Accounting Firm Mergers

The Urge to Merge
Alignment for Improved Firm Mergers/ Acquisitions

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The article focuses on the significance of merger and acquisitions for accounting firms in Australia. According to the author, the expected benefits of mergers include geographic expansions, gaining scale, adding new services, gaining access to capabilities and addressing issues in one or both firms. It is stated that the possibilities of a successful merger can be developed through merger benefit adjustments, merger-fit and integration approach.

Historically mergers and acquisitions (M&As) have been an important strategy for accounting firms to expand geographically, gain office scale and add new services.

Current M&A activity is substantial. The ‘Big four’ are seeking to expand their presence in the middle market. For example, Deloitte recently snatched the Melbourne office of BDO and the Sydney office of Horwarth. The second tier firms are trying to get scale and specialist skills to take advantage of ‘Big four’ conflict issues. Publicly listed consolidator WHK Group has acquired around 100 accounting and financial service firms over the last nine years and Count Financial has recently commenced a new consolidator, CountPlus.

For small firms, M&As are a potential antidote to partner succession issues, difficulties recruiting staff and keeping up with legislation and technology.

Not all accounting firm M&As have achieved their objectives with many causing substantial pain for all of those involved. Expected benefits have often proved to be illusions. Some merged firms have lost key clients, partners and staff and, in extreme cases, seen whole offices defect. New services have been found to be a poor fit and divested shortly after the merger. After some mergers, an ‘us versus them’ attitude can exist and result in culture clashes for years post merger.

This article argues that the prospects of a successful merger/acquisition can be improved through aligning expected merger benefits, merger firm fit and integration approach before the deal is finalised. This alignment is shown in figure 1.

EXPECTED MERGER BENEFITS

Firms merge for many reasons, but overall there is generally an anticipation of merger benefits where the combination will be greater than the individual firms.

Expected benefits from mergers can include:
• Geographic expansion: adding offices to service or win clients with multi location operations,
• Gaining scale: strengthening capabilities in offices, getting large enough to service the ‘big end of town’, combining and reducing spending on technology, marketing, training, methodology development and administration,
• Adding new services: cross selling services between the clients of the merging firms,
• Gaining access to capabilities: including people, process, clients and systems,
• Addressing issues in one or both firms: structural and financial issues can include partner succession problems or the need to exit a high unit dominant senior partner or non performing ‘dead wood’ partners.

It is important during the pre-merger process to clearly define realistic expected benefits, net of integration costs. The success of the merger/ acquisition will be measured against these expectations. Benefits expected are also a crucial input into analysing strategic fit of a specific potential merger partner by determining capabilities.

FIGURE 1 ALIGNMENT IN FIRM MERGERS
Accounting Firm Mergers

required. The benefits expected drive the need for integration approach to release those benefits with significant benefits generally requiring substantial post merger integration. Agreement of expected benefits by the partners of both firms during the merger process is more likely to result in commitment and support during the pain of integration.

MERGER FIRM FIT

This includes the strategic and organisational fit of the merging firms as discussed below.

Strategic Fit

Strategic fit is as important as the stand alone quality of a potential merger partner and the attractiveness of new services and markets. Strategic fit is the degree to which the alignment of the services, market focus and capabilities of the potential merger partners would enable the expected merger benefits to be achieved.

For example, if the planned benefits of the merger are building scale or geographic reach in order to sell services to large corporate companies it is important to understand whether both firms have the required specialist skills. Merging firms where the professionals have generalist skills focussed on SMEs does not necessarily create required specialty skills. Where cross selling benefits are expected it is vital that the merger partners provide services that are understood, valued and at a quality perceived by the other firm partners as worth introducing to clients. It is also important to ensure that the firms are not potentially worse off merged due to conflicts in the services provided.

Mergers where firms don’t have required capabilities make achieving expected benefits impossible without further mergers or internal development of required capabilities.

Organisational Fit

Organisational fit is the degree of alignment of the way each of the merging firms operate compared to each other and compared to how it is planned for the merged firm to operate. The way of operating includes structure/ systems fit and people fit.

Structure/ systems fit includes factors such as how the firms are governed, the amount and methods of calculation of partner compensation, the roles, rights and expectations of partners, organisation structure and sophistication of processes and systems.

People fit includes the corporate cultures of the firms with some of the key attributes being: the degree that services are standardised versus entrepreneurship, individual orientation versus team based approaches, lifestyle versus profit generation and farmers of existing clients versus hunters for new clients. Also important to people fit are the skills and experience of partners and staff at each level in each of the firms.

Low levels of organisational fit can result in resistance that limits the degree and speed which integration can be performed affecting the ability to achieve expected merger benefits. Poor organisational fit can also result in substantial post merger difficulties such as culture clashes.

INTEGRATION APPROACH

Integration is the physical combination of the people, processes and systems of the merging firms. There are many approaches to integrating firms. The approaches can range from keeping the firms relatively separated, such as a federated model or one firm as a division of the other. At the other extreme is fully integrating by co-locating the firms, moving to one set of common processes and systems and combining each of the equivalent business units of both of the firms.

Integration decisions need to take into account the trade-off between expected benefits and the costs of integration. Integration activities can have a significant cost in terms of expenditure and distraction from client service activities. Costs of integration can be extremely high where there is poor organisational fit. Significant clashes can result when partners and staff from firms with different ways of operating and cultures are thrown together during integration. Large differences may make it impossible to develop common processes and systems without a compromise for both firms. Inability to achieve planned integration can significantly reduce merger benefits achieved.

It is important that the planned approach to integration is considered during the merger deal process. This includes agreeing major integration decisions such as the name of the new merged firm, whether firms will be co-located, how the firm will be structured and who will lead the firm and each division and whether one firm’s processes and systems will be utilised, the best of both firms will be used or new processes and systems developed. This enables assessment/ adjustment of expected benefits, better assessment by partners of both firms of the organisational fit and commitment to the integration process when the deal is done.

CONCLUSIONS

Clearly defining, aligning and communicating expected merger benefits, member firm fit and integration approach prior to completing the merger enables more realistic views on whether a merger should proceed. Completed mergers will have greater commitment through post merger integration.

Achieving substantial merger benefits generally requires strong strategic fit and significant post merger integration of the firms. High levels of integration are more likely to be successful when there is good organisational fit between the firms.

To avoid poor merger results it is vital that action is taken where either strategic fit or organisational fit are lower than required to achieved planned integration and expected benefits. This may include adjusting post merger plans and expectations to reflect the reality or abandoning the potential merger and seeking a better-fit partner.

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