PRACTICE MANAGEMENT

# After the merger: Creating a culture of success

Incorporating the right components into a post-closing integration plan improves the odds for a smooth transition and positive results.

By Terrence Putney, CPA, and Joel Sinkin

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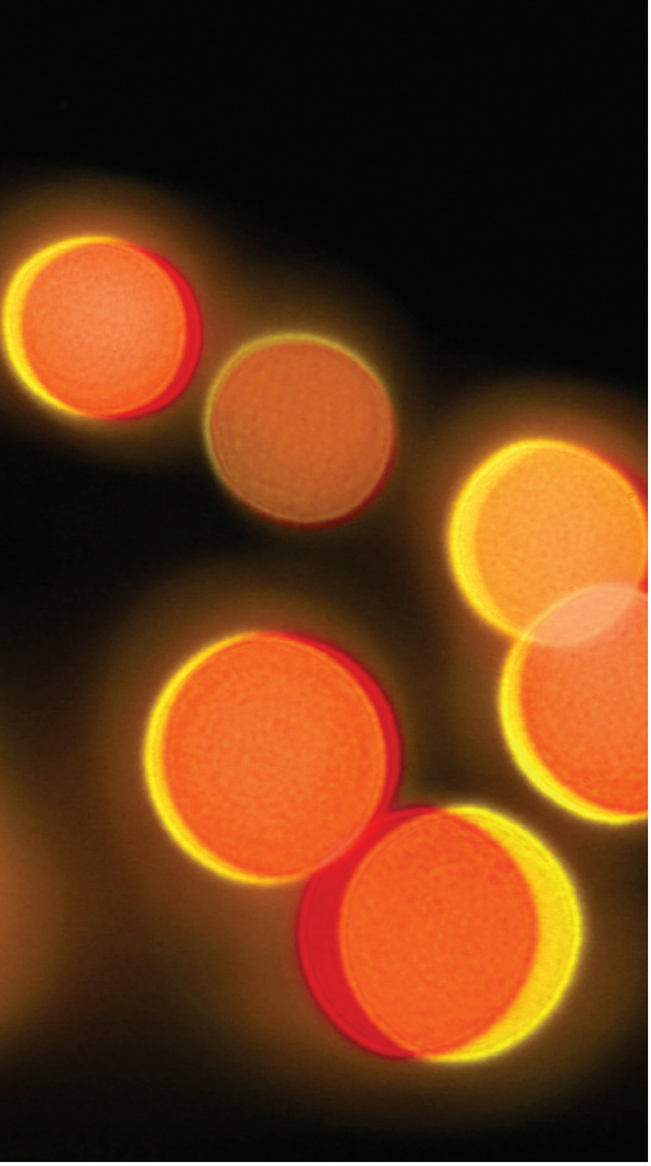

While negotiating a merger of CPA firms, both parties tend to focus most of their attention on the final deal terms, such as buyouts for retiring partners, contributed capital requirements, and compensation guarantees. While these issues are clearly important, very few deals fall apart after closing due to the negotiated terms.

Many times, mergers that fall short of expectations do so because of cultural conflicts and poor post-closing integration. Incorporating the right components into a post-merger integration plan and emphasizing the creation of a strong, homogeneous culture can greatly increase a merger's chances of success.

Note that the term "merger" is used in this article to generally describe the business combination of two accounting firms. However, the legal structure of many of these transactions is not a merger, but, rather, an acquisition of assets, the hiring of key personnel, or another means of combining.

## IDENTIFY AND DOCUMENT A POST-MERGER INTEGRATION PLAN

During merger negotiations, you should be developing a written business plan for the combined firm. The business plan should influence decisions such as with whom you are merging and the deal structure. Include operational and financial goals for the combined firm. Share the plan with the key people responsible for executing it. Typically, these are the partners and functional executive leaders of both firms. You can't hold people responsible for results if they don't know what the expectations are. Then transition the business plan into a formal, written post-merger integration plan. The post-merger integration plan needs to be as detailed as possible, stating who is responsible for executing each task and an expected timeline. Distribute the post-merger integration plan throughout the firm and ensure it addresses key issues in the following general areas:

- What changes will be made in the approach to client service, operating methodologies, and the technology we use?
- What training will be conducted on new technology and other systems, and when will that be performed?
- What changes in organizational structure are intended?

