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Accounting Firms/CPAs

SIC: 8721-01

NAICS: 541211

Number of Businesses / Units: 89,188

Rule Of Thumb

100 to 125 percent of annual revenues plus inventory

2 to 3 times SDE plus inventory

2 times EBIT

2.2 times EBITDA

Pricing Tips

"No individual client or industry type over 20% of Gross Revenue. Gross Revenue earned from Audit, Accounting, or Tax Returns"

"Even distribution of revenue from tax return preparation and accounting fees is better."

"CPAs commonly use 1 times gross although we have frequently exceeded that amount."

"Product mix and any special areas of practice can affect selling price to the right buyer. There is always the possibility to split up a practice among two or more buyers if specialty work is involved."

"Pricing levels have increased slightly over past several years. In general, pricing ranges from a low of 75% of sales for firms under \$50K in revenue to 130% for larger firms in excess of \$1M in sales."

"SDE should be 40% to 60% of gross revenue. The higher the percent of SDE, the more valuable the practice. Other important factors: no client over 20% of revenue, and type of work mix (audit, tax, consulting, bookkeeping)"

"Many buyers want an earnout but there is demand for practices, and buyers will pay more than 1 times gross."

"Revenue composition is important; retail tax, writeup, monthly accounting, review work, audit, consulting, types of revenue streams—all have an effect on sale's price."

"Generally sold based on an annual multiple of gross revenue."

"Biggest factor is the terms and whether seller will guarantee part or all of the income."

"SDE should be between 40% and 60% of revenue."

"Many accountants automatically expect all practices to be worth one times gross. We find that is not true. Most practices will sell for higher than that amount."

"Selling price is usually based on percent of gross sales. Small practices, under \$100K, will usually sell for less than 100%. Large firms, over \$500K, may sell for \$120% or higher."

"CPA buyers always want to pay 1 times gross . . . sellers tend to want more . . . terms drive price."

"Generally will sell for a multiple of annual GROSS revenues (billings)."

"1 to 1.25 times revenue, with SDE of 30% to 60% of gross revenue."

"Employees on non-compete will increase; composition of services, accounts receivable, pricing of client work, recovery percentages. These last few will swing price in both directions."

"Accounting, tax, bookkeeping, EA and/or CPA firms typically sell for 100% to 135% of annual gross revenue. They tend to sell for 2–4 times SDE."

"Sale price should yield an SDE range of 40% to 60%."

"Location is paramount. Same practice will sell for 1.3 times gross revenue in one location and 1 times gross revenue in another."

"The composition of billings is important. The split between recurring/one time. The split among taxes/accounting/audit/consulting/other is important in determining staff composition. Labor costs are extremely important in bottom line. Accounts receivable levels may indicate problems with billings and/or clients."

"The commonly accepted rule of thumb is one times annual gross sales. The biggest cause for variation from this (50% more or less) is location. Prices in big metro areas are seldom that low. Prices in rural areas are often not that high. Also, it is VERY important to consider the wide variation in definition of 'one times annual gross.' One definition is a total 'work out' situation paying seller 20% of collection each year for five years. On the other end of the scale is a check for all cash at closing with no seller risk regarding retention of clients. These differences in definition of 'price' can mean that actual present value can vary by as much as 100% depending on definition used. Owners (sellers) and buyers are often very confused and misled regarding these issues."

"EBIT and EBITDA are difficult to use in this industry. This depends a great deal on the staffing requirements, which in turn are dependent on the services provided. It is important to understand the composition of the billings—audits, annual bookkeeping, monthly write up, composition of tax returns (corporate, partnerships & individuals) and the average fees for each of the client lists. Non-recurring consulting billings must also be examined. If regular and for existing clients more valuable than for non-clients (one time consultations). Existing staff represents the greatest danger to the buyer, non-compete agreements are important. State laws vary widely on who can perform what services and what they can call themselves."

"Sales price will be the lesser of 1.3 times gross revenues or 3 times SDE—and will include FF&E."

"Accounting firms generally sell based on a multiple of annual gross revenues. That multiple is generally 1 times billings. Premium factors may add to this multiple, such as fee structure, location, services provided, length of time the firm has been established, etc."

