	Percentage of A, B, C & D clients relative to total client population	Dominance of A & B clients in total client population		

Strategies checklist to address under performance

Strategy	Expected impact	Timeframe for effect	Other impacts
Develop a target client profile	Should increase your marketing focus on acquiring the right type of client for your practice	3-6 months	Should assist in increasing profitability
Where you are client dependent, increase client base to lessen dependency	Reduced sensitivity should a key client leave the practice or have a change of circumstance	1-2 years	Will force pace of revenue growth and require increase in resources
Set partner client numbers and move clients between partners where necessary	Should smooth partner workload and create capacity for partners with excess client numbers	1-2 years	Growth will occur more readily
Establish and manage a client rating system	Will identify clients the practice needs to focus on, and also clients the practice should assess for their value to the firm	6 months	Where the firm needs to shed clients to create capacity, those clients will be readily identified. Also will provide data for effective delegation of client work
Establish a client acceptance criteria in accepting clients to the firm	Improved use of practice capacity because you are prepared to say no to some new clients	Immediate	Your client mix will trend in the right direction because you won't add to existing lower end clients or work
Consider sale or 'firing' of low quality clients	Will free practice capacity. Should only be used where there are real capacity issues or	Within 3 months	Will generally improve staff morale and where sold may provide some capital return

	where you are prepared to take a more drastic approach		
Develop your marketing around the characteristics of your target client	Should lead to more qualified client referrals and enquiries	Within 6 months	Will make your existing clients aware of the services you provide – may cause some passive cross sell

SERVICE RANGE

In terms of increasing revenues and profits, the introduction of new services has many advantages, including:

- Adding value to your existing client base
    - clients perceive they are receiving value for money
    - the average fee per client is increased
    - attracting new clients through additional services.
- Adding value to your practice by
    - relying less on traditional compliance work as the major revenue stream
    - better utilisation of existing capacity and providing more interesting work for team members
    - maximizing the goodwill of the business.

Increasing your service range will also act as a defensive mechanism for your practice. A broader service range will assist in client retention. Where you are planning to introduce new services you should make sure this aligns with your strategic direction. Also think about whether the focus should be on services that create active income i.e. where revenue is only generated from work performed, or passive income i.e. where some revenue may generate without work being performed e.g. trail commissions from financial planning or mortgage broking.

Most practices are dominated by compliance work. Tax and accounting may represent 80-90% of fees generated. In these cases, you have a ready market for the establishment of new services.

Broadening your service range is not something that happens overnight. In fact, it requires careful planning and implementation. Here are some matters to consider:

Capacity	Does the practice have the skills and the capacity to deliver the new services?
Market	Is there a market for the new service and is it complementary to existing services? Will this new service attract additional clients to the practice? Are these target clients?
Revenue & profit contributions	Over time (within five years) will the new services contribute at least 10% of the current revenue stream? Is the profit contribution by the new service at least equal to the firm's current threshold profit contribution?
Business analysis	Is the new service a growth area and can it be delivered within reasonable risk levels? To proceed to the implementation stage, the answers to the above questions should be yes. If the answer to any of the questions is no, you will need to reassess the proposal to introduce a new service.

Implementation	Obtain the necessary skills required to deliver the new service. Generally, this will require research, attending training and possibly employing or contracting additional resources or even gaining an additional qualification. Talking to and learning from other practitioners who have successfully implemented this new service can also save you a huge amount of time and effort. Appoint a professional who will head up the new service. This will generally be a person who has specialist skills in the area. Establish prices and prepare a financial forecast for the next 12 months for the new service, including any capital expenditure. Document the systems to deliver the service and develop examples of outcomes for marketing purposes. Target existing clients with whom you are likely to have immediate success, critical to building confidence and providing testimonials. Keep promoting the new service as it will need to be delivered at least 10 times before it gains momentum.

Expanding your range of services must be viewed as a long-term initiative. Sure, there will be early wins but the real benefit is from fine-tuning the service over time to be an established revenue and profit contributor.

