SMALL FIRM SOLUTIONS

WINNING STRATEGIES FOR PROFITABLE FIRMS

VOL. 3 • ISSUE 2 | SPRING 2009

AICPA

IN THIS ISSUE

HOT TOPICS FOR SMALL FIRMS

FROM JAMES C. METZLER, CPA, AICPA VICE PRESIDENT, SMALL FIRM INTERESTS

How was your busy season? This issue of Small Firm Solutions *will examine the ups and downs of the most recent season. In our News Update section, we'll also offer great ideas from the small practitioners on our* Small Firm Solutions *Editorial Advisory Board on how to deal with the challenges and take advantage of the opportunities in the current economy. One general conclusion is that the small firm advantage is still working for our practitioners. Because of their greater flexibility, their deep relationships with clients and their position as a low-cost alternative, many smaller firms have been able to hold their own and even thrive in the current recession.*

I'd like to update you on some of the developments that are or will be affecting smaller firms soon.

The ARSC Reliability Project. The AICPA Accounting and Review Services Committee has published exposure drafts of proposed Statements on Standards for Accounting and Review Services that would, among other things, permit a CPA to express a review conclusion on financial statements when that CPA is not independent from the client by virtue of some of the nonattest services they provide. The proposed SSARSs would also harmonize the review standards with the International Auditing and Assurance Standards Board's International Standard on Review Engagements No. 2400.

What it means for small firms. This is an extremely significant development for small firm practitioners. Many have long believed that when preparing financial statements for smaller, private company clients, the reliability of the financial statements is more important than the practitioner's independence from the client (not including financial relationships). This new guidance will make it easier for CPAs to provide needed services to small private clients. I urge you to review and comment on the ED by the July 31 comment deadline.

Internal Revenue Code Section 7216. The Institute understands the many difficulties caused by compliance with Section 7216. The AICPA has been extremely active in letting the IRS know about the many consequences that this onerous regulation poses for practitioners. We are working with IRS officials to create a series of FAQs that explain this unnecessarily complicated privacy regulation, which became effective on January 1. I have made this a top priority because of its impact on our small firm members.

Why it's important for small firms. The regulation requires tax preparers to obtain written permission from the taxpayer before they disclose or use tax information. It must be considered when making disclosures to third parties, such as bankers or investment firms, when outsourcing returns or using retired partners or temporary staff to prepare them, and even when personal information is used for sending newsletters and other information to clients. In addition, 7216 prohibits retroactive use of written consents and obliges practitioners to establish a specific period for the consent (if none is set, the consent expires in one year), a mandate that we find bewildering. Equally bewildering to practitioners and clients, tax preparers must obtain permission to share information essentially with their own colleagues in affiliated firms.

Our recommended FAQs address these issues, establishing answers to common questions that respect the spirit of the rules without creating needless roadblocks for CPAs that will hinder their ability to effectively serve clients. The regulation comes at the request of privacy groups, but as part of our behind-the-scenes advocacy on behalf of small firms we made a concerted effort to explain to the IRS the unintended impact on practitioners. You can find out more on the AICPA site, including a practice guide on the subject written before these FAQs were developed. We will keep you updated on our further efforts on this front.

Economic Crisis Resource Center. I hope you have all checked out the many informative and practical resources on the AICPA Economic Crisis Resource Center, a comprehensive source designed to help our members weather the bad economy. Of particular interest is the blog on small firm issues written by senior technical manager Mark Koziel from our PCPS team.

The site is also the home of the CPA Job Finder, the official job posting site of the AICPA. To help you find the staff you need, firms are allowed to post jobs free. ■

James C. Metzler

NEWS UPDATE

How CPA Firms Are Faring in Tough Times

What's the most powerful tool that practitioners can use to weather a rough economy? The Small Firm Advantage. During a recent teleconference with the Small Firm Solutions *Editorial Advisory Board, we heard again and again that the basic attributes that define any small firm are also among the greatest assets during a recession. A small firm's size allows it to adapt more easily to changing business conditions, for example. Long-lasting relationships with clients enable practitioners to identify the best answers for business owners eager for solutions to the challenges they face. And small firms' low overhead makes it possible for them to position themselves as the low-cost alternative at a time when cutting expenses is a top priority for companies and individuals.*

Our Editorial Advisory Board is made up of practitioners from very small firms throughout the country. What else did they have to say about their experiences during the recent busy season and their plans for the future? Here's a rundown of some key observations.