The written plan should include:

- The goals of the merger.
- Advantages of the merger for all firm members.
- Investments planned to improve the firm.
- Changes planned for firm leadership.
- Changes to the organizational structure.
- Changes to the decision-making structure.
- Whether there are staff redundancies.
- Changes to technology.
- Client communication initiatives.

## DEPLOY RESOURCES NEEDED TO EXECUTE THE INTEGRATION

Most of the resources you will need to execute the post-merger integration plan are people in your firm, consultants, and outside vendors. Integration plans often understate the costs and time required to train people on new systems. Be realistic with timelines, due dates, budgets, and especially the amount of time that will be required of your people in training and adapting to new systems. You may experience a temporary loss of productivity as a result.

Another key resource that frequently receives inadequate budgeting is technology. As an example, the cost to bring a firm onto a new IT platform ▸


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is often as much as $10,000 per full-time equivalent. Post-merger integration resources are often inadequate because successor firms are unwilling to be realistic about the capital necessary to execute the merger.

Capital *always* will be required to close a deal. Those requirements come in many forms, including legal and consulting fees. If you are buying a practice, there likely will be costs associated with the purchase and investment in working capital to support the growth. There are often costs associated with investments in office expansion and technology upgrades. If the successor firm is accustomed to financing operations primarily out of cash flow, partners tend to resist providing capital in the form of outside debt or other sources. As a result, some firms provide inadequate capital to implement a strong post-merger integration plan. If your merger is successful, it will drive a significant return on the entire investment. Failure to invest adequately in plan implementation can stunt or even halt the return on investment.

### GAIN COMMITMENT FROM KEY INDIVIDUALS IN THE FIRM

The firm's leadership team needs to be fully committed to executing the post-merger integration. During the integration, some individuals may resist making the required changes, perhaps because they are more comfortable doing things the way they've been done in the past. That thinking even can lead key people in the firm to making a sound case for why changes aren't necessary or why they shouldn't be implemented now. Unless you are willing to hire outside personnel and consultants to execute the post-merger integration plan, your people's time may be stretched and some routine tasks may have to be delayed. Firm leaders have to demonstrate their commitment to the plan to make sure the organization follows through.

### DEVELOP A ROBUST CLIENT RETENTION PROGRAM

First, accept the fact that the combined firm will lose some — hopefully very few — clients following the merger. Some attrition will occur among clients that were already looking to leave. The merger provides these "at-risk" clients with a convenient excuse to do something they had already planned to do. Although the nature of the client base and services offered by a specific firm can result in different outcomes, most CPA firms experience annual attrition of 3% to 6% in their client bases. Make sure your business plan accounts for a realistic level of post-merger client attrition.

Conversely, very few mergers will be considered successful if client attrition is too high. The key to client retention is to communicate often and clearly with clients. To do this, start by developing a communication plan (see "Sample Client Communication Plan," which can be downloaded with the online version of this article at journalofaccountancy.com/merger, for an outline of a firm's objectives for communicating the merger to clients). Emphasize what synergies the clients will gain from the merger. Make the messaging about the clients, not about the combined firm. The message should focus on what's in it for them, e.g., more resources, larger platform of services, etc. (see "Sample Announcement Letter,"

## IN BRIEF

- The post-merger integration plan should be as detailed as possible. It should include who is responsible for executing each task and an expected timeline.
- Merging firms should be realistic with timelines, due dates, budgets, and the amount of time required for employees to train and adapt to new systems. Firm leadership must demonstrate commitment to the plan to ensure follow-through.
- Few mergers will succeed if client attrition is high. Firms should develop a communication plan and communicate with clients early and often. This is key to client retention.
- A merger can offer a chance to introduce improvements in organizational structure. Create interoffice functional teams, especially in the beginning, to address cultural integration.
- Almost every merger tries to drive growth through revenue synergy. Firms should develop an aggressive plan for introducing the newly combined firm's capabilities to clients and prospects, and take advantage of enthusiasm resulting from the union.

