PRACTICE MANAGEMENT

Voices Is your firm ready to stay independent?

By Gary Shamis, David M. Toth February 15, 2024, 10:00 a.m. EST 6 Min Read

Recent years have seen a wave of disruption in the accounting profession. M&A activity has significantly accelerated, fueled in large part by private equity investments into many well-established accounting firms, among other areas, including succession challenges, capacity restraints and technology investments.

Plenty of firms will remain independent. But with the growing competitive pressures and changing landscape, it's a discussion that more leaders need to be having with their partner group or executive committee to ensure alignment and clarity. Achieving and sustaining success as an independent firm demands a thoughtful, intentional approach going forward, and the time to have that conversation is now.

An unprecedented wave of M&A activity

Since 2021, the acceleration of activity has made headlines in the news around the consolidation of the profession. The majority of the top 20 firms have grown through merger or acquisitions, not organically. In addition, the influx of capital from private equity has created new competitors in

With the top 15 firms actively pursuing both M&A and organic growth, achieving the necessary revenue to fight for a spot in the Top 10 is more competitive than ever before. This leaves middle-market firms with tremendous opportunities (and challenges), whether it be investing in technology, dealing with multiple generations in the workplace, developing a one-firm approach with multiple offices, and developing the capabilities to capture larger clients. In many cases — and geographies — the middle market has become a "blue ocean."

This influx of M&A activity is fueling higher valuations. Today, an accounting firm might expect to sell for 20% or 40% more than a few years ago, all other things being equal. Investors are placing a significant premium on a certain type of firm: well-run organizations with an impressive bench of younger talent or areas of specialties including advisory services.

A strategic crossroads with three options

Firms have three options: Seek private equity funding, sell to another firm, or stay independent. This may be a worthy topic for your next partner retreat or executive committee meeting — we suggest starting with the question of whether your firm should stay independent. We are in no way advocating that firms stay independent, but today's options might not be there tomorrow, so firms need a real open-minded discussion on their future.

While the decision to stay independent might be the assumed feeling, it's important for firms to interrogate that choice. When my firm, SS&G, sold to BDO, this conversation never happened. Rather, In a lot of cases, the question of whether to stay independent is skipped over in the strategic planning process. Seems silly, but it's true.

Is your firm ready to stay independent?

There are three immediate criteria that firms need to satisfy to entertain the question of whether to stay independent. If a firm cannot definitively meet the criteria below, it must intentionally correct its path and be willing to address the gap.

These three critical areas are:

1. **Partnership alignment**. A strong consensus in the leadership group must be aligned on the long-term strategy and vision of the firm. In many cases, this discussion closely evaluates the inherent assets of the firm.
2. **Succession plan**. To stay independent, firms need a strong bench of leaders that embrace the firm's culture to ensure seamless transitions, and provide confidence among the current leaders of the firm that the legacy (and deferred comp requirements) that the firm demands will continue to be met.
3. **Talented leadership**. To be independently successful, firms need a commanding managing partner and executive team who are capable of executing long-term strategies and are surrounded by key personnel equipped with the skills to assist.

Establishing where any firm lands on these three issues clearly demands significant internal discussions. Given the nature of these conversations, it's often helpful to leverage a partner retreat to give leaders the freedom to step back from the day-to-day and assess the future of their firm together.

The ingredients for success

growth and profitability as an independent firm also requires in-depth assessments of its capabilities, culture, and business model.

One of the key issues is a firm's financial performance. To remain independent, the firm has to be able to generate enough profits to fund deferred compensation, keep active partners happy, and provide opportunities attractive enough to retain emerging leaders with no shortage of career opportunities.

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In many instances, that can lead to a debate over the partnership model itself, with many firms considering a shift toward a corporation model that provides stronger opportunities for up-and-coming professionals and provides a governance model that allows for faster decision-making and more control by the managing partner or CEO. Historically, decision-making under the partnership model has required a consensus of many. When competing against PE-owned firms, this does not provide a competitive edge when it comes to decision-making and execution.

strategy is becoming ever more important, technology is changing the way services are provided, and many firms are starting to embrace outsourcing in response to capacity challenges. Adapting to these changes is key to the firm's long-term growth, but requires partners to sacrifice today's profits to invest in the future.

Independent firms also need to invest in creating new advisory services that create stickier client relationships: cybersecurity, wealth management, data analytics, HR, payroll, and so on. If firms want to remain competitive and drive the profits necessary to reinvest, investing in building out practices around these services is vital in keeping and growing client relationships.

Toward the future: Assessing your options

One thing is clear: Accounting firms today have far greater optionality than at any point in recent memory. The industry is still in the early innings of this new era, and it remains to be seen how things will shake out in coming years.

So much of this issue comes down to your firm's culture. To be successful as an independent firm, firms need an entrepreneurial, growth-oriented culture that empowers individual leaders to deliver results. Building that culture is a journey, one that leaders must take a thoughtful, highly intentional approach toward.

With the right culture and a considered approach to the question of whether to remain independent, accounting firms have a bright future full of opportunities, regardless of the path they decide to take.

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