The Economy and the State of Small Firms

- The state of small firms is generally good. Many firms are thriving, in fact, depending in large part on their client base. Location is also an important factor. Many areas that did not experience a meaningful boom during the last decade have been spared much of the crash. Banking, investment firms, credit unions and construction are among those particularly hard hit, however. Some firms with large niches serving these industries are struggling as a result. In the Midwest and other sections heavily dependent on the auto industry, many are dreading further problems in that sector. Service businesses, such as health care, for example, do well, with the exception of architects, who have been hit by the construction slowdown.
- Clients in good financial shape can still borrow, but the credit terms have become stricter.
- Firms generally did not report losing clients for fees, but rather because a client went out of business.
- Bernie Madoff was not the only bad apple in the investment world. CPAs can perform a needed service by reminding clients about the potential pitfalls in investments, particularly older individual investors, and offering objective feedback on their choices.

Practice Opportunities

- Some smaller businesses are cutting bookkeeping and payroll staff and giving the work to their local CPA firm. Practitioners can become the lower-cost outsourcing solution for accounting and any number of other services as companies retrench and look for cost savings.
- Many clients are doing well but remain anxious because they are waiting for their luck to turn. Some are cautious in anticipation of the government's next tax or regulatory moves. Firms can help by listening to their concerns and offering strategic planning or similar services.
- Compilations may become a growing practice area. Many small business clients now need this service in addition to tax returns in order to get or maintain financing. This is part of an overall trend creating greater demand for compliance and assurance services.
- Given the stronger focus on economizing and cutting unnecessary costs, clients are more interested in tax planning and other services that can give them a feeling of greater control over their financial lives and potentially put more cash in their pockets.
- There is a looming shortage of peer reviewers, another development that presents a practice opportunity for smaller CPA firms. Many who began working as the first wave of peer reviewers are now retiring. This niche is not difficult to enter and easy to market. Teaching courses on peer review at local CPA societies is one great way to expand into this area.

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- While re-examining their business model, smaller companies are becoming more aware of the importance of succession planning, which also opens opportunities for estate planning.
- International opportunities present another opening for CPAs. Firms can, for example, offer controllership services for companies that want a U.S. office.
- Business valuation and litigation support continue to be busy niches.
- Practitioners recommend scheduling client meetings immediately after tax season as a great way to maintain contact and get a sense of the client's situation and near-term plans. CPAs should initiate the contact.

Practice Management

- As busy season ends, a firm's collection problems may not yet be over. Many firms have concentrated on partnerships and larger business clients during busy season and put individual clients on extensions. That leaves open the possibility for collection issues when this second wave of returns is done.
- One great idea for avoiding collection problems: Accept credit cards. Firms receive immediate payment and can promote the idea as a convenience for clients.
- The season was more stable for some firms because they are experiencing less turnover than in the past as people hold on to the jobs they have.
- The recession has raised interest in purchasing accounting firms. As firms lose clients in some industries, they seek out other practices with different client bases. (For more on mergers & acquisitions, see the Practice Management/M&A column in this issue.)

Strategic Planning

- Marketing is cool again. Firms should review their value proposition and consider how to communicate it in their market and to existing clients. Process improvement has also become popular once more as CPAs attempt to streamline operations. (For more on process improvement within firms, see the Productivity Boosters column in this issue.)
- In fear of business declines, some firms have mistakenly reacted by slashing and burning through expenses rather than asking partners to focus on marketing. It's important not to lose talented people or compromise good practices now so the firm can be in a strong position when the economy improves.
- CPAs are in a good position to help clients make sense of the contradictory—and sometimes inaccurate—reports they hear on the news.
- Service still matters. If firms deliver as promised and offer tangible value, clients will remain with them. ■

PRODUCTIVITY BOOSTERS

Finding the Silver Lining

By Roman H. Kepczyk, CPA.CITP

We are all painfully aware that the economy is affecting our businesses. Most of us have been through previous recessions and know that things will eventually get better. Unfortunately, since business owners are inundated with so much external bad news, many forget that in every downturn there are companies that not only maintain their business position but actually thrive. They do so by adapting their processes and products to better meet the needs of their customers and clients and constantly communicating with them. Downturns provide a unique opportunity for organizations to honestly evaluate their products, processes and training, and improve on them so that their business is well positioned to thrive when the economy turns around.