Matching your service range to your client base

Too often accountants introduce new services without undertaking an analysis of their client base and their needs. The fact that a particular service area works well for one firm does not mean that it will work equally well in another firm. Before introducing a new service you need to have a clear picture of your client base, the segments they represent and their demographics. For example:

- an ageing client base is likely to have a need for financial planning and estate planning services
- a client base dominated by mature SMEs is likely to have a need for succession planning services
- a client base of fast growth entrepreneurs is likely to be interested in business improvement services
- a client base of profitable mature businesses is likely to want risk management and tax planning services
- a client base of micro businesses may have a demand for bookkeeping services.

Knowing and understanding your client base is a pre-requisite to the successful introduction of any new service line.

Delivering financial advice

Accountants should consider what role, if any, they want to play in the financial advice space. Almost certainly, the typical client of a CPA will have a need for financial advice at different stages in their lifecycle. The provision of financial services advice as a service stream of your practice could represent a part of your growth strategy. Equally it could be a part of your business risk management to ensure that you do not lose clients who are looking for a broader service proposition.

Currently about 50% of accountants in practice provide some form of financial advice solution for their clients. This may be through holding their own limited or full Australian Financial Services (AFS) licence, being an authorised representative of an AFS licence holder, or referring clients to an adviser who can provide advice. The latter two options are the most common solutions.

Over the last two decades the provision of financial advice has been dominated by financial planners operating through large financial institutions or non-aligned dealer groups. In some cases, these planners have worked in conjunction with the client's accountant, in other cases independent of accountants. Certainly there is evidence of financial planners and financial services institutions and groups seeking to build on their financial planning relationship with the client to broaden their service offer into space that has traditionally been the domain of the accountant. These planners are looking to secure 'the most trusted adviser' relationship that has historically been held by the accountant.

The financial services environment

There has been significant change over recent years in the legislative and regulatory environment for the delivery of financial advice. This has caused a level of disruption for providers into this market. Much of the change is a result of the quality of advice delivered to clients, losses suffered by investors and evidence of conflicted remuneration.

The focus of the change was to improve the quality of advice being provided, ensure that the interest of the client is paramount in the advice process, and to move the industry from a commission-based model to a fee for service remuneration model.

Decision process: What is right for you?

The decision on whether or not you participate in the financial services space, and if so, the best way to achieve this, is both a professional and commercial decision. There is no one answer that is right for every accountant. You need to work through a decision process to arrive at the conclusion most appropriate for your practice.

A starting point for this, at a business level, is to understand your client base, the services you currently provide to them and the extended services which may be of value to them. Where you have an individual client base, SMEs, SMSFs or high net worth clients it is likely that they will have a need for financial services advice. Accepting that a need exists, the follow-on question is do you want to provide this service? This can be a matter of professional aspiration together with resource requirements and your business strategy.

A practice that specialises in a corporate, government or institutional client base or focuses on the provision of specialist services such as audit, insolvency, corporate finance or high-level taxation advice may find that there is a lesser demand for financial services advice. This is all about understanding your market channels.

Further information on providing financial advice can be found on the CPA Australia website.

Download a Service range improvement workpaper.

Diagnostic checklist to assess your performance

Test method	Method of calculation	Benchmark objective	Your result	Test indicators
The number of service areas offered by your firm	Documentation of your areas of operation	Provision of a minimum four service areas		
Revenue contribution by service area	Identify and quantify fees by service area	Each service area should produce not less than 7% of practice revenue		

Strategies checklist to address under performance

Strategy	Expected impact	Timeframe for effect	Other impacts
Assess your capacity capability to introduce a new service	You will understand whether you have existing capacity or whether you need to address the capacity issue first	Immediate	You may need to secure additional resources
Identify possible new service areas and test market appetite with a small group of existing clients	Should lead to a hierarchy of new services for introduction	1-2 months	Will raise some client awareness about your provision of these services
Identify specific resource requirement of new service	Will identify resource requirements and their cost	3 months	Should ensure resources are in place to deliver service
Project and measure revenue and profit contributions from new service	Should confirm financial integrity of step	1 month	Will establish initial budgets and test financial expectations
Ensure that each new service has a partner responsible for its implementation	Provides the greatest chance of success when sponsored at a senior level	3 months	Will cause faster acceptance by both clients and your team
Have a specific marketing program for each new service introduced	Should cause a faster awareness and acceptance level of the service	3 months	Where marketing is linked with budgets this should increase accountability levels
Unless related services, avoid introducing more than one new service in a year	Will allow highest level of focus and should assist acceptance level	1 year	Avoids dilution of impact and allows fine tuning of implementation strategies

PRACTICE MATURITY

This is not an area that you have a lot of control over and it can only be changed with time.