"Type of professional service for clients, client industry mix, no client over 10% of practice revenue, professional staff with firm, time & billing records or charge by service, length of time as a client with the firm, economic outlook for geographic area of service."

"CPA firms typically sell for 100 to 130% of Annual Gross Sales. Larger firms typically demand a higher percentage. Small single CPA offices may only warrant 100%. The size, training, and qualifications of the firm's staff have an impact on pricing."

"Earnouts are used for most do-it-yourselfers."

Expert Ratings

Amount of Risk : 1.80 (1=Lot of : 4= Not Much)

Historical Profit Trend : 2.60 (1=Lot of : 4= Not Much)

Location & Facilities : 2.00 (1=Lot of : 4= Not Much)

Marketability : 3.00 (1=Lot of : 4= Not Much)

Industry Trend : 2.40 (1=Lot of : 4= Not Much)

Ease of Replication : 2.00 (1=Lot of : 4= Not Much)

Experts Comments

"Great buyer demand....difficult industry to grow organically."

"Most smaller CPA firms either specialize in a type of industry audit or avoid all audits. The special industry audit firm may be more difficult to sell due to small demand."

"Competition is aging and the regulating agencies are making an impact on various areas of practice, in particular taxation. Accountants are usually not very good at generating new business so acquisitions are a key growth strategy."

"The profit trend and industry trend is upward due to increased tax and government regulations on businesses and individuals. Location and facilities are located in office or upscale retail locations. A profitable, well-balanced CPA practice is highly marketable to those entering the profession from corporate and established firms to expand their client base. Replication or opening a practice is not difficult. Establishing a client base is the challenge for a new CPA practice."

"Easy to start but takes a lot of time to build good client base."

"In general CPA firms are low risk and high profit. Profit can easily reach 30% of revenues. Existing firms are easily marketed with well-qualified buyers."

"Industry outlook is increasing due to a complex tax code and need for business financial reports and services."

"Business owners continue to age, and the sole proprietorship is at risk if he or she does not plan an exit, something they are poor at."

"Marketability is high because practice purchase is a quick and low-cost method of increasing revenue and long-term SDE."

"CPA firms are easily marketed. The pool of buyers usually has significant financial resources to close a deal."

"Although a very stable industry, current government regulations and the changes of such have put increasing demand on service. There is also a decline in numbers of people entering and staying in public accounting."

"Risk of client loss is the biggest factor in a purchase."

"CPAs benefit from changes in tax law. Due to upcoming change of President, expect many tax changes to be enacted that will drive tax work to CPAs."

"Demand for client service is increasing. Purchasing a client base may be less expensive and quicker than new client marketing."

"The marketability of accounting firms is much greater in major metro areas but still fairly marketable even in rural areas."

"People don't leave their CPA often—so there's competition but it doesn't affect established firms much. Very low risk—very few CPAs go out of business. Profits are up although firms can be adversely affected by local trends—i.e., Silicon Valley fallout where CPAs have a concentration in a particular industry. Facilities are often Class A buildings. There's definitely a market for CPA firms but finding the right buyer is difficult. The industry is increasing while fewer people enter the profession. Replicating an existing practice is often very difficult and the reason we sell 400+ practices a year."

"Competition is of minor consideration in the industry. Location is key. Good firms are in hot, growing areas and 'good customer services' and high prices run hand in hand with quality office spaces."

"The accounting/tax industry as it pertains to small privately owned locations has been steady for some years. Profitability has always been high and replication difficult, especially in the CPA field. As for risk, CPAs are the second best rated business loans to make—their default rate is very low."

"The industry is aging and recent decisions by the professional groups have made it difficult to enter. The ability to perform even basic marketing is limited, resulting in acquisition being a key growth criteria. Specialization in terms of market and product continues and while entry is easier, breaking into profitable niches is difficult."

"CPA firms usually have high client and revenue retention when properly transitioned to a new owner."

"It's easy to create a CPA firm but costly and time consuming to get the clients."