You can make your own opportunity by taking the time to communicate effectively with your clients and business partners in a positive light to determine how you can continue serving them or provide products they need. Open communications spotlight what can be improved and help to cement relationships. If a product or service is not delivering everything that is promised to or needed by the client, companies must either fix them or find another way to meet the customer's need.

Firms should consider their internal processes to evaluate what changes can be made to streamline production or service delivery. In today's environment, leaders of every organization know they must be faster and more nimble, so a downturn provides an opportunity to evaluate better processes when there is time to think, assess and implement. This often entails installing either new or updated applications, equipment or infrastructure, which are often available at a more competitive cost or terms during a downturn.

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Finally, once the firm has implemented better production or service processes, it is critical to provide training and documentation. Doing this when there is time available will ensure that the new processes or services are actually captured in written format, which will make it easier for your staff to use it in the future, when it is really needed. Other added benefits of good documentation are that your firm will retain this knowledge for new hires and written procedures further promote standardization and efficiency.

Yes, times are tough, but instead of focusing on the negative economic reports from the media, firms will improve their chances of future success by focusing on what they can improve and build upon, which is the job of all business owners during these difficult times.

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PRACTICE MANAGEMENT/M&A

The Value of a Smooth Transition in Tough Times

By Joel Sinkin

During a time of economic uncertainty, both buyers and sellers will be giving extra scrutiny to all aspects of a merger or acquisition. A key measure of a deal's success is the percentage of clients retained afterwards. To plan for the highest level of retention possible, start by considering why you have your clients. Most are unaware of your competency level. They trust that you are knowledgeable and capable, but the key word is trust. You are their most trusted business adviser and this trust can be taken advantage of, in a professional and ethical way, and should not be feared.

Most of that trust can be attributed to the client's personal and professional comfort level with you. You can use that trust to transition your clients to your successor, a partner or a staff member.

The Importance of Continuity

The two major keys to a successful transition plan are maximizing continuity and focusing on what clients gain, not what they lose. Let's start with continuity. Change is a daunting and scary concept to most people, particularly with so much else changing around us in the midst of a recession. Your clients are comfortable with your approach to service, billing and other concerns. If your successor firm dramatically alters that approach—through radical changes in service or fees—you likely chose the wrong successor and there will probably be lower retention of your client base.

That doesn't mean the new firm has to mirror your policies forever. The old approach can be altered over time, but gently. Most initial changes by a successor firm should be internal and invisible to the client. However, if the new firm leaders tell a client who traditionally gets a personal visit that they now must mail in their work, they clearly risk losing that client. The same is true when a client who is accustomed to dealing with a partner now must deal with a junior or if clients' billing procedures are substantially changed.

What's in It for Me?

Clients will accept the idea of the merger or acquisition if they believe it is in their own interest. Be sure to explain the benefits to them, including the opportunity for even better service. The major concerns of most clients when notified of a merger are:

- Are the principals I trust still there?
- Will this cost me more money?
- Is the practice's location still convenient to me? Will staff still be able to come to my office?

In an age of specialization, it's important to target your message. We typically divide the client base into industry categories, such as tax return only, retail, manufacturing, doctors, etc. We then create a message from the seller to the clients. The message to clients in the wholesale business, for example, may say:

I am pleased to announce I have affiliated my practice with John and Jane Doe. They have expertise in the wholesale industry and I wanted to take advantage of their knowledge and obtain additional back up and support. I will be remaining the principal in charge of your account and we will be operating under the same fee structure as in the past. Our staff is becoming part of this newly combined team

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of professionals and we are remaining located in the same community.

In one paragraph we have taken away most of the initial fears. The largest clients would get this message in a personal meeting, while clients in the middle would get a phone call and the lowest level clients a letter. The next step is a transition period during which the seller gradually reduces his or her role in the firm while the successor takes over.

How long should the transition take? That depends in part on the message—direct and indirect—that clients receive from the outgoing owners. We have seen firms work three years and more together with their successor but fail to transition properly. They hold on to their role as the clients' go-to person and stand in the way of the client's relationship with the new owners. We have also seen clients transitioned with the seller staying on in a very part time role for six months with excellent results. It is more the message than the time dedicated to the transition.

One of the best steps the seller can take is to convey the message that there is a value added in working with the new owners. Most of your clients trust you and if you lead them down that path, they will follow. ■

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