Mature practices should command values at the higher end of the valuation range. This is because they should exhibit most of the following characteristics:

- an established brand and presence
- have good operating systems in place
- have developed longer term client relationships, with clients committed to the firm
- a good quality client base
- established infrastructure
- established staff relationships
- a network of other professionals and referral sources
- a history of financial performance
- a history of maintainable growth
- the absence of silo management – clients have contact with multiple people in the firm.

Many of these characteristics come with time as the practice evolves and moves through different growth phases. Having said this, time is not the only ingredient. There are practices that have been around for many years but which on assessment could still be described as immature. The level of active management of the practice will have a significant impact on this. Practices evolve in one of two main ways. The majority evolve in an unstructured way. The principals or partners are good at their profession, and they provide a reasonable service to those clients who come to the firm. Growth comes from being reactive to existing client growth and from referrals. This type of practice will have a very broad range of clients with the client base, in numbers, being dominated by smaller clients. These are generally good quality firms, however, the focus of the principals and partners tends to be on the profession of accounting rather than the business of accounting.

The alternate model is a firm that is developed strategically in a structured way. The business model and objectives are clear and detailed. And the operation of the practice is driven out of this model and its objectives.

If your practice doesn't have 'age' on its side, then the more strategic and structured your practice is the greater the number of maturity characteristics it will exhibit. Test yourself against the maturity characteristics we have identified in this section and then where they are under developed in your firm, start to work on them strategically. The only areas you will be limited in are where there is an absolute time requirement e.g. years of association with clients.

Keep in mind that a mature practice that has ceased to grow may be seen in the market as having limited upside potential. The market will always be attracted to firms that are growing irrespective of their maturity.

Your objective should be to exhibit the characteristics of practice maturity in the shortest possible time frame.

Download a Maturity improvement workpaper.

STAFFING

Profitability and work management efficiency go hand in hand. If your workflow efficiency is struggling, then it will show up in your profitability fairly quickly.

You have a busy practice. There always seems to be a lot on - plenty of things to do and you never seem to be fully on top of all the work demands. But even with all this activity, profitability just isn't where is should be. And even more frustrating is the fact that the partners are overworked and constantly under pressure. You think the only way to get on top of this is to work harder, put in those extra hours.

The answer to your problem could be as simple as examining your existing staff mix. Sometimes workflow efficiency falls away or is under pressure simply because you don't have the right mix of people in your practice.

Who makes up the staff mix?

Let's have a look at a typical accounting practice, the people it employs and their likely skill sets.

Partners	Normally experienced practitioners with a broad range of skills and sometimes specialist skills. Beyond their technical expertise they are also key to the business in the acquisition of clients, maintenance of client relationships and general practice management. Typically, they are managing a broad range of issues at any one time.
Managers	Would usually have 5+ years technical experience and are generally proficient with the technical aspects of the work. They may also have a technical specialisation and are the people we are most likely to go to, to handle the more complex issues or questions. They are also expected to be able to manage the work and production of a team, and reliably work with clients.
Intermediates & Seniors	Generally qualified and on their way along the professional career path. Normally reliable and efficient in their workflow. They may not have the same depth of technical expertise or experience in managing people.
Graduates	Plenty of enthusiasm and energy but still with a fair amount of learning to do. They need support at a technical level and ongoing review of their work progress.
Bookkeepers & support staff	Provide strong back office support for the practice and some levels of client interaction.

All of these professional job roles are important and each has a part to play in a busy practice. Take one out and you can either have people working without adequate supervision and access to senior staff or alternately seniors working on jobs that cannot support their charge rate. In both cases workflow efficiency suffers and quickly impacts on the bottom line.

Ask yourself, why is it that many accounting practices have high write-off levels? As a profession we have almost come to accept double digit write-off levels as the norm. This just doesn't make sense. In many cases the underlying reason behind high write-off levels is a poor staff mix.

Where you don't have a graduation in the experience and skill levels between the partners and the graduate professional staff you will often find:

- jobs delayed waiting for partner review
- partners spending significant time reviewing and working on low level jobs because they have no one to delegate the function to
- high level of job reworks due to inadequate supervision throughout the job process
- frustration of junior staff who can't get access to partner or senior time
- opportunities missed because the partners do not have adequate time to spend with their clients.

