The new breed of buyers

The market for acquiring accountancy practices is being re-energised by more varied suitors, such as outsourcers, private equity and IT firms, says Keith Underwood

There have been stirrings in the accountancy acquisition market over the past 18 months. The consolidators have long gone but the market is attracting attention from a couple of groups of new, specialist buyers.

These are outbidding traditional practices for high-quality firms of all size, or for firms that have particular characteristics. The sums payable for the 'right' businesses are certainly above the levels seen in this sector over the past three decades – that is, ignoring the consolidator era of 10 years ago. The new buyers are:

1. outsourcers looking to service accounting back offices from overseas
2. entrepreneurial individuals and family offices
3. non-UK based firms in associated services wishing to establish themselves in the UK, either to diversify their client offering or to establish a presence onshore
4. international firms, strong in either the US or Asia, looking to expand in the European market
5. UK and European entities seeking a range of skillsets and clients that complement their services in other parts of the world.

The outsourcer model has been around for a number of years. The premise is to introduce a cloud-based service, with accounts preparation and other back-office functions being provided by cheaper, offshore accountants. The approach has been used in some cases to ramp up offer prices on the back of lower direct costs – but it is not a long-term solution. The issue has always been the relationship with the client, particularly when there is a change at the top of that company.

Offshore outsourcing might also become less advantageous as IT becomes more intuitive and eliminates employee functions. As with other sectors, if labour costs are driven down by advances in IT, the advantage of outsourcing diminishes.

New buyers in the second, third and fourth categories mentioned above are seeking either strongly specialist portfolios or single-platform providers, whether they be management accounting, payroll, corporate or straightforward accounting services. Compliance services are usually attractive but audit is not desirable and often needs to be ring-fenced and either excluded or dealt with separately as part of any deal.

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Refreshing change

The concept of scale and optimisation is attractive to many of these acquirers. They are looking for management teams to remain in place and retain some equity. This is a refreshing change from the usual scenario where practice sales are triggered by the retirement of senior partners and there is a reluctance, even aversion, to working in the future with a purchaser that has different strategic aims.

In the new model, those left with a small amount of equity have a chance of reaping significant rewards in working with the new buyers and then selling out their minority interest at a later date.

These buyers are usually backed either by private equity or a family office investor. There have been a number of private equity acquisitions in the sector – for example, the purchase of SJD Accountancy and Nixon Williams by Sovereign Capital in 2014, and deals in 2016 by CogitalGroup, HgCapital's investment arm, for Blick Rothenberg, CLB Coopers and Baldwins.

Private equity-backed businesses often have slightly different objectives, needing to spend the money invested within three to five years so that the value of the firm can be maximised for a resale.

This model may not be attractive to the traditional firm, or practitioners who have been working for 20 to 30 years with their clients providing a full range of services. However, with new IT applications and platforms, and a shake-up in the pricing and profitability of general practices, which will become more evident over the next two or three years, the new players in the market will provide very interesting opportunities.

Beware software

It may also be that the advent of IT companies buying practices to protect their product distribution may not be far away. Whether this is a viable model is uncertain but, as we have seen recently, software houses have started to sell direct to small and medium-sized businesses. If this approach becomes widespread then the role of the accountant selling licences and capturing SME client information might fall away.

If you look at the recent announcement on the corporatisation of Blick Rothenberg, it is clear that CogitalGroup's largest operation is not Baldwins or Blick Rothenberg but an IT back-office system that operates in Scandinavia.

Visma BPO provides outsourced accounting, payroll and HR services to 20,000 businesses in the Nordic region. According to its website, it 'brings leading technology that both assists practice accountants in the delivery of their service and also enhances the client experience through easier and more effective client/adviser collaboration'.

How a strong back-office system servicing multiple accountants in Scandinavia and the Baltic region is compatible with the high-level personal tax advisory services with which Blick Rothenberg developed its reputation – as well as some small accounting practices that had initially joined Baldwins – is unclear. No doubt time will tell whether synergies and rationalisation can improve the bottom lines of these seemingly disparate business entities.

However, the grouping of IT investment and practice acquisitions could offer a similar scenario to the outsourcing model discussed above. And as we see with other IT applications in different sectors, the development of 'dashboard' type information by software developers is sought by a growing number of smaller owner-managed businesses but is a challenge to the services currently offered by traditional accountants.

A number of offshore firms are interested in UK entities, although not the audit aspects of a multi-service practice. The premium values attached to streamed business – such as accounts preparation, tax and payroll running off single-platform systems – is going to bring pricing competition to the traditional accounting practice. So we foresee them being driven more firmly into advisory services.

It is critical that accounting practices retain and grow the SME and owner-managed business sector, or focus on a specific type of client – for example, UK inbound tech companies.

The advantage of leverage

It is difficult to change a general practice to become attractive to some of these non-accounting investors, but there are parties with particular features or characteristics that can be sold to these new acquirers. In some cases this has meant firms have had to be broken up to realise significantly higher valuations.

We have seen some resistance from accountants in general practices to the governance and commerciality of the new entrants to the market. These businesses are commercial, they work on sustainable earnings before interest, tax, depreciation and amortisation, and they are seeking rationalisation and change in this traditionally conservative sector. Clients and service are uppermost, but as these businesses have associated services, they have the advantages of leverage and an international platform to work with clients as they move across jurisdictions.

There are interesting opportunities for the short and medium term, but practices need to be flexible and have the capability to evaluate these opportunities and embrace change. ■

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