

Improving Firm Profitability



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Donny C. Shimamoto, CPA, CITP, CGMA

Polls: open itk.cnf.io in a web browser

- Donny is the founder and managing director of IntrapriseTechKnowlogies LLC, an advisory-focused CPA firm providing innovation management and organizational development services for small businesses, middle market organizations, and nonprofits. Donny is a nationally recognized thought leader and educator in the accounting technology, emerging technologies, IT risk management, and organizational performance management fields.
- Donny serves as an outsourced Chief Innovation Officer and business transformation advisor for accounting and internal audit departments who are seeking to increase their value proposition and help drive holistic improvement in their organizations. He helps with IT risk assessments and guides remediation strategies, development of departments' innovation strategies, streamlining of internal operations, and increasing staff proficiency with IT tools supporting operations and service delivery.
- Donny was recognized as one of the Top Thought Leaders in Public Accounting by CPA Practice Advisor from 2012 to 2019, Top 100 Most Influential People in Accounting (2013,2014,2017-2019) by Accounting Today, received the 2009-2010 President's Award from the Hawaii Society of CPAs, was named to CPA Technology Advisor's 40 Under 40 list in 2007 & 2009 & 2014, and was also a Hawaii Top High Tech Leader in 2004.



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Audience Polls – Open itk.cnf.io in your web browser



- **Organization Type/Size?**
 - Solo Practitioner
 - Small Firm (2-10 people)
 - Medium Firm (11-40 people)
 - Large Firm (41+ people)
 - Business & Industry
 - Consultant/Vendor
- **Primary Area of Practice**
 - Admin / Practice Mgmt
 - Audit / Assurance
 - Consulting (non-Audit/Tax)
 - Financial Reporting / Accounting
 - Information Technology
 - Tax
- **Role in Organization**
 - Lead Executive
 - Executive Leadership
 - Dept Director/Manager
 - Dept Staff
 - Vendor/Consultant



Choose one from each set of options that best matches how you view your organization and your role in your organization.

Improving Firm Profitability



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- **Understanding Your Firm's Performance**
 - Highlights from the AICPA's PCPS Management of an Accounting Practice (MAP) Survey
- **Strategies for Improving Firm Profitability**
 - The "Profit Wheel"
- **Increasing Performance Through Firm Operational Transparency**

Understanding Your Firm's Performance



- Content for this section is adapted with permission from "Behind the Numbers...Understanding the Business Side of CPA Firms", AICPA Women's Global Leadership Summit, by William Pirolli CPA/PFS/CFF/CGMA, Nov 2019

Benchmarking Your Firm

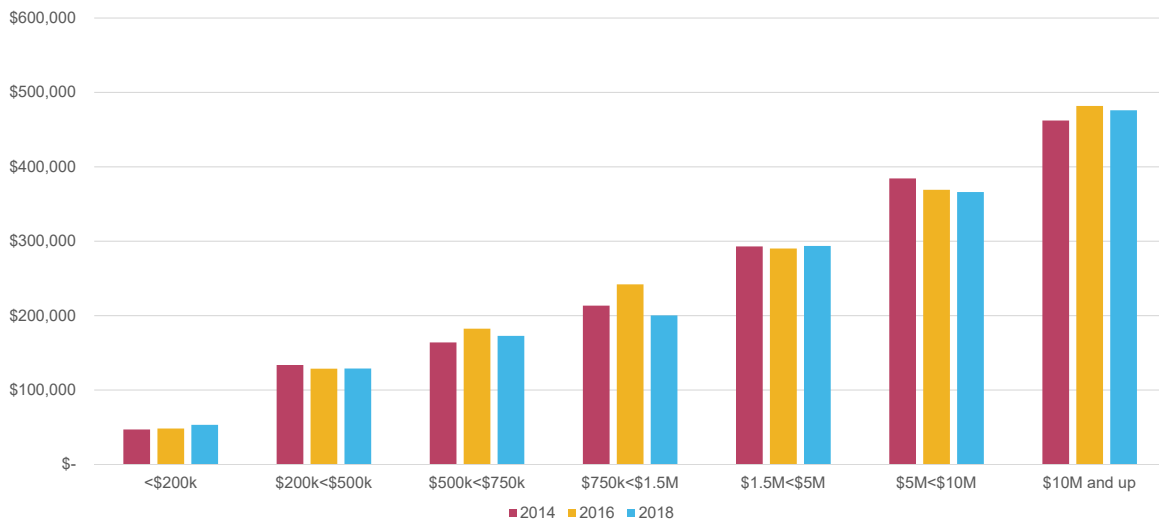
Data from PCPS MAP Survey

- Net remaining per owner (median)

