

The New Economy and the Future of the Accounting Business

By Peter D. Coburn, President and Founder of Commercial Logic.

This article takes a high-level view of the business of accounting and its prospects for the future.

Although the business of accounting was expanding through 2008 and has weathered the recession relatively well, our view is that the accounting industry is going through a sea-change more profound than any we have seen in the last twenty years.

This view is not universally held. Many, perhaps a majority, of partners and shareholders in accounting firms take the view that (a) the worst of this recession is over and (b) we need but wait for better times to return. My response to (a) is "maybe," and my response to (b) is "you may wait a long time!"

If the accounting business is indeed experiencing a fundamental shift, what strategic actions should a firm take to adapt successfully to the new business culture?

Accounting firms have had a good run for most of the last decade, primarily due to two factors: Sarbanes Oxley and the work it created for accounting firms and the dramatic expansion of the economy from about 2003 to 2008. This growth had peaked by the time of the crash in late 2008.

Since then the great recession has significantly reduced opportunities for CPA firms -- as most of you reading this article will attest. A number of businesses failed in the recession, reducing the client base for corporate audit and tax work. Those companies that remained cut back on discretionary services and many shopped aggressively for discounts on tax and audit services. In this they were encouraged by the Big Four and other large firms that cut prices on audits by as much as 70%. Meanwhile the cheaper alternatives offered by H&R Block and other tax preparation companies and by do-it-yourself tax software from Intuit and others made deeper inroads to the individual tax business of CPA firms.

Despite this, the accounting industry has held up remarkably well. Revenues for 2009 and 2010 were roughly the same as 2008 -- which is a lot better situation than most industries have experienced. While accounting is not recession-proof, companies still need annual audits and both companies and individuals continue to need to file taxes. Many firms have developed wealth management divisions catering to high net worth individuals and this and other consulting services have helped to fill the holes left by the ebbing tide of the recession.

This has left many CPA partners and shareholders with the impression that all that is needed is to wait out the recession and look for better days ahead. While that is to some extent true -- business will surely improve in the next up-market cycle -- this article takes the view that there is a fundamental shift occurring in the accounting business and that the good old days of the first decade of this century are never coming back. If this is true, it follows that accounting firms must learn to adapt and compete in new ways -- or be absorbed into a firm that can do so.

Roughly 80% of the business of accountants is annually renewable tax, audit, and accounting work. Renewable work is the gold standard, because there is a strong tendency for the client to stay with the CPA year after year. But there is stiff competition for that renewable business, not only from larger firms cutting prices to "buy the audit business," but also from companies like Block and Intuit that have commoditized individual tax services. The current recession has changed the mood of the market to focus on reducing cost, so accounting firms are more vulnerable to client attrition than ever before.

I suggest that accounting firms are chasing a shrinking demand for tax, audit, and accounting services and that this situation may pertain for the foreseeable future. Furthermore, there is evidence that the current sensitivity to price is a shift that may be with us for a long time.

If this is so (and you need not agree) what general strategies can a firm adopt to respond to these new elements in our market? I suggest there are just two ways to respond:

- Become more competitive with the services you currently offer and the market that you serve.
- Expand your service offerings into less competitive areas.

Note that these are not unworthy things to do even if you believe that the next boom is right around the corner!

Strategy 1: become more competitive. As never before accounting firms are faced with the need to retain the clients they have and to move assertively to acquire new clients. This has resulted in a renewed interest in client relationship management and business development at many firms, which is a laudable approach. Certainly there is great room for improvement in these areas in much of the accounting industry.

This is a pretty obvious approach, but is there a problem here? Well, yes. Accounting firms are not generally in the habit of devoting important energy to marketing their services. There is general agreement that it is the partners who have the greatest potential to bring in new clients, but these are busy people who are generally compensated based on the business they are currently managing rather than the new business they generate. It is tough to sell a partner on the idea that he or she must reduce their billable hours by 10% to focus on recruiting new business. As a result we see the installation of CRM systems which are then left to idle and the employment of one or two people to “do marketing.”