Example:

Terry and Steve have been partners for years and operate their practice in country Victoria. They have found it more difficult to employ senior staff, and to save some costs they have four graduates and three intermediaries. All of the face-to-face work is managed by the partners and much of their day is taken up with client meetings and phone calls. The staff, whilst enthusiastic and hard-working, have limited experience. They also have limited access to the partners throughout the day as they are normally tied up with clients. Most of their queries need to wait until after hours when the partners can look at them. They also typically do their work review outside of normal business hours, leaving notes with staff on corrections that are required. There is a growing level of frustration in the firm. The partners are becoming annoyed at the number of corrections required in work and the staff are frustrated at their lack of access to the partners and their ability to develop their skills. A recent review of the financial performance of the firm has also indicated a drop in profitability. Terry and Steve realise that they need a more experienced accountant to work with and be available to the junior staff.

What is the answer?

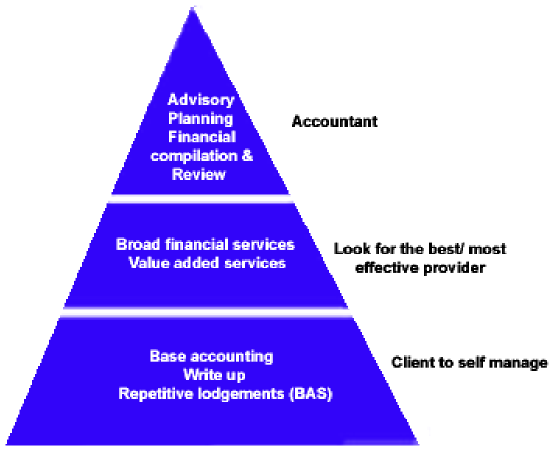
A good staffing mix will see a partner with a manager, two or more seniors and intermediates, and two graduates. This should be taken as a guide only and you need to look at this in light of the services provided by your firm. Business services and audit teams tend to fit into this type of staff mix model. For more specialist service areas you may find there is less need for graduate level staff and a greater requirement for more experienced staff.

The mix between compliance and advisory work will impact this. The greater the proportion of compliance work delivered by your firm the more the staff will fit the traditional mix model. Firms or teams within firms that are more advisory dominant may require a modified staffing model.

Allowing for your support staff, a partner/staff ratio of at least 1:7 is ideal to achieve good staff leverage and one which will allow you to drive your profitability into the upper quadrant.

Take a moment to review your staff mix. It may be holding back the development and profitability of your firm. Once you have worked out the staffing mix you need, make sure that the next time you recruit, you bring on people at the right level.

The other issue to consider is the nature of the work being undertaken by your practice and changes that may be occurring in your work program. Certainly, there is evidence in the profession that there is a change in the type of work being undertaken.



Work for most of us falls into these three segments. At the base we have all of the write-up work, base level repetitive compliance requirements and the more straight forward accounting functions. This has been typically the domain where we have engaged graduates and less experienced staff who have driven much of the 'hack work'. An important part of the overall accounting function but one that could be capably delegated and managed. Today technology is replacing this work function. You may be applying technology solutions or your clients may be managing this directly. The extent to which this is occurring will influence the type of base work you do and the skill sets required. The use of bookkeepers or less qualified people in some cases will be replaced by computer literate people familiar with accounting applications.

In the middle is the value-added work. This is the more specialist work, business advisory, financial planning, valuations, specialist tax advice etc. Some firms have found their way into this space but most have not mastered it. Often the general compliance demands mean that there is not enough time or resources to focus on this area and at times it is a bit hit and miss.

At the top of the pyramid is the work where principals, partners and senior staff spend most of their time. Review and sign off, financial compilation, audit and other attestation work, and tax planning can consume much of our time.

When you look at it, for the typical public practice firm it is this top layer of the pyramid where we earn our 'salary'. This is where we get our labour return. The good news is that this work is relatively safe and will continue to be there. So your salary should remain intact. This is not, however, where firms have typically made their profits. Profits have been largely generated from the work at the base of the pyramid. This has been where you could employ less expensive labour, charge them out at a multiple of around three times direct labour cost and providing you could keep the process reasonably efficient, then there was money to be made on a reliable and predictable basis.