Firm Revenue	2018	2016	2014
<\$200K	\$52,968	\$48,111	\$46,815
\$200K < \$500K	128,750	128,630	133,535
\$500 < \$750K	172,598	182,294	163,875
\$750K < \$1.5M	200,136	241,817	213,211
\$1.5M < \$5M	293,496	290,086	292,842
\$5M < \$10M	366,037	368,916	384,268
\$10M and up	475,943	481,731	462,212

- Where does your firm map to on revenue?
- How does your firm compare to the medians shown here?

Net remaining per owner



Benchmarking Your Firm



Data from PCPS MAP Survey

• Owner compensation (median)

Firm Revenue	2018	2016	2014
<\$200K	\$43,675	\$50,000	\$60,000
\$200K < \$500K	105,000	101,422	91,329
\$500 < \$750K	136,797	142,082	118,420
\$750K < \$1.5M	175,000	216,667	180,000
\$1.5M < \$5M	251,392	254,833	245,345
\$5M < \$10M	298,740	323,079	295,543
\$10M and up	453,428	443,320	384,786

- Where does your firm map to on revenue?
- How does your firm compare to the medians shown here?

Owner compensation



Benchmarking Your Firm



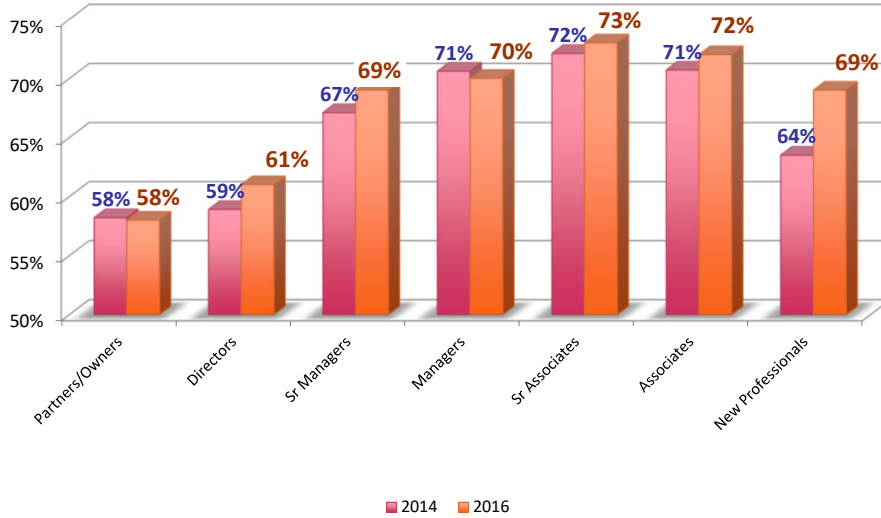
Data from PCPS MAP Survey

● Realization (median)

Firm Revenue	2018	2016	2014
\$750K < \$1.5M	96.0%	100.0%	99.1%
\$1.5M < \$5M	91.0%	94.6%	94.3%
\$5M < \$10M	88.6%	88.2%	87.7%
\$10M and up	85.0%	89.4%	87.6%

- Where does your firm map to on revenue?
- How does your firm compare to the medians shown here?

Utilization by Staff Level



Utilization - Firmwide



Benchmarking Your Firm

- Net client fees per owner (median)

Firm Revenue	2018	2016	2014
<\$200K	\$102,500	\$100,000	\$116,134
\$200K < \$500K	291,000	290,000	280,323
\$500 < \$750K	526,210	534,935	505,503
\$750K < \$1.5M	569,286	640,000	558,039
\$1.5M < \$5M	863,731	824,068	772,171
\$5M < \$10M	1,201,947	1,185,152	1,111,728
\$10M and up	1,566,667	1,661,347	1,443,166

- Where does your firm map to on revenue?
- How does your firm compare to the medians shown here?