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which can be downloaded with the online version of this article, for an example of how to communicate an upstream merger to clients). If you have to introduce changes to the client experience, try to delay as long as possible the changes that will have the greatest potential negative impact. Many clients of an acquired firm will be wary of how the merger will affect them. Buy some time to demonstrate the future will be better by introducing changes slowly.

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### COMMUNICATE WITH STAFF TO PROMOTE RETENTION

A merger can be a frightening experience for staff. They usually have had no say in what has happened. The public headlines of large mergers outside the accounting profession often emphasize employee layoffs. In most mergers of CPA firms, the larger firm is the successor firm, and, absent messaging to the contrary, the acquired firm's employees may feel at risk of not fitting in or even being terminated. However, staff career opportunities are often enhanced in a larger organization. If you can genuinely do so, reinforce in your communication that the merger creates more opportunities for the staff as well. However, note that in some situations there will be forced attrition of staff as discussed below. Make sure your staff communication is transparent and tailored to each person's situation.

Often, there will be differences between the two merging firms regarding perks, employee policies, compensation rates, and other employee issues. Normally, the successor firm's policies and compensation systems will prevail. If alterations need to be made for the acquired firm's employees, it is usually preferable where possible to make adjustments such as increasing compensation for the loss of paid time off or avoiding an imposition of compensation reductions to keep staff attrition to a minimum. Excess loss of staff in an acquired firm can also lead to problems with client retention.

The keys to retaining staff post-merger are:

- Don't leave out any details about how the merger will affect staff, no matter how trivial. Unless people are given the answers to their questions about how they will be affected by the coming changes, they tend to assume the worst.
- Communicate with staff often and as early as possible.
- Create a mentoring or buddy system, especially for staff from an acquired firm. It helps to have someone at a similar level as well as someone at a senior leadership level to talk with.
- Remember that most employees seek counsel from someone outside the firm, such as a spouse. Indirectly educate those outsiders on the benefits of the merger as well. Consider holding a social gathering with the spouses of employees to talk about the merger. Try to build support for the merger on your employees' homefronts.
- If you made accommodations to keep employee compensation and the value of benefits intact, emphasize this in your communication to the staff of an acquired firm.
- If you require employees to sign an employment agreement, try to position it as not only what the employee is being asked to commit to, but also what the successor firm is committing to.

### ADDRESS NEEDED CHANGES IN ORGANIZATIONAL STRUCTURE

Depending on the scale it represents for the combined firm, a merger can be a chance to introduce substantial improvements in organizational structure. If the combined firm is much larger than either of the two firms alone, this may represent an opportunity to invest in a stronger management infrastructure. Some combined firms may reach a size that justifies an investment in professional management of human resources, information technology, marketing, finance, and operations.

Try to integrate the two firms' cultures by blending the people wherever possible. If everyone ends up sitting in the same place doing the same things as before, integration tends to be stunted. Identify best practices in systems and procedures from both firms. Without creating unnecessary inconvenience for staff, consider transferring people to an office in the "other" firm. Some larger firms that execute a lot of mergers try to transfer a partner or up-and-comer to the office of an acquired firm to accelerate the transition of the acquired firm to their culture. Look for reasons to hold meetings that allow personnel from different offices to mix with one another. Create interoffice functional teams, especially in the beginning, to address integration.