It is not enough to make half-hearted gestures in the direction of better client relationship management and business development; it is required of most firms that they change their corporate cultures. For example, one firm hired a director of marketing with the job description of “building a marketing culture into this firm.” In combination with other initiatives, including especially the commitment of top management, this has a chance of succeeding. At least it shows a understanding of the real problem with the strategy of improving the firm’s marketing. In the immortal words of Pogo, “we have met the enemy and he is us.”

Another cultural change that may be needed to prevail in the new economy is to replace the traditional partner governance structure with a more responsive corporate structure. This is not a new idea and many firms have already moved in that direction, some even hiring a CEO who is not an accountant to manage the business. But again, it is not enough to change the labels from “partner” to “shareholder,” the partner culture itself must change and that is a more difficult proposition. How does a firm change its own culture? It is a difficult proposition because we are largely unconscious of our own corporate culture and how do you change something you have difficulty perceiving? It requires an outside perspective and it is a tougher proposition than it sounds. Habit may be the strongest force in the universe, which is why most diets fail, for example.

We shall have more on changing the fundamental culture of a firm in a subsequent article.

But becoming more nimble and more competitive will not address the core issue: the market for traditional accounting services is shrinking. Good marketing will make your firm more competitive (and that is highly important), but it will do nothing to expand your market.

Strategy 2: expand your market. Expanding the market boils down to offering a new set of services. Traditionally these have been *business consulting* or *management advisory services*, which means working with companies and HNW individuals to evaluate business or financial issues and advise on what should be done to resolve the issue. About 20% of the business of accountants is already in this area, which makes good use both of an accountant's business and financial skills and the CPA's credibility as a "trusted advisor." But the consulting or management advisory business for accountants has been in play for a long period and is also very competitive. Wealth management, to provide one example, is served by the investment banks, hedge funds, individual financial planners, and the trust department of nearly every bank in the country.

Thus the question becomes: is there a service area that is not currently provided by other CPA firms or other well-entrenched competitors and which draws on the skills and credibility of the trusted advisor? *Business coaching* meets these criteria.

What is business coaching and how does it differ from business consulting? *Business consulting* is what most CPA firms provide under the heading of advisory services. It is about evaluating a business or making recommendations to improve it. Management is left with the task of actually implementing the recommendations. Unless the recommendations are trivial, they will often involve the company in some profound and uncomfortable change, which they haven't the training or time or inclination to manage. *Business coaching* is the service designed to bridge that gap.

Business coaching is increasingly accepted as an important service by the business community. There is a rising demand for these services. The recession has forced companies to re-evaluate their business and culture and to embrace a need to change those things.

Business coaching is as yet a very open and unstructured market, primarily served by small companies, most of which are engaged in *leadership coaching*. Larger companies, including some of the *Big Four* accounting firms, are starting to take an interest, but any sort of meaningful market consolidation is a decade or more away.

Business coaching is lucrative: a team of four coaches can typically bill \$1M annually, though this is subject to regional variance. Sound interesting?

Business coaching has the potential to make the difference between success and failure for your clients. This not only increases their loyalty to you but has the potential for increased traditional accounting business for your firm as a consequence of their success and growth. More referrals from your clients are a reasonable expectation from a successful coaching practice. What's not to like?

Question: if this service opportunity is opening up and the Big Four are taking an interest (and in the process validating the importance of business coaching), can you afford to ignore this market?

Question: if you wanted to open a business coaching practice, how would you go about it? How would you train your people to be business coaches? How could you control and validate the quality and professionalism of your offering in this new area? Where would you go for such training? Until recently there has been no good answer to these questions.

To meet this need Commercial Logic has partnered with *Shirlaws*, a global business coaching company with US headquarters in San Francisco. Shirlaws USA not only offers a cadre of coaches and trainers, but also has a set of IP models that serve to capture and focus the work. Shirlaws has provided high-quality business coaching services world-wide for many years and has organized its experience and IP into a business proposition that they can offer to firms that want to add highly professional business coaching to the services offered to clients.

Shirlaws' assessment is that the demand for business coaching is expanding faster than Shirlaws can expand to meet it. Shirlaws has therefore concluded that the best way to capture this market is to work with like-minded CPAs that want the best for their clients -- rather than set up Shirlaws offices in every major US city.

If creating a new stream of revenue from your existing customers is of interest to you, please call Peter Coburn, President of Commercial Logic, for further discussion and introduction to our Shirlaws partners.

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