Benchmark Data

Statistics (Accounting Services)

Number of Establishments	89,188
Average Profit Margin	15.6%
Revenue per Employee	\$154,500
Average Number of Employees	5
Average Wages per Employee	\$65,930

Source: IBISWorld, March 2012

Products and Services Segmentation

Auditing	44.7%
Corporate tax services	21.8%
Consulting	17.4%
General accounting	16.1%

Source: IBISWorld, March 2012

Industry Costs

Profit	15.6%
Wages	42.5%
Purchases	3.0%
Depreciation	3.0%
Marketing	4.3%
Rent & Utilities	7.0%
Other	24.6%

Source: IBISWorld, March 2012

Market Share

PricewaterhouseCoopers	10.2%
Deloitte Touche Tohmatsu	10.1%
Ernst & Young	10.1%
KPMG International	5.3%

Source: IBISWorld, March 2012

Distribution of Employer Enterprises by Employment Size

Number of Employees	Number of Enterprises	Percentage of Total
0 to 4	35,787	68.5%
5 to 9	9,874	18.9%
10 to 19	4,210	8.1%

Source: IBISWorld, March 2012

"SDE should be 45% to 60% of Gross Revenue for the three- to five-person firm."

"Staff wages no more than 33% of revenue. Professional staff should annually bill 3 to 5 times their salary."

"SDE as a percentage of sales should be, as a minimum, 35%."

"Gross is the key."

"Most net approximately 40% to 50% annually."

"Employee should bill three times salary cost."

"Diversification of revenue source by industry and from individual clients. No single client over 10% of total revenue."

"Labor costs less than 1/3."

"Payroll should be less than 30% of gross receipts. Net earnings to the owner, including salary, can easily range from 30% to 50% of gross revenue."

"Adjusted net income of SDE can have a big impact. Industry average tends to be 33% of sales but can be much higher in a very good office."

"\$100,000 billings per employee."

"Solid accounting firms with gross revenues of \$100K to \$2 million tend to have SDE of 35% to 50% and even more in some cases."

"Hard to benchmark due to high fluctuations of billable rates. CPAs in the same community may bill from \$75 per hour to \$250 per hour or more depending upon size of firm and expertise. Professional staff should be able to bill 3 times their base salary."

"There should be gross revenue of \$100,000 to \$150,000 per employee if you expect to be profitable. Most practices have 35% to 50% of gross revenues dropping to the bottom line as SDE."

"Labor should be no more than 1/3 of gross receipts."

"We consider gross receipts of \$100,000 per year per person in the office is a benchmark indicating profitability. For a typical small firm from \$250,000 to \$450,000 of annual receipts, the cash flow to owner should be at or above 50% of gross in order to be a top firm. Cash flow percentages vary greatly and decline as annual gross increases."

"Should be \$100,000+ in revenue per full-time staff person, including the owner— more in given markets. SDE should be 40% to 50% of gross to sell for premium price. Anything under 40% and we start looking for problems."

"A successful CPA practice will value employees as well as clients. Finding and keeping good employees for work in public accounting is a distinguishing feature of a successful firm. Flex hours, on-premises nursery, and production bonuses are a few of the successful firm employee benefits."

"Annual growth rate in excess of 7 percent owner profit, SDE in excess of 40% of sales, stable revenues from recurring billings -- approx. 80% of total billings."

"Many firms generate gross revenues of \$100,000 to \$150,000 per staff person. Labor costs generally run around 32% of gross revenues."

"A successful CPA firm should bill \$100,000 to \$200,000 per professional staff member per year. Gross wages should be in the 30% to 35% range."

"Employee cost below 30% is excellent"

"Billing at 3 times employee cost"

Expenses as a Percentage of Annual Sales

Cost Of Goods :0% to 05%

Payroll :25% to 35%

Occupancy :10% to 20%

Profit (pretax): 35% to 45%

General Information

"Most of the smaller CPA firms either specialize in client audits or avoid all audits. A CPA firm that specializes in certain client types of audits may be more difficult to market or sell. 4 years' earnout method with 25% to 40% down."

"There is always a demand to purchase a good practice in a metropolitan area by larger firms and individuals."

"The industry is aging, with barriers to younger people coming in."

"Due to increased risk related to audit work, many CPA firms are no longer offering the service. Firms for sale with audit work may be harder to sell."

"Look for a strong non-compete agreement from the seller."

