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Unspoken Obstacles Prevent Many Accounting Firm Mergers and Sales

By Robert Fligel

Based on demographics of the accounting profession, it's commonly accepted that a sizable number of CPA firms should be merging or selling. Many of these firms—ones with maturing ownership and others that need to combine with another firm in order to realize their growth potential—say they recognize the need to merge or sell, and indeed many say they want to. However, only a small percentage follow through. Meanwhile, the list of firms that could or should be selling or merging grows larger by the month. The good news is that there are solutions for both sellers who want to overcome their discomfort and for acquiring firms that are frustrated by their inability to close a deal.

Demographics indicate the types of firms that should be or could be merging or selling at this point are:

- Aging firms without successors;
- Small or midsized firms that have mergers or acquisitions as part of their growth strategy;
- Firms with strong specializations that want to provide a fuller range of services; and
- Firms with other significant challenges, such as recruiting and retention or a need to invest in technology.

Beyond the standard answer of "We can't find the right fit," several fears that rarely get fully articulated prevent CPA owners from speaking with potential buyers or from moving forward once they begin discussions. Unmasking these major stumbling blocks that prevent mergers or sales speaks to the difficulties involved in CPA firm mergers, but allows for the development of practical ways to manage and overcome these obstacles.

Why Do Firms Hold Back?

Based on discussions with hundreds of small and midsized CPA firms that previously indicated at least some interest in selling or merging, the author quantified these often unspoken obstacles, asking acquirers why they believe sellers are reluctant to move forward with deals. Simultaneously, sellers were asked about their biggest concerns and compared the two sets of answers in the *Exhibit*.

The research illustrates a significant disconnect between the perceptions of sellers and acquirers. The fact that acquirers may not fully understand the obstacles limits the number of deals that are completed and creates a barrier between the buyer and seller. Sellers and acquirers can take steps to bridge the gap.

Issue 1: Don't want to give up control/be "managed." The issue of control is real and perhaps at the crux of almost every potential seller's ambivalence. Stepping away from making all firm decisions, such as signing off on financial statements, tax returns, bills, and the like, is quite difficult. Acquiring firms have an existing structure that the seller will need to work within. But for the right firm and the right "fit," this is a small price to pay.

It's important to remember that during the sale or merger process, everything can be negotiated. In the right merger or purchase, firm owners may be able to better manage how much control they retain or give up, and the transition time for this change. Perhaps for the first six months, the acquired firm operates as a "division of." Perhaps the owner retains certain management duties for an even longer time.

In some cases, despite initial apprehensions about a loss of control, former firm owners find they are relieved not to have certain management tasks. The right acquirer will work with a firm looking to sell in order to be sure its management does not feel marginalized.

Issue 2: Can't find the right fit. CPA firm owners who say they can't find the right fit usually mean they aren't ready. They haven't determined what they really want or haven't documented what they can offer another firm. Most likely, they haven't taken time to analyze and document their business. They need to ask and answer: What are the percentages of the various services offered to clients? The percentages of work done in specific industries or other niches? What kind of role do they want or could they accept in a new firm?

The solution is all about planning, preparation, and motivation. Devote time to the process just as for any other significant project. Like any other project undertaken by the firm, this has an ROI attached to it—a very strong one if done properly. First and foremost is to prepare fully by documenting exactly what the firm has to offer and what is most important to the owners, the clients, and, if applicable, the staff. Because being objective about one's own firm is difficult, being guided through the process by an expert consultant is helpful.

If all of this is taken into account and the CPA takes the time to identify potential targets, a series of meetings, and ultimately a transaction, will occur. This is not easy, but simply a structured way to address a very important business task.

Issue 3: Can make more money by not selling. Sometimes aging CPA owners think they can make more money if they let their

EXHIBIT
Why CPA Firms Are Reluctant to Merge or Sell

	In the opinion of potential:	
	Sellers	**Acquirers**
Don't want to give up control/be "managed"	5	3
Cannot find the right fit	4	1
Can make more money by not selling	3	2
Don't have time	2	3
Fear of change	1	5
Have no other interests besides work	1	4

Note: Rating scale of 1 to 5; 5 is most important practices self-liquidate. This rarely works, however, because clients and staff start leaving, resulting in a loss of both current income and overall firm value. Even for younger CPA owners, determining which path will result in a larger long-term financial payoff is an important evaluation.

The bottom line here is that both the buyer and seller need to come to a conclusion—and the terms of a deal—that allows both of them to make more money together than apart.

