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## ***HOW TO ASSESS AN ACQUISITION STRATEGY TO START OR EXPAND A FINANCIAL SERVICES PRACTICE***

Either you have decided to offer financial services to your clients or you want to grow the talent pool of your existing financial services practice. Should you acquire a firm that already offers those services to accomplish that goal? Acquisitions or mergers with CPA firms with financial services practices or with dedicated financial planning or investment management firms offer a great opportunity to execute your strategy. Make sure you have fully evaluated what you will encounter before you leap.

There are four areas that you should consider that will affect how you will operate a financial services practice:

- ***Products and services***
- ***Marketing***
- ***Culture***
- ***Regulatory and organizational***

As you evaluate target firms, determine how you want to operate your financial services practice and evaluate the candidates' current and intended tactics against that benchmark.

### ***Products and services***

There is a wide range of financial services and products accountants offer their clients in today's market. At one end of the range are fee-based financial planning engagements that don't result in the recommendation of specific products. With referral arrangements the accountant offers the client more guidance regarding solutions although the execution will be handled by a third party. Fee-based asset management arrangements with a limited set of product solutions (such as indexed mutual funds) involve making specific product recommendations with at least the perception of some limitation on risk. At the other end of the spectrum are accountants that manage accounts holding specific equities and the sale of products like limited partnerships. Another important consideration in products selection is whether or not to offer insurance products.

Before you pursue a merger or acquisition of a financial services firm, determine what products and services you want to offer and how you want to be paid for the value you help create. How much risk are you willing to accept? Are you comfortable with the way your clients and referral sources will view your firm based on this new offering? Are you willing to accept commissions or fees for making referrals?

If your practice has a substantial number of attest clients you may have some ethical issues providing certain types of financial services to the business entity and its owners. Are there other large client segments in your practice that present ethical or strategic restrictions on the types and manner in which financial services are provided? This consideration should have an impact on the structure of your financial services practice. Otherwise, you may have difficulty creating alignment and support, within your firm for the strategy. Ethical conflicts can sometimes be diminished through the use of a separate entity to provide financial services.

### ***Marketing***

There are two specific considerations regarding how you will acquire financial services clients: cross-selling these services to your existing clients and acquiring new clients in your marketplace using financial services as a featured offering.

#### ***Cross-selling your existing clients***

The biggest performance gap for accounting firms that launch financial services practices is a failure to penetrate their existing client base. This is especially the case if a firm merges in or acquires a firm that already provides such services. Usually, financial services professionals that join a CPA firm in a business combination or affiliation assume they will be given total access to the existing client base. The acquiring firm normally makes the same assumption in developing the business case for the merger or acquisition. Both parties often also assume the cross-selling opportunity is a two way street. The firm you acquire may also have clients that are candidates to utilize the services your firm offers that the merged firm doesn't offer. Both of these assumptions are valid and access to these captive audiences is at the core of why firms pursue this strategy. However, it is important to specifically address how cross-selling will be executed for both client bases and be realistic about what internal obstacles will have to be overcome.

The reasons why accounting professionals responsible for client relationship management (CRM) are often unwilling to introduce clients to new areas of service are many. The primary reason is the perception that there is risk of losing client relationships. The difficulty of cross-selling financial services in many firms isn't any different than cross-selling other non-core services. If your firm has unsuccessfully attempted to cross-sell specialized services in the past, this can pose an even greater problem. CRMs that fail to embrace and execute the strategy do so because:

- They aren't comfortable discussing services and solutions that they don't understand with clients.
- They aren't comfortable turning over a client relationship to someone else for fear that the client won't be treated appropriately.
- They don't really support the concept of offering the service to clients in the first place due to ethical or branding issues.

You may not achieve total buy-in from everyone in the firm for this strategy. However, if you develop a complete analysis and discuss the plan with all the parties involved you are more likely to achieve the desired results. Consider doing the following during the pre-merger planning process:

- **Analyze the existing client base.** Determine the specific number of clients that will be candidates for these new services. Identify candidate clients by name, estimate what investable assets might be available and document what services they would be interested in based on what you know of their circumstances.
- **Develop a plan for how the clients will be introduced to the services.** What communication tactics will be used? Will you depend on the existing CRMs to communicate the offering or will you allow direct access by the financial services professionals? What form and in what venue will the communication take place? Verbal? Written? As a part of other regular client meetings? Will you offer seminars, a popular way to communicate with financial services targets? Include the new financial services professionals who will be coming with the merger or acquisition in this discussion to assure you have proper alignment of plans.
- **Obtain a specific commitment from the existing CRMs.** Have them determine how many of their clients will be introduced to the new services in accordance with your marketing plan. Make them be specific. For example, if you intend to use seminar marketing, have them commit to how many clients they will invite to the first three seminars. It is easier to get a commitment for participating in the marketing process than specific outcomes like generating assets under management. Normally, if you can get past the introduction stage with CRMs, generating new financial services clients will follow.
- **Put teeth in the CRM commitments.** Usually this is best done by tying some of the CRMs or other key associates' compensation to delivering on the commitments they made to the process.
- **Educate the CRMs.** You don't have to turn all the CRMs into financial services experts. In fact, make sure they understand their limitations. You are acquiring or affiliating with a financial services firm to obtain the necessary expertise. Give them enough knowledge so that they can identify opportunities in their client base and in the market and can open the discussion so that an internal referral can be made. Many cross-selling opportunities are missed because a CRM tries to internally deliver a financial services client instead of a referral.
- **Reverse the planning process for the acquired firm's clients.** Make sure both parties to the merger understand how your existing services will be offered to the acquired firm's clients and obtain the same commitments from the other firm's CRMs.