Benchmarking Your Firm

- Net client fees per professional FTE (median)

Firm Revenue	2018	2016	2014
<\$200K	\$96,598	\$78,594	\$95,112
\$200K < \$500K	140,433	141,972	161,570
\$500 < \$750K	150,125	142,452	180,000
\$750K < \$1.5M	164,323	171,238	197,115
\$1.5M < \$5M	181,373	183,925	207,426
\$5M < \$10M	199,614	185,127	213,899
\$10M and up	\$96,598	\$78,594	\$95,112

- Where does your firm map to on revenue?
- How does your firm compare to the medians shown here?

2018 Average billing rates

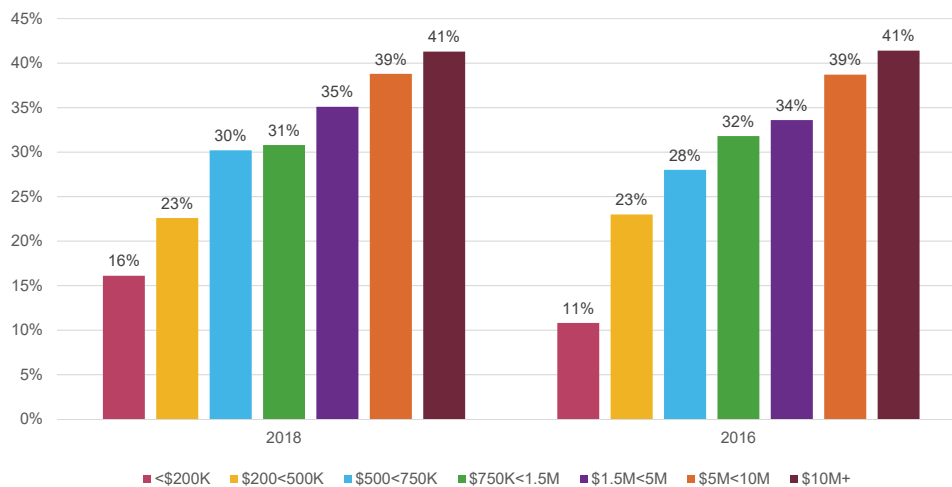


Data from PCPS MAP survey

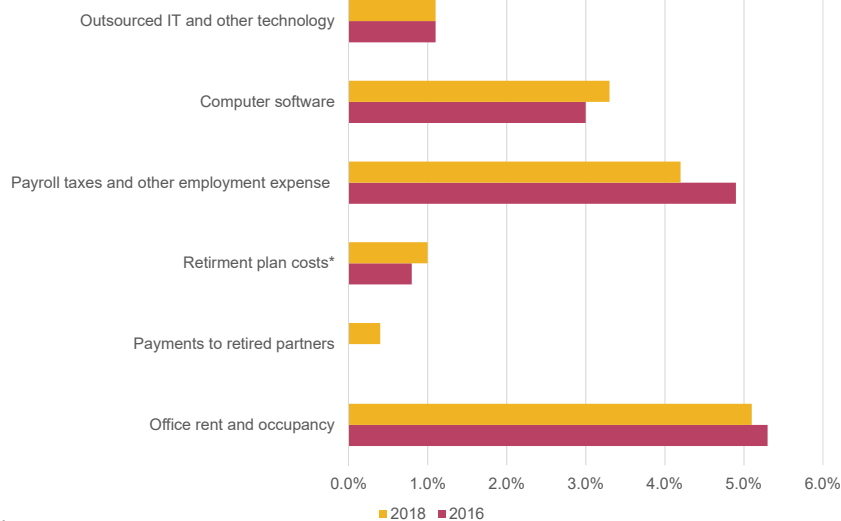
	<200k	\$200k <500k	\$500k <750k	\$750k <1.5M	\$1.5M <5M	\$5M <10M	\$10M +
Partners/Owners	\$137	\$175	\$195	\$200	\$249	\$289	\$323
Directors	*	143	170	155	208	250	279
Sr Managers	*	125	135	141	174	195	231
Managers	*	110	123	125	153	175	193
Sr Associates	*	90	100	109	125	146	161
Associates	*	75	85	89	100	115	125