The problem we have is that this is the work area that is eroding. Clients are taking back some of this work, in some cases with our encouragement. Computer accounting software programs are promoting and accelerating the transition. There is also a growing industry of bookkeeping services where this base level write-up work can often be delivered at a much lower cost. As this work disappears so does some of the profit base of the traditional firm. Another impact of this is that there is less sustainable work for graduates and less qualified staff. With this will come a pressure on staff mixes as work demand moves around.

In some cases, this trend is leading to a reduction in demand for lower qualified staff and an increase in demand for more senior staff. To manage this effectively you need to monitor the work demands of your practice and then ensure that you match your staff mix to the work mix you have.

Download a Staffing improvement workpaper.

Diagnostic checklist to assess your performance

Measurement	Method of calculation	Benchmark objective	Your result
Staff turnover	Annual staff resignations, terminations and retirements divided by average staff numbers for the year	Staff turnover rate should be within 10%	
Write-off levels	Total net write-off on jobs, as a percentage of gross fees	Should be less than 6%	
Surplus capacity percentage	Available capacity less gross fees as a percentage of available capacity	Should be less than 10% unless the practice is moving through a planned growth phase	

Strategies checklist to address under performance

Strategy	Expected impact	Timeframe for effect	Other impacts
Review your work program and identify levels of staff required for the practice	Achieve a better match of work to worker	Will depend on your recruitment requirements – more senior staff are harder to attract	Once in place should reduce write-off levels
Ensure you have a middle tier of staffing – one to two seniors or managers per partner	Will free up partner time and reduce demand dealing with lower level queries	3 months	Reduce frustration level of junior staff who can’t access partners or who have delayed reviews
Have a clear delegation system in place – not everything has to be managed by a partner	Authority and responsibility levels for all staff will lead to better work throughput	3 months	Better access for clients and greater job satisfaction for staff
Understand your staff motivators and implement programs to address these e.g. performance feedback, team building exercises, good work environment, market-based remuneration, coaching and mentoring	Reduced staff turnover and attendance costs	6-12 months	Improved staff morale, reduced sick leave and a more enjoyable work environment

Provide staff with career paths	Will increase your average years of staff retention	1-3 years	May create your partners of the future and your own succession path
Always be in the market for good quality staff	May assist in picking up scarce senior staff when they come on to the market	Ongoing	Tends to force a growth mentality in the firm
Establish a graduate development program	A grow your own strategy that may develop your senior staff of the future	Ongoing	Will place an increased focus on staff retention to ensure that you don't lose good people you have trained

LEVERAGE

Leverage is something that should interest every principal or partner. At its most basic, it is about creating more with less. Where you have scarce resources or expensive resources managing and making the most of leverage is critical. Most principals or partners wish they had more time. It is the greatest limiter in what can be achieved and the problem is accentuated because you cannot readily replicate what you do. Or can you?

Effective leverage will increase revenues and profits. At the same time it will reduce risks and frustrations.

Leverage can be achieved in a number of ways, including through:

- people
- systems
- business models.

Professional services businesses are seen as personal services businesses. And in most cases they are. The majority of practices are small in people numbers and dominated by the key principal or partners. Most of the direct revenue and business generation comes from one or a few people. A by-product of this has been that most principals or partners require the majority, if not all, of the work flow to pass through them. An argument to support this has been the need for quality control, a principle everyone would support. As a result, the growth and revenue capacity of a firm is normally limited to the available time of the key people. Once they are time 'locked', growth stops. This tends to set a finite limit around what a practitioner can achieve, and a reasonably predictable range on revenue and profit returns.

Leverage is one of the ways to extend the capacity and range of what can be achieved.

People leverage

People leverage comes in two forms – low and high. Low level people leverage is where you engage staff to perform support functions. This may include secretarial work, basic bookkeeping, write-up work or any of those functions that are typical back office roles within a professional services firm. This will free up the principal or partner to spend more time with clients and on more complex work. The result of this should be more chargeable time at partner rates, with some lower level work charged out at lesser rates. Whilst there are still limitations, you achieve the best outcome for the time available. This form of leverage allows you to get the best out of yourself.

Practices producing fees in the range of $300K to $700K per principal, per annum, generally are engaging low level leverage to some degree.