### ***Acquiring new financial services clients in the marketplace***

Assuming you intend to acquire new financial services clients from the general marketplace, develop a complete understanding of how the marketing and practice development will occur. Financial services firms often use practice development tactics for acquiring new clients that are different than CPA firms use for practice development of core services. The types of new clients may also be different than your current target

core clients. These differences, if not addressed in the planning, can lead to poor execution of marketing plans.

If you are depending on the acquired firm to develop client relationships independent of your existing client base, look at how well they organically develop new clients now. Many financial services firms are attracted to CPA firms in business combinations because they perceive that as a means to overcome the poor practice development results they are achieving on their own. A change in scenery may not result in different outcomes. It is often better to acquire a firm that has demonstrated an ability to grow organically prior to the combination if that is an important aspect of your business case.

Financial services firms may use different marketing tactics to acquire new clients. These tactics may be considered too aggressive for your culture. Or they may introduce your firm's brand to segments of the marketplace you are unaccustomed to or not interested in pursuing. Develop a complete understanding of the types of clients the acquisition candidate serves and targets in their marketing. Are these the types of clients you want to serve? Will they fit in well with your firm's culture? Are your other services relevant to them? The marketing tactics and financial products and services that are appropriate for business clients differ dramatically from those designed for individual clients. A financial services firm whose existing clients are primarily of one type will find it difficult to transition to the other and may not make a good acquisition or merger candidate.

If your firm doesn't offer financial services to its clients now you undoubtedly will have clients and referral sources that work with you because of that fact. When you start offering those services, some of those relationships may be lost because you are now considered a competitor. The typical conflicts will be with other financial services professionals (like stockbrokers or financial planners), insurance agents, and bankers. This conflict is often one of the first excuses that CRMs use for not following through on their commitments to the initiative. Therefore, it is important to get this issue out on the table early so the commitments made by CRMs are based on the knowledge that there may be this downside. The more visible your intended marketing tactics, the harder this issue is to avoid. If you have this issue, consider the following:

- **Identify the potential conflicted relationships.** Have each CRM in your firm make a list of specific potential conflicted professionals that are clients, referral sources, or centers of influence.
- **Quantify the potential downside for each conflicted relationship.** What is your potential lost fee income from each of these clients if they leave you as a result of the conflict? What are the fees from annual referrals you receive from each of these relationships? Include the worst case scenario to determine the total potential investment in this initiative.
- **Consider talking to the potential conflicted relationships about your plans even before you undertake the merger.** This can have two benefits. You may find that they don't perceive a conflict after all. They also may be willing to help you by becoming an advocate or partner in your venture.

A similar problem probably exists for the acquired firm. Most financial services firms have relationships with other CPA firms that will be affected by your merger. Make sure both parties have a complete understanding of the scope of those conflicts and how they will be managed.

## **Culture**

There are potential significant differences in culture aside from marketing issues that you should consider before you decide to move forward. Culture is an issue in any merger and it can have a devastating effect if not addressed up front. However, there are five specific cultural issues you should address when combining a CPA firm with a financial services firm.

**Performance management.** Most CPA firms use measures of input, primarily time spent on certain activities (most importantly chargeable or billable hours) coupled with some measure of output such as realization on charged hours, as a means of measuring performance. Most financial services firms measure performance strictly on output, normally revenues generated from client service or sales, as a means to measure performance. As a result, many financial services firms don't keep timesheets to measure performance. Make sure the parties have agreed in advance how performance will be measured. Also, make sure this is understood throughout both firms to avoid misunderstandings.

**Compensation.** This issue is at the top of the list for any merger because compensation concerns are so tangible and personal. The most important aspects of compensation are the amount of risk borne by the associate or principal in their compensation plan and the specific performance the compensation is tied to. If your current compensation plan contains high base salaries relative to expected total compensation and bonuses that are based on primarily group performance it may be difficult to assimilate with a firm that uses low base salaries and bonuses based on individual performance.

**Client service management tactics.** Make sure you understand how relationships are managed in the acquired firm. Your CRMs may be unpleasantly surprised if the two firms have significantly different approaches. For example, in your firm owners or other senior management may be very involved in all aspects of client matters. This puts a decision maker directly in the client relationship which clients appreciate especially when problems arise. However, the firm you acquire may rely on the principals of the firm primarily for practice development or investment management expertise. Client management may be the responsibility of lower level associates. This approach can be effective as well, but your CRMs may lack confidence in it and they may resist referring their clients to that model.