*Information not available due to limited responses

Salaries as a % of NCF (excludes owners)



Expenses as a % of NCF



*excludes owners

Figure out which metrics are important



Adapted from "Behind the Numbers...Understanding the Business Side of CPA Firms", AICPA Women's Global Leadership Summit, by William Pirolli CPA/PFS/CFF/CGMA, Nov 2019

These are but a few of the hundreds of metrics that can be tracked, including

- Realization (Net WIP billed/gross WIP relieved)
- Measure of billing efficiency/profitability
- Utilization / ~~Productivity~~ (billable hrs./total hours)
- Measure of people management
- Average partner managed billing
- Measure of partner leverage
- Revenue per full time equivalent (FTE)
- Measure of staffing leverage

Donny's Tips

- Remember that what gets measured can drive behavior
- Be careful which metrics you choose as the wrong ones can have adverse effects.

Strategies for Improving Firm Profitability



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Attributes of Highly Profitable Firms

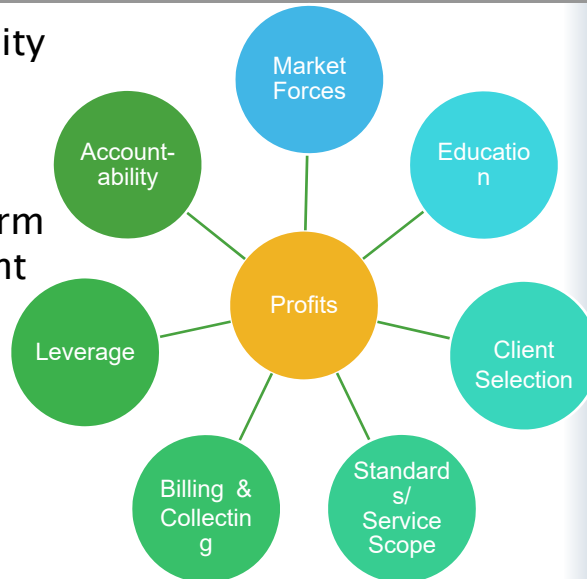
Adapted from “Behind the Numbers....Understanding the Business Side of CPA Firms”, AICPA Women’s Global Leadership Summit, by William Pirolli CPA/PFS/CFF/CGMA, Nov 2019

- Strong leadership
- Committed to best in class business practices
- Empowered management team
- Strong partner unity
- High Accountability
- Transparent
- Unified vision of growth strategy
- Specialties and niches....go deep
- Aligned compensation system

The Profit Wheel

Adapted from "Behind the Numbers...Understanding the Business Side of CPA Firms", AICPA Women's Global Leadership Summit, by William Pirolli CPA/PFS/CFF/CGMA, Nov 2019

- Firm Profitability is driven by a variety of factors that makes each firm a little different



Understanding MARKET FORCES

Adapted from "Behind the Numbers...Understanding the Business Side of CPA Firms", AICPA Women's Global Leadership Summit, by William Pirolli CPA/PFS/CFF/CGMA, Nov 2019

- Environmental Scan
 - Local, Regional and National
 - Effects of technology (Blockchain, AI)
- Who is the customer?
- What are the customer's needs?
 - Shift in Service Model – Cloud
- Who is the competition?
 - Constantly changing with M&A activity
 - Pressure from outside the profession
- What is your firm's core skill set?
- What do you like to do and do best?

Bill's Tip

If you don't know the answers to these questions consider answering them as part of a strategic planning retreat

EDUCATION of our people and the market



Adapted from "Behind the Numbers...Understanding the Business Side of CPA Firms", AICPA Women's Global Leadership Summit, by William Pirolli CPA/PFS/CFF/CGMA, Nov 2019

- We need to train our people / partners in the business of accounting
 - Firm Economics training
- Improve transparency throughout the firm
- Educate clients about our services
- Understand what our key profit drivers are
- Benchmark and improve those drivers

Improving CLIENT SELECTION and retention



Adapted from "Behind the Numbers...Understanding the Business Side of CPA Firms", AICPA Women's Global Leadership Summit, by William Pirolli CPA/PFS/CFF/CGMA, Nov 2019

- Poor clients produce poor results
- Develop client intake filters that work
- Is the client strategic?
 - (important or essential to a plan of action)
- Develop industry verticals
- Stop being all things to all people
- Keep the best, fire the rest
 - Consider the AICPA's PCPS Client Evaluation Tool

Are you managing SERVICE SCOPE?