## FIND AND IMPLEMENT COST SYNERGIES AS SOON AS PRACTICAL

Cost synergies are available in almost every situation. These usually involve elimination of redundant resources. Our rule of thumb is to find savings equal to at least 5% to 10% of the smaller organization's revenue if the offices are not combined. If the offices are combined, the cost synergies can be as high as 20% of the smaller organization's revenue. Keep in mind that roughly 70% of most accounting firms' costs are personnel related (including owners). Cost synergies may have to come in the form of personnel reductions.

As noted above, staff often fear that a workforce reduction is one of the goals of a merger, and they might be concerned they will lose their jobs. With a tightening market for professional staff, we see very few mergers that include a plan to reduce professional staff. If a proactive move to reduce headcount is planned, it will likely involve administrative personnel. Also, there is often an opportunity to use natural attrition to implement people-related cost reductions. Avoid telling staff that no one is going to lose their job only to implement headcount reductions soon thereafter. Be as transparent as you can. If a certain portion of staff will be leaving, explain why to the remaining staff so they are not alarmed. Be especially empathetic in how you manage the cuts. When considering headcount reductions, retaining staff that have a lot of direct client contact can be an important tool in client retention.

## DEVELOP AND EXECUTE A STRONG REVENUE SYNERGY PLAN

One plus one equals two unless you execute revenue synergies. Almost every merger tries to drive extraordinary growth. Revenue synergy will come in the following forms:

- Cross-selling new services to existing clients. One or both of the merging firms are likely to have services and expertise that the other didn't have before the merger, or existing capabilities that will be augmented through the merger.
- Brand enhancement, allowing for a much greater penetration of markets served by the combined firm.

To effectively capture revenue synergies, develop an aggressive plan for introducing the combined firm's capabilities to clients and prospects. Start immediately following the merger to take advantage of enthusiasm created by the union. The expectations you have for the "gatekeepers" of client relationships (aka partners) to execute the cross-selling plan need to be laid out and shared in your business plan.

## CREATE AN INTEGRATED CULTURE

The common definition of culture in a CPA firm is the shared values, beliefs, and behaviors that define how people do things in the firm. The first step in integrating cultures is to be clear about those components. Develop and distribute a culture statement that creates a benchmark to inform every decision people in the organization have to make (see "Sample Culture Statement," which can be downloaded with the online version of this article, for an example). Your firm's culture statement is unique. Some common themes in culture statements include:

- Respect between colleagues in the firm.
- Integrity and honesty.
- Team orientation.
- Exemplary client service.
- Passion for the firm and the profession.
- Constant improvement.

Also, ask yourself the following types of questions about the ways both firms operate. These questions can lead you to operational characteristics of the two firms that are good indicators of where cultural differences might exist:

- How are the clients served and by whom?
- How are they charged for services?
- What are the expectations of staff, and how is feedback provided?
- How are partners managed, and what roles do they play?
- How do people in the firm communicate with each other?

Those are just a few examples of how to assess culture. For example, a firm with a low partner-to-staff ratio that relies heavily on partner time to serve clients will likely have a much different operational culture than one that is more highly leveraged.

Identify where there are significant differences in the characteristics of the two firms' cultures, then find ways to bridge those differences. Unless you develop a consistent culture within the combined firm, you run the risk of the merger not meeting expectations.

## LAYING THE FOUNDATION FOR SUCCESS

An effective post-closing integration plan greatly increases the odds for success in a merger of accounting firms because it helps to establish a realistic timeline, good communication with employees and clients, and a strong revenue synergy plan. More importantly, the creation of an integrated culture constructed through shared values, beliefs, and behaviors will not only serve the merger well in its early stages, but it also will lay a foundation for the future success of the newly combined firm. ■

## AICPA RESOURCES

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"Building a State-of-the-Art M&A Target," *JofA*, Aug. 2018, tinyurl.com/ycthadw2

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"Roadblocks to Avoid in Accounting Firm M&A," *JofA*, Sept. 2015, tinyurl.com/y9zqbgs7

### Publication

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