High level people leverage occurs when you employ people to do what you do; that is care for clients and deliver high level services. This doesn't occur instead of low level leverage, but in addition to. It will remove the ceiling on the number of clients the practice can take on. It is not just limited to what you can do. There are a number of seniors able to manage clients and complex work assignments. High level leverage will normally allow principals or partners to manage fees in the range of $700K to $1.5 million per annum.

The higher the level of leverage you employ, the more important it is to have strong quality control and operating systems in place.

A good staffing mix will create a partner/staff ratio of at least 1:7 – an ideal level to achieve good staff leverage and one which will allow you to drive your profitability into the upper quadrant.

Take a moment to review your staff mix. It may be holding back the development and profitability of your firm. Once you have worked out the staffing mix you need, make sure that the next time you recruit, you bring on people at the right level

Systems leverage

Systems leverage comes when your business systems and processes can complete or assist what otherwise would have been a labour-based function. Strong systems can take the human element out of the equation. These systems will either be focused on reducing costs or in some cases actually driving revenues. Systems linked with technology delivery tend to achieve the best result.

In developing your systems, the greatest gains will be taken from systems that deliver:

- a quality control process
- automation of routine and repetitive tasks
- effective delegation of work functions
- management of job progress and workflow
- reduced documentation and paper flow
- automated client follow-up.

Business model leverage

Business model leverage occurs when your business model drives growth and revenue in its own right. The typical professional practice business model is an hours-charged model. Under this model the aim is to maximise the hours being charged and to maximise the charge rate of those hours. Delivered effectively it will produce strong profitability. The limitations tend to be resourcing the firm with sufficient people to deliver the hours and acquiring the clients willing to pay the charge rates employed. These two primary limiters create the boundaries for the firm.

If this is the case, then the only way to overcome it is to modify your business model. This could be achieved by introducing a level of passive income into the firm. The most common examples of this in accounting practices would be the introduction of financial planning or mortgage broking services, where there is some level of recurring income. Annuity income normally has a time period to produce a meaningful impact within a firm, but once it starts it will normally accelerate and drive significant profit improvement.

Download a Leverage improvement workpaper.

Diagnostic checklist to assess your performance

Measurement	Method of calculation	Benchmark objective	Your result
Workflow turn around time	Average number of days from receipt of work till completion of job	Have a process in place for a work completion within 30 days of receipt or as agreed with client	
Partner staff ratio	Number of staff per partner	A partner staff ratio of 1:7 or greater should provide high level leverage, providing it includes some senior staff managing client portfolios and complex work matters	
Annuity income	Percentage of annuity income to gross revenue	Once annuity income exceeds 10% of gross revenue it begins to make a meaningful contribution to the business	
Premium services	Delivery of services where a premium above standard charges rate is achieved	Your service mix should include services that produce revenues greater than 15% of total fees and where those services command a premium greater than 30% of standard charge rates	

Strategies checklist to address under performance

Strategy	Expected impact	Timeframe for effect	Other impacts
Set partner staff ratio levels	Partners will have a clear understanding of the number of staff they need to manage and the leverage levels required	Will depend on current status but improvement should be achievable over one year	Forces partners to delegate, manage higher level work and grow their client base
Delegate client management	Managers and senior should be managing C & D clients	1 year	Grows the skills of your seniors and managers and frees up partner time for high level work and client acquisition
All routine work delegated	Work should be driven to the lowest skill level where it can be efficiently completed	1 year	Will provide greater work variety for all staff, increasing job satisfaction
Set a minimum requirement of at least one manager and one senior for every partner	Forces partner development and creates staff career paths	1 year	Will open up internal succession opportunities

Identify significant processes that can be automated	Increasing levels of systemisation will produce cost savings	3-6 months	Will enhance quality control and risk management
Assess annuity income opportunities for the firm	Enhanced revenues and profitability	1 year	Revenues created that are not as people dependent
Identify specialist services appropriate for your client base and where a premium charge rate could be applied	Enhanced revenue and profitability	1 year	Firm reputation grows through differentiated service offering

SYSTEMS AND PROCEDURES

Systems are the lifeblood of a business. They allow a business owner to work on the business not in it. They increase the sales value of the business, they add to profitability, they reduce the incidence of problems within a business and they enable the owner to take a holiday without the business shutting down. They form a part of the risk management and quality control foundations of any business.

