

2009-2010-2011: Merger Mania

By Jay N. Nisberg

The CPA community has never before experienced the flurry of merger activity it has seen in the past 18 months. Suffice it to say that the number of mergers is well above the predictions, and the activity is likely to continue at the same staggering pace for at least the next 18 months. It almost seems that everyone is a buyer or a seller! Given this level of activity, it is fair to ask what are the “buyers” and “sellers” looking for in a deal and whether their motivations are different. I do not think they are.

The six most common reasons for merging

The following six points summarize in a nutshell the underlying reasons these deals happen:

1. *Succession Planning.* Many partners are very concerned about the next generation of management. Partners on the cusp of retirement look behind them and wonder who is left that can bring in more “new” business, service existing clients and lead the firm to the next level. There are many uncertain sellers out there who do not believe their bench is strong enough to continue their legacy. Their conclusion is to merge it up, over or sell.
2. *Leadership.* While firms may have great clients and strong technical service partners, they may not have the visionary or the “motivator” who can keep the inspiration alive. As a result, they feel the

need to merge or sell. A lack of leadership is a void that no organization can sustain and expect to demonstrate growth and continuity.

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3. *The Exit Strategy.* A number of sellers are very much consumed with the belief that “all businesses are built to be sold.” Whether you subscribe to this philosophy or not, many sellers are looking for the instant gratification of cash. Unfortunately, there are very few cash transactions these days. Most buyers are looking for a longer-term payout and lower down payment. There is one consolidator who is still doing lucrative cash deals, but they are few and far between. Large multiples are also rare. (The classic scenario of 1 to 1.2 times purchase price on gross fees never made sense to me: as a seller would actually end up paying for their own practice in a period of five or six years.)
4. *Quality People.* Sellers often claim they just cannot find

good people to buy into their practices, and they expect that by merging or selling they can obviate this need. This reasoning may have been valid two or three years ago, but not today. While smaller firms generally have a more difficult time competing with larger local and regional firms, there is a larger pipeline of experienced people, and I believe that, with current economic trends, this trend is likely to continue through 2010 and 2011.

5. *Realization, collections and accounts receivable.* The current economic tide is definitely causing client defections, terminations and dissolutions, which are all good reasons to make CPA firm owners nervous. It is getting increasingly difficult to collect fees, get the billing rates firms charge and develop new business. These issues are all causing firms to consider merging. But why would a seller think those problems go away at a larger firm? Unless that firm has a strong industry or service-area specialization that can help mitigate the problems, they will still be there.
6. *Long-term Financial Security.* A good many mergers are strongly motivated by sellers who simply fear the ability to maintain the long-term value of the practices and believe it is in their best interest to let someone else create that financial security for them.

Common values are the key for successful mergers

Firms have all kinds of reasons for merging; the six above are the most frequently articulated concerns. Once it is determined that merging is the option a firm wants to pursue, conducting a due-diligence evaluation of the deal is the next step. Many practitioners say they are looking for a merger of “common cultures.” Culture is often cited as the most critical ingredient of any successful merger. But a common culture can be elusive. In many firms, the culture varies between departments or different firm locations. Once you drill down, a location can simply mean a different floor in the same building.

The true ingredient of success is not common culture, it is common values. Common values are the standards and principles upon which a firm is built. A firm’s culture is the environment in which it implements those values. Values, in this sense, refer to the level of quality at which work is measured, the way a firm determines how it bills and collects and the timeliness of both.

Don’t overlook the obvious

Much is made of the due-diligence process when effectuating a merger or acquisition. However, this process is often underutilized. Unless there is some glaring flaw, firms that are attracted to each other often want to “do the deal” so

badly that they ignore or overlook the small stuff when assessing the quality of the other firm’s work. It takes a major concern on the quality of work to overthrow a decision to put two firms together. One deal I was involved in never happened because a small firm being acquired by a national practice actually asked to perform a due-diligence activity on the national firm’s clients. They were immediately rebuffed and told that their request was absurd. The smaller firm happily walked away from the deal.

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While many firms dig deep into the quality of a firm’s work and may spend anywhere from one half to one full day at the other firm’s offices, the process is usually an affirmation that there is nothing major that should end discussions. Why this is the case lends itself to a preliminary assumption on both sides that they have a preconceived notion that the other firm’s work is of a high quality or they probably would not have started discussions in the first place.

An “Aha!” moment

My “aha” moment on this issue came when Jeffrey Wein-

er, Managing Partner of the Marcum Group, presented his theory on culture to a recently merged audience of partners. He noted that culture, like attitude, is very hard to define and can be very hard, if not impossible, to change. Consequently, his goal was to get all offices, partners and staff sharing the same ethical and moral values. He was convinced that this was the factor that would make his firm’s mergers highly successful.

As a result of this “aha” moment, I recognize that while it would be nice to have a common culture, that may be an unattainable goal, at least at the beginning of the merger process. It will be much more beneficial to have firms focus on working toward a set of common values that expects everyone to concentrate on doing the right thing for the firm, its members and its clients. Common values will lead to greater success with mergers—and maybe even create a common culture.

About the author: Jay N. Nisberg is an internationally known consultant to the CPA community. Jay is prepared to help practitioners think through these questions and re-engineer their firms to be competitors in the firm of the future and the world of tomorrow. Jay can be reached at his Ridgefield, Connecticut, office by calling: 203-743-2567 or through e-mail at jaynisberg@snet.net. ♦