Adapted from "Behind the Numbers...Understanding the Business Side of CPA Firms", AICPA Women's Global Leadership Summit, by William Pirollo CPA/PFS/CFF/CGMA, Nov 2019

- The relentless pursuit of perfection is the death of profit
- Standards are meant to be met...not hurdled
- Avoid scope creep in the name of client services
 - Clearly define scope in engagement letters
 - Engagements change...bill accordingly
- Constantly improve and streamline your processes

Managing Standards / Scope Creep



Adapted from "Behind the Numbers...Understanding the Business Side of CPA Firms", AICPA Women's Global Leadership Summit, by William Pirollo CPA/PFS/CFF/CGMA, Nov 2019

- Review your engagement letters to determine if the scope is adequately communicated and understood
- Educate your team to communicate issues and lost time proactively
- Create separate engagements for different services and invoice separately
 - Pre-audit adjustments
 - Audit services
 - Tax services
 - Consulting services
- Invoice with clarity and in phases

Bill's Tip
Most poorly performing engagements are service opportunities to generate Trusted Business Advisor engagements.
Sell value!

Better BILLING practices



Adapted from "Behind the Numbers...Understanding the Business Side of CPA Firms", AICPA Women's Global Leadership Summit, by William Pirolli CPA/PFS/CFF/CGMA, Nov 2019

- If you are not going to bill and collect, why come to work?
- Strong billing and collections keeps your firm sustainable

- Communicate fees and billing arrangements up front
- Avoid the "how much will it cost" trap
- Bill early and bill often – phasing

- Know the difference between value pricing and value billing
- Form a billing committee
- Mentor underperformers...teach good billing habits
- Create accountability

Donny's Tip
When defining your billing approach consider:

- Deliverables
- Project flow
- Incremental delivery / milestones
- Project manager motivations
- Who bears the risk? Client or firm? Or shared?

Define and enforce COLLECTIONS



Adapted from "Behind the Numbers...Understanding the Business Side of CPA Firms", AICPA Women's Global Leadership Summit, by William Pirolli CPA/PFS/CFF/CGMA, Nov 2019

- Have standard policies...and follow them
- Set clear payment expectations up front
- Consider fixed auto-draft [for recurring services]
- Stop servicing clients who do not pay...don't make their problem your problem
- Go on the client's payroll...credit cards / PayPal
- Send statements...make the call too
- Let administration handle it
- Sent it to collection if necessary

Bill's Favorite Billing Myths



Adapted from "Behind the Numbers...Understanding the Business Side of CPA Firms", AICPA Women's Global Leadership Summit, by William Pirolli CPA/PFS/CFF/CGMA, Nov 2019

- The client is fee sensitive
 - All clients are fee sensitive. If the client won't pay the fee then you haven't communicated your value.
- We are discounting this work in hopes of getting more
 - You have just set the precedent that you will do work cheaply
- The client had a problem, I didn't want to take advantage
 - The client had a problem and we came to the rescue. Communicate, value bill, and help them fix it.
- We will make it up next year
 - You will never make it up...do the math.
 - Are you keeping a running tally so that you can tell?

Bill's Favorite Billing Myths – part 2



Adapted from "Behind the Numbers...Understanding the Business Side of CPA Firms", AICPA Women's Global Leadership Summit, by William Pirolli CPA/PFS/CFF/CGMA, Nov 2019

- We need to lower our price, we keep losing bids
 - Sometimes true...also a crutch for lack of billing courage or inability to communicate value.
 - Are we over performing on services?
- It is off-season work...we already have the overhead so it is all profit
 - Partially true...but why is everything priced as off-season work? Has the rate become the norm? Staff hate working on losers.
 - Do we have a busy-season rate? Does the client know?
- It is good for staff training
 - SEE ABOVE
- The client is a good referral source
 - Great...more just like them!!!?
 - Are we getting the referrals? What realization are we getting?