All good reasons for the implementation of systems. Many businesses, including professional practices, don't do this because they need to be planned, documented, enforced, reviewed and updated to be of any use.

Let us do a stocktake of the areas that your practice should have documented systems in place. Tick Yes if you have documented systems in place which are updated and followed. If you have systems in place which are not documented or updated, tick Maybe and tick No if there are no systems in place.

Area	Yes	Maybe	No	Comments
Budgeting				
Computer (hardware and software)				
Debtors control				
Equipment management				
Filing system				
Financial reporting				
Marketing				
Personnel				
Training				

WIP management				
Work processing				
Work scheduling				

If you have a number of ticks in the Yes column, you understand the value of good systems. If the ticks are in the Maybe or No columns, then you should think seriously at dedicating resources into developing or improving systems within your practice.

For accountancy practitioners there are some generic notes of systems available on the market. These can be a great cost-effective base to start from to help build and document appropriate systems for your practice. The time saving from not having to start from scratch can be significant.

Download Systems and procedures improvement workpaper.

Diagnostic checklist to assess your performance

Test method	**Method of calculation**	**Benchmark objective**	**Your result**	**Test indicators**
Documentation of practice systems	Evidence of documented practice systems used in operations	All key operating areas of the practice are documented and systems adhered to by staff		
Single system approach by all staff	Review of working papers and files demonstrate single system approach within the firm	No evidence of silo approaches in firms where different partners operate in different ways or where staff have operational discretion		
Peer reviews	Review of professional body quality review report	Receipt of an unqualified quality review report		
Risk management system	Documented risk management system	Fully documented risk management system and evidence of annual review		
Adherence to professional standards	Measurement against all relevant standards	Fully compliant with all standards		

Strategies checklist to address under performance

Strategy	**Expected impact**	**Timeframe for effect**	**Other impacts**
Conduct a systems audit	Should identify systems gap and areas that need to be addressed	1 month	May identify quality control or risk management exposure

Create a hierarchy of systems or procedures requirements	Will provide a to do list and address the most important areas first	3 months	Should assist in failing to do something because you don't know where to start or are overwhelmed by the extent of the work
Allocate systems development to people responsible for operational areas	Delegation of the work should produce a faster and better result	3 months	Involvement of key members of the team should increase the level of systems awareness
Buy-in or subscribe to systems and procedures providers	Will shorten time frame and may lower cost of systems development	3 months	Allows you to access what is already working. May be closer to best practice
Timetable and milestone change process	Should assist in ensuring the job is done	3-6 months	Will maintain the pressure to deliver and elevate the focus
All partners to agree a single system approach	Staff buy-in will only occur when supported by partner implementation	6 months	Will create efficiency where all the staff are using a single system or where work flow or staff move across partner teams

WRITE-OFF LEVELS

Year in and year out practitioners give away large amounts of money in the write-off levels we accept within our practices. The difference is that this money isn't going to a good cause – it's simply going down the drain.

Take a moment to think about it. Consider the gross fees of your firm. Now work out what 1% of that number is. For example, with gross fees of $500,000 every 1% represents $5,000. Now start to think about your write-off levels - that's if you've taken the time to work them out. If you have a write-off level of 10% that would represent $50,000. How many firms with fees of $500K per annum can afford to write out a cheque to a charity for $50,000 and are prepared to do so every year? The answer is not many, if any.

Yet as a profession we seem to be prepared to accept double digit write-off levels as an acceptable part of life. It just doesn't make sense.

To assess your write-off levels you can go to your practice management system and pick up the number that represents your write-off level for the year. Alternately, if you aren't using such a system or it isn't up to date, then you can come up with a pretty good approximation by looking at your revenue capacity for a year after adjustment for your write-off expectation. Then compare this number with your actual revenues. Be careful though, you may cringe a little at the result.

It's important to understand that every practice has write-offs. The reality is they are unavoidable. We all have those jobs where it just doesn't go right and there is a big 'rip up' at the end. The key is to drive down the number of times it occurs and ensure that it is not a part of the culture of the firm. And that's where practice management comes in.

As a guide, the following table provides you with a suggestion on write-off levels to work with across your firm.