"Technology is at cross purposes to customer service in many cases. Having said this, there are many advantages to issues such as automatic fee collection and paperless approach."

"Successful firms should be easy to market. Non-compete from seller and staff important."

"Congress could potentially have a huge impact on the industry with the passage of a flat tax."

"This type of business generally requires licensure and certification by the accounting and tax regulatory agencies. Consult the State Board of Accounting in the state where you plan to practice. Go to the following Web page for a list of state boards and their contact information: <http://www.aicpa.org/yellow/ypsboa.htm>."

"State regulation must be understood, and depends on the nature of the practice. For instance if there is an audit element to the composition of the practice, only qualified individuals may own the practice."

"Many of the smaller firms will not do client audits due to the cost of insurance. Those firms with audit clients may not sell as fast or for as much as a small firm with no audit clients."

Advantages

- "Needed by everyone, regardless of age, income, geographic location. Personal relationship often drives the business."
- "The advantage is the ability to provide a necessary service to businesses and individuals that do not understand tax regulations or other government regulations."
- "Little fixed investment, marketplace growing. Also aging of competition."
- "Respected member of business community. Can usually work bankers' hours."
- "Recognized professional in the industry and business community."
- "Annuity-type income."
- "High profit for service business"
- "Low capital investment, relatively high margins, growing customer base at the lower end"
- "Strong profit margins, professional practice, ease in transferring the business"
- "Small amount of operating capital, increasing use of technology (reductions in operating expense), value of the knowledge industry, complications of government requirements, increasing legislation restricting entry"
- "Recurring revenues from a service business. Strong profits with relatively small practices."
- "Can be easily done as a sole proprietor at less than \$200K in annual billings. Technology continues to enhance practices. The market will always be there and customers tend to remain loyal, even in a transfer of ownership. Ongoing market need."

- "High profitability and continued strong growth within the industry."
- "Everyone needs accounting and tax help"
- "Good margins in client service businesses. Unlimited upside potential for a professional with a good mix of marketing and technical skills. Increased reporting scrutiny and regulation leads to increased demand for accounting services."

Disadvantages

- "Personal involvement and inability to duplicate for solo practitioner. Several of the services are dictated by the competition."
 - "Regulation on the increase"
- "Very long hours during tax season"
- "Service business that is hard to leverage"
- "Tough to leverage for most people"
- "Regulation, finding skilled employees"
- "Clients do not understand time required to solve their problems, and the hours of 'Tax Season.'"
- "Margins are near zero. Few if any professionals have succeeded in leveraging employees to the bottom line. Primarily all profit is a function of owner's personal production and services. In other words, this is more of a profession as opposed to a business."
- "Declining margins. Very significant increased competition, due to technology for tax preparation and bookkeeping becoming much more available to clients directly rather than being controlled by accountants."
- "Personal service business—you must be there. Not able to be absentee owner."
- "The public does not understand the work involved that results in fees charged."
- "Strict licensure and continuing education requirements are required in most states. Legal exposure can be high for certain types of services performed such as the audit function and financial planning services."
- "Qualified, dependable staffing can be difficult. Ongoing changes in both regulation of the industry and tax law. Tax season represents greatest earning period and greatest number of hours by the owner."
- "Long hours during busy season. Potential overhaul of tax code to flat tax would change this business significantly."
- "Lack of younger accountants going into the profession is a disadvantage. This lack of 'staff' accountants in public accounting forces those senior in the profession to work more hours on less profitable aspects of the job."
- "Personal service intensive"

Industry Trend

"Employee costs as a percentage of sales is an important number. 40% or less is considered good. Above this leaves little room for profits."

"Increased government regulations that will require more need by the small business for accounting and tax advice."

"Many baby boomers are getting ready to retire."

"Industry trend is upward due to increased tax and government regulations on businesses and individuals."

"Still a seller's market"

"Industry regulation makes entry difficult yet demand for services continually increase."

"An increase in the number of small single-owner firms billing \$100K or less as laid-off industry CPAs open their own firms."

"Shortage of staff accountants for public accounting "

"Many baby boomers will begin to retire."

"Changes in govt. regulation continue to increase. Strong likelihood of licensing for tax preparation will reduce competition, and aging practitioner base will reduce competition."