**Roles of support personnel.** The term "assistant" may have dramatically different meanings in the two firms. Assistants in financial services firms sometimes are licensed professionals that have significant day-to-day responsibility for client management or product solutions. As a result, their compensation and authority may differ dramatically from that of an assistant in your firm. Make sure you fully understand each person's role in the acquired firm and position them in the new firm appropriately.

**Seasonality.** Many accounting firms' seasonality leads to modifications in the way they operate during the busy time of year. Associates are expected to work more hours. Activities such as marketing are suspended to make way for client service. Certain types of client services might be deferred to after the busy season. Financial services firms often do not have the same spike in services and as a result may not be prepared to modify their operations during that time of year. Discuss this issue in advance and prepare for it. Generally, the best time to market financial services to your clients is during tax season. If you aren't accustomed to taking the time to cross sell during tax season determine how you can change that tradition. Otherwise, you will be missing some prime opportunities to introduce these services to your clients.

### ***Regulatory and organizational***

Develop an understanding of the level of licensing and regulatory oversight you will be subject to before you proceed. Obtaining instant licensing and processes is an excellent reason to pursue an acquisition or merger with a financial services firm. However, consider the following:

- **The type of licensing your firm and its professionals have dictate what products and services you can offer.** Make sure the acquired firm has the required licenses to offer the services you have in your business plan or make arrangements to obtain the appropriate licensing.
- **Securities licenses can only be held by one brokerage firm.** If you have existing professionals whose licenses are held by a brokerage firm that is different than the one your target acquisition firm uses, you will find it awkward at best to deal with more than one broker. You should at least consider consolidating with one broker. This can be difficult and can result in the loss of revenue during the transition if it isn't handled properly.
- **Clients acquired must positively affirm the transfer.** Two accountants can merge or sell client lists. Although the clients have the final say in whether they choose to continue working with the successor firm, the two firms can usually assume that the clients will move to the successor unless they give notification otherwise. This is not the case with financial services clients where fees are attached to assets. In that case, the merger involves transferring assets to a successor firm or a new broker the successor is affiliated with. Clients must individually and affirmatively agree to transfer the assets and the transfer must actually be consummated. Until this happens, the successor firm is essentially without the client and certainly the revenue stream. The process can take several months. Planning ahead is very important.
- **Perform due diligence early in the process.** As soon as you identify an acquisition candidate, look into the backgrounds of the firm and its principals. Because this industry is so highly regulated you can obtain a lot of information from a Google type search on the internet and by accessing public databases for organizations that license and regulate the firm and its principals.

You should also give a lot of consideration to the new organizational structure of the successor firm. There are advantages and disadvantages to operating the financial services practices in a separate entity.

The advantages of a separate entity include:

- **Risk isolation.** A separate entity may compartmentalize the different risks the financial services business has from your other services reducing the overall risk to the owners and the cost of risk mitigation such as insurance.
- **Performance management is simplified.** Although a separate entity is not necessary for separate accounting, it generally makes measuring the performance of the financial services business easier. This can be critical to appropriate determination of compensation.
- **Regulatory issues.** If your financial services offering will require licensing of the firm as well as the individual professionals, a separate entity may be necessary.
- **Brand considerations.** A separate financial services entity will allow you to operate under a brand name that highlights that area of service which may be beneficial for marketing purposes.
- **Professional ethics.** A separate entity can result in better compliance with ethics conflicts you might have with your core services clients.

The disadvantages of a separate entity primarily relate to a less integrated culture. This can result in:

- **Confusion and awkward relationship management for clients.** Clients will be served by two different brands and service teams. Extra effort may be necessary to assure a seamless delivery of services which, if achieved, normally results in higher client satisfaction.
- **Acceptance of cultures by associates in both firms.** Associates in both firms may be less likely to feel a part of the combined entity. This can lead to a lack of execution of the global business plan.
- **Increased costs.** Marketing and administration costs will be higher. Marketing costs will be especially affected in order to support a second brand name.

Accounting firms routinely acquire books of business to increase their client base for core services. Firms that already have strong financial services practices and excess capacity might consider acquiring financial services firms with similar service offerings as a means of increasing their book of business. However, firms with that objective should consider acquiring accounting firms that do not currently offer those services and that have client bases that are good candidates for cross-selling. Practices with high net worth individual clients are good examples. These types of acquisitions are generally easier to find, easier to consummate, and can be less costly. A significant return on investment can be obtained from providing the acquired clients the core services they are accustomed to with substantial upside being in the cross-sold financial services.

There are many valid reasons to pursue an acquisition or merger with a firm that already offers financial services as a means to create or expand the team that provides such services in your firm. If you do not have the experience or licenses a merger, acquisition, or some other form of affiliation is typically the fastest and can be the least expensive way to get started. This type of merger or acquisition can be a lot more complicated than merging two accounting firms. It is normally good practice to engage experienced professionals to provide guidance for any merger and it is even more critical with this

type of business combination. A well-planned, thoroughly executed acquisition or merger strategy will avoid potential costly errors.

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