LEVERAGE Clients and Staff

Adapted from "Behind the Numbers...Understanding the Business Side of CPA Firms", AICPA Women's Global Leadership Summit, by William Pirolli CPA/PFS/CFF/CGMA, Nov 2019

- Easier to expand services to an existing client than to get a new client
 - All the new business you need already exists in your client base...go sell something
- Create billing leverage
 - Develop value-added niche services
 - Push work down to create staff leverage

- Most responsible for lost profits



Illustration: The Power of a Quarter Hour

Adapted from "Behind the Numbers...Understanding the Business Side of CPA Firms", AICPA Women's Global Leadership Summit, by William Pirolli CPA/PFS/CFF/CGMA, Nov 2019

If everyone found an additional .25 billable hour per day that would translate to....

- \$705,250 in annual billing for a 62 person firm
- Calculation:
 - $62 \times .25 = 15.5$ hours per day
 - 15.5×5 days = 77.5 hours per week
 - 77.5 hours/week \times 52 weeks = 4,030/year
 - $4,030 \times \$175$ (average net firm rate) = \$705,250

Focus Your Marketing & Business Development Vertically



Adapted from "Behind the Numbers...Understanding the Business Side of CPA Firms", AICPA Women's Global Leadership Summit, by William Pirolli CPA/PFS/CFF/CGMA, Nov 2019

- Some of the most profitable firms in the country have gone deep into industry or service niches
 - Repetition = Efficiency...Efficiency = Profit
- You can concentrate on:
 - Client mix, service mix, or non-traditional services
- Any specialty makes you attractive for merger
- Consider a practice alliance to enhance your niche
- Consider a firm alliance to enhance your reach

Hold everyone ACCOUNTABLE



Adapted from "Behind the Numbers...Understanding the Business Side of CPA Firms", AICPA Women's Global Leadership Summit, by William Pirolli CPA/PFS/CFF/CGMA, Nov 2019

- Accountability starts with you
 - Align your compensation system
 - For both staff and for partners
 - Every team members has a fiduciary responsibility to the firm to create profit
 - Goals should be customized to, measurable by, and attainable by each person
 - A goal without a plan is...
 - Who has enforcement power? MP? EC?
 - Enforce through rewards or penalties?
- Accountable (def)
- Required or expected to justify actions or decisions; responsible.

Increasing Profitability through Firm Operational Transparency



- **Everyone has a part in Firm profitability**
- The following slides are adapted with permission from a presentation that Bill's firm gives to all new hires and the entire Firm on a regular basis

Everyone has a part in Firm profitability

Adapted from "Behind the Numbers...Understanding the Business Side of CPA Firms", AICPA Women's Global Leadership Summit, by William Pirolli CPA/PFS/CFF/CGMA, Nov 2019

- Firms need to improve transparency in financial and other areas of the Firm including
 - Path to promotion, path to partnership,
 - Firm strategy for growth,
 - Business development efforts, and
 - Professional trends and issues.
- You don't have to reveal ALL of the numbers, but you need to share enough that the staff feel like they have a representative and realistic picture of the firm
 - Not sharing enough can create dis-trust



What the firm does...

Adapted from "Behind the Numbers...Understanding the Business Side of CPA Firms", AICPA Women's Global Leadership Summit, by William Pirollo CPA/PFS/CFF/CGMA, Nov 2019

- Find and develop the client relationship
- Service the client's needs
- Gather time, invoice and communicate the value of the services we provide
- Collect the billing to fund operations
- Repeat the process



Gathering time...