"More consolidations. More minority and foreign ownership."

"Steady to upward trend continues."

"Increased demand for tax advice"

"Number of sellers may increase."

"Specialty shops can be in the wrong sector and therefore be hit heavily by current downturn in economy. Market for new business and small business continues to be strong."

"Continued upward trend"

"CPAs may see increased revenues in years to come with tax changes. Costs not impacted by oil crisis, so rate increases go more to bottom line."

"An increase in the number of small firms changing hands due to the average age of firm owners approaching retirement age"

"More outsourcing and more retiring practice owners"

"Increasing exit from the profession. I see prices decreasing as supply of firms increases vs. a relatively decreasing number of persons entering the profession. This exit is because the profession is in decline and margins are shrinking."

"Although the marketplace of accountants is aging, there are excellent opportunities for the future entrants into the industry. Future government legislation will result in fewer competitors in taxation. The audit market has slowed with legal difficulties, but other sectors have expanded with government legislation."

"As baby boomer owners start to retire, more firms will come to market possibly lower prices."

"Consolidation of the marketplace continues, Specialization in terms of product and customer. More regulation imminent, especially in tax preparation."

"Consolidation as smaller firms (1 to 4 professionals) are purchased and merged into mid-size firms of 5 to 10 professionals."

Seller Financing

- "Four years earnout method with 25% to 50% down"
- "Seller financing is usually only a last resort."
- "3 to 5 years"

Questions

"What period of time will they guarantee the billings."

"Any client concentrations, risks of client losses."

"Why are you selling? Is any individual client fee over 10% of the Gross Revenue? Is any single industry over 10% of Gross Revenue? How much of Revenue is earned from tax return preparation and how much from accounting or auditing? What percent are corporate returns or individual returns? What type of client audits? What type of work does your staff do? What tax and accounting software do you use? What is the billing rate per hour? Do you bill by hour or project? How long have your clients been with this firm? How long have the employees been with this firm?"

"(1) Why are you selling? (2) Do you have any open complaints with the state CPA board? (3) Do you have any clients that represent more than 5% of revenue? (4) Do you require your staff to sign non-compete agreements?"

"What are the strengths of your firm? What areas can be improved? Have you attempted to sell on your own?"

"Client mix, services mix, average billings for services, accounts receivable and status of employees"

"How close is the seller to the end customer?"

"Why are you selling? Will you work part time? Will your staff stay?"

"Info relating to clientele, fee structure, employee information, pending litigation, office lease, type of services performed, need for licenses/certifications"

"Do you do any audit work? Are your licenses current? How many hours do you personally bill per year?"

"Why are you selling? Is any one client or industry over 10% of gross revenue? What percent of revenue is from tax, audit, bookkeeping? Client length of time with the firm? Staff knowledge and client contact?"

"Gross revenue for the last three years (trend). Percent of revenue from tax, audit, bookkeeping, or other. Number of tax returns by type, Audits by industry, bookkeeping clients monthly or quarterly. Client mix—by industry, profession, etc. and revenue per type. Client location by zip code. Any client over 10% of total revenue. Length of time as a client. Are there time and billing records? Staff-number, location, length, duties, competency, salary. Office lease time period. Tax software in use."

"The quality of the fees should be investigated both by looking at the cash flow percentages and investigating the billing rates of the personnel and the owner. Post- sale competition is a major risk factor so this possibility should be investigated carefully."

"Nature of clients and services, market definition, geography of practice, employees have a non-compete, accounts receivable status"

"Are there any concentration issues—any 3–5 clients that represent 10% or more of gross revenue? Take a look at A/R aging—could be a sign of deadbeat clients. Is there the potential for staff members to leave and take clients with them? Age of clients—if 80% over 65 years old, could be a problem. And the list goes on."

"Why you are selling, growth rates, stability of clients, composition of services offered and average fees"

"Revenue level? Growth rate for each of past 5 years? How many employees? What are rates charged to clients? Are there time and billing records? Why are you selling? How long have you been in business? What are the demographics of the client base? Age, location, size of businesses. What software products are used? Do clients come to your office or do you go to them?"

Resources:

Associations:

- American Institute of CPAs - www.aicpa.org