Less than 2.5%	Best practice
2.5% - 5%	Good
5% - 8%	Average
8% - 12%	Requires review
Greater than 12%	Structural management problems exist within the practice

If you are experiencing high write-off levels it will generally be for one of the following reasons:

- poor job flow management
- poor quality records from the client
- lack of job systems and procedures
- a mismatch between the work and the skill set of the person assigned to the job
- lack of appropriately qualified staff
- lack of adequate staff training
- inadequate job supervision
- fee for the job below a realistic level
- inappropriate charge rates.

You can see from this list that we are either looking at an internal problem in terms of work and staff management or a problem with your client mix and how work is being billed and charged.

If your write-off levels are too high, then have a look at your practice. You should be able to identify fairly quickly where the problems are. Then go to work on them – a piece at a time.

What you are trying to achieve is performance modification and positive progress. As an example, if you have a current write-off level of 15% then it is unlikely that you will be able to turn this into a 5% level over a short period of time. An improvement of 2-3% over a six-month period should however be achievable. Improvement will all be about incremental steps.

And those steps are worth it. How much is a 1% difference worth in your firm? It may take a little time and effort but get it right and you will be a beneficiary many times over. And in the process the next time you go to make a donation to a charity, you have a greater capacity to be generous in your giving to a good cause.

Example:

Juan operates a small sole practitioner firm. He notices over a period of time that he has a consistent write-off level on client work of 12%. Most of his work is recurring business services work for an SME client base. He agrees fixed fees with his clients to avoid any fee uncertainty for them and he bills them in instalments each month to smooth out cash flow. His liquidity is good but his profitability is less than he would like. In an effort to identify the problem Juan reviews the details of a sample of client jobs. The outcome is that, on a consistent basis, the actual accounting and tax work he does is within the budget. However, the clients contact him from time to time with queries or seeking additional advice and this is causing the budget over run. Juan decides to increase his fixed fee quote by 10% to allow for these minor contact points and recover his time cost.

Download a Write-off level improvement workpaper.

Diagnostic checklist to assess your performance

Measurement	Method of calculation	Benchmark objective	Your result
Write-off levels	Gross fees written off from work in progress divided by gross revenue capacity for the year	Maintain write-off levels below 6% per annum. Where write-off levels are in excess of 10%, significant corrective action is required	

Strategies checklist to address under performance

Strategy	Expected impact	Timeframe for effect	Other impacts
Set write-off expectations and communicate to all of the team	Higher accountability will increase the performance focus	Should be immediate	Forces partners to take a more active approach to management
Measure write-off performance on not less than a monthly basis	Increased visibility will highlight problem areas and make people more conscious of performance	3 months	Performance may improve through competitive pressures
Have an active job management system in place that identifies job budgets and actuals	Issues will be identified at an earlier stage	1-2 months	Will allow a level of team management, where staff have access to information on what is happening
Be prepared to decline work where the record quality is poor, or alternatively charge for it	Should produce better record quality from clients	3-6 months	Reduces staff frustration where the problem is outside of their control
Have clear procedures in place for all jobs, supported by standard workpapers and checklists	More efficient processing of job stages	3 months	Staff will have greater certainty on what is expected
Ensure that job allocation process is appropriate	Staff allocated work should be capable of completing the work	Immediate	Significant reduction in review and rework time
Have appropriate job supervision and review processes in place	Staff will have access to assistance throughout the job and receive feedback on job progress	Immediate	Should reduce level of rework and time required in rework of problem areas
Fees quoted on jobs are appropriate for the work required	Clear alignment between reasonable time to complete work and fee quoted	Immediate	Remove staff frustration where fees quoted create a no win position
Work to be driven down through the firm to the level where it can be effectively completed	Avoids high charge rate staff completing low charge rate work	Immediate	Matches work to worker and forces senior staff to engage in more complex work

FURTHER RESOURCES

- Client service mix
- Succession planning
- Roadmap to practice growth and succession (PDF)
- Unplanned succession (PDF)
- Succession options (PDF)
- Valuation and pricing (PDF)
- Succession implementation (PDF)

About the author
Greg Hayes, Director, Hayes Knight (NSW) Pty Ltd, has broad experience and knowledge in the area of public practice succession. With over 20 years experience as a public practitioner, Greg's focus is on business consulting and taxation. He specializes in strategic planning techniques and is well known in the areas of practice management and business development, having been an active commentator in this area for over 15 years.

Support and Guidance
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