Adapted from "Behind the Numbers...Understanding the Business Side of CPA Firms", AICPA Women's Global Leadership Summit, by William Pirollo CPA/PFS/CFF/CGMA, Nov 2019

- 75% of all revenue in the profession is earned by the hour....right or wrong.
 - 25% is either fixed fee (majority) or value billing (rare)
- Keeping time is like cost accounting....it is a tool
 - Don't just use a code....explain time, create a trail
 - Used to improve performance, understand work flow, allows benchmarking and creates accountability
- The long journey from time entry to billing
 - Explain the importance of timeliness



Invoice for the value of our services



Adapted from "Behind the Numbers...Understanding the Business Side of CPA Firms", AICPA Women's Global Leadership Summit, by William Pirolli CPA/PFS/CFF/CGMA, Nov 2019

- Have up front value communications, price with purpose and before you do the work
 - YOU are the Trusted Advisor
 - Set clear scope specifications and avoid scope creep!
- Consider menu pricing/fixed fee arrangements (The Southwest Model)
- Always bill timely
 - Collect retainers
 - Consider monthly/quarterly fixed billings
- Consider auto-draft payment agreements
- Stop work until paid on past due amounts



Collect billings to fund operations



Adapted from "Behind the Numbers...Understanding the Business Side of CPA Firms", AICPA Women's Global Leadership Summit, by William Pirolli CPA/PFS/CFF/CGMA, Nov 2019

- Cash flow is the life blood of the firm
- Timely billing leads to timely collections
- Bill early and often
- Stop services in the absence of payments
- Allow for collections electronically
- Go on the "payroll" for collections
- Use ACH auto drafts
- Yes, we take credit cards!!!



Firm Economics: Major Cost Centers

Adapted from "Behind the Numbers...Understanding the Business Side of CPA Firms", AICPA Women's Global Leadership Summit, by William Pirolli CPA/PFS/CFF/CGMA, Nov 2019

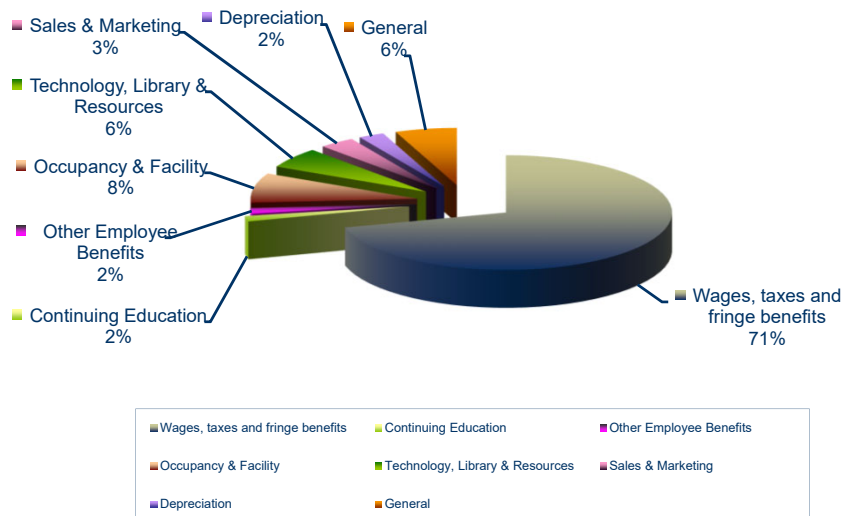
Help staff to understand the firm's cost centers

- Salaries and Benefits: can make up more than 70% of total expenses and 40% - 45% of fees
 - Wages and statutory taxes
 - Health insurance and other benefits
- Occupancy - 7%
- Technology and Software-4%
- Training and Education-2%
- Marketing & Business Development-3%



Example: Where we spend our money (% of total dollars - exclusive of partner compensation)

Adapted from "Behind the Numbers...Understanding the Business Side of CPA Firms", AICPA Women's Global Leadership Summit, by William Pirolli CPA/PFS/CFF/CGMA, Nov 2019



Improving Firm Profitability

- There is no magic formula for improving profitability
 - Each firm must figure out which aspects of the Profit Wheel provides the right opportunities to improve its profitability
- Benchmark your firm to help identify areas that you may want to focus on first
 - Remember that the numbers on the MAP surveys are averages or medians, if you match the number you are just an average or middle performer
- Educate your partners and staff, and create transparency to build shared accountability
 - Adjust compensation plans to tie to accountability (not profitability) goals



Thank you for your attention and participation!

Any Questions?



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