It is fairly common knowledge that most practice sales where the prior firm's leader will be retiring in 12 to 24 months are retention-based. In the right situation, a transaction can be structured where the "retiring" partner does not make less than at present. That would be contingent on client retention and similar efforts relating to billable hours, as if the practice was not being sold. A buyout would commence at an agreed-upon reduction of billable time. Similarly, an arrangement could be negotiated where the seller stays on indefinitely post-buyout and gets paid a percentage of revenue collected.

The answer here is to qualify, qualify, and qualify some more. The owners should have meaningful and detailed conversations and meetings only with firms that share their vision of how the owners would like to transition and what their role will be. Firm owners considering a sale need to do a serious reality check by making sure what they want is realistic in the current environment. Outside consultants are often helpful in providing that unbiased view of a firm's worth.

Issue 4: Don't have time to deal with it. The "no time" excuse is a major smokescreen. All people make choices about what to do that reflect their priorities as well as their fears. Why do some people work 12-plus hours a day rather than "nine-to-five," or exercise regularly instead of merely thinking about going to the gym? People make time for what they deem important.

CPA firm owners who have said they "don't have time" need to examine closely what they have time for, and determine where the sale or merger of their firm stands against these other tasks. Most likely the time isn't right or the motivation simply isn't there. It's never just the lack of time.

Issue 5: Fear of change. Moving away from the status quo prevents more mergers and acquisitions in the accounting profession than any other obstacle—yet it is often unspoken. Most people don't handle change well. Think about CPAs who have managed their firms for anywhere from 20 to 40-plus years. They need to consider what will happen to their family, staff, and clients when (not if) they are unable to work. It is a rare person, CPA or not, who can coolly and calmly think through all of the alternatives and map out a plan. This is true even for younger CPA firm owners who have built a practice and created something of which they're proud. The idea of moving in a different direction is often paralyzing.

To determine whether the fear of change is rational or not, firm owners need to become comfortable with the idea of change by speaking with other accounting professionals and firm owners who have done it successfully. First, speak with other CPAs who have sold or merged their practices. They should solicit input from their closest advisors about a possible sale or merger. Another option is to speak with a consultant who handles these kinds of issues daily and who can provide an unbiased, third-party opinion void of attachments to the subject firm. This sort of expert should be able to provide examples of firms that have successfully completed numerous mergers and could facilitate discussions with these firms' merged-in partners.

Issue 6: Have no other significant interests. A lack of outside interests could be a significant underlying reason many CPAs hold back taking steps to transition their practices. Although not readily admitted, it needs to be addressed. Even in the case of the new firm that has a great record of merged-in partners staying active for an extended time, having more free time than before is almost guaranteed.

The best question a practitioner can ask himself is: "What will I do if I slow down or retire and have a good deal more free time?"

As Dr. Phil, the popular TV psychologist, might say, these CPA firm owners need to ask how they define themselves. Is it in their best interest to redefine themselves at this point in their lives and careers? Or can they?

Sometimes all it takes is some deep thinking about the options, which can include:

- Spending more time with spouse, children, or grandchildren
- Traveling
- Cultural activities
- Reconnecting with a passion from earlier in life, such as music, literature, golf, or collecting memorabilia
- Exercising and getting in better shape
- Volunteering, which could involve working with a state CPA society, mentoring, or participating in college accounting programs.

The options are unlimited and, for many individuals, quite exhilarating. On the other hand, many CPAs (and people in general) have defined themselves so much by their work that they can feel lost without it. For these individuals, it will be best to find a firm that will be comfortable with a long-term attachment.

Big Questions

CPA firm owners who don't have a successor and are one to seven years from wanting to retire, or who want to consider a merger for long-term growth, should ask themselves if they are totally happy now with:

- The work they are doing;
- Their work/home balance;
- Their earnings; and
- The future prospects of their practice.

A "no" answer to even one question is reason to begin determining a way to act on it and plan accordingly. CPA firm owners should get their spouses behind them, line up close advisors to guide them along, and confide in fellow CPAs.

Additionally, look at the alternatives. If the firm owner became ill and otherwise unable to work, how would the family be provided for? Will clients leave? (Of course they will, if they need work done and only the firm owner can do it.) If there is staff, could the firm be "stolen" by long-time staff members in the absence of an agreement by which they purchase the practice?

Considering how unpleasant these thoughts are, it's surprising that more firm owners are not moving forward on their stated desire of selling or merging. Conversely, if that stated opinion has not been fully thought through, don't start the process. It's very time-consuming and could have a negative effect on a firm's leadership, its staff, and potential acquirers.

Another consideration is the current marketplace. The demographics are such that, over the next several years, more and more firms will need to sell or merge. Valuations will go down as supply increases and buyers become increasingly discerning. This will lead to pricing pressure and result in lower payouts for a merger or sale.

For many CPA owners, now is the time to start actively considering long-term options by accepting some of the realities contained in this article, and starting the process. ❑

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