2015

The Good, the Bad & the Ugly of the Australian Accounting Profession®

BENCHMARKING REPORT & PRACTICE IMPROVEMENT GUIDE FOR AUSTRALIAN ACCOUNTING FIRMS

Developed & produced by

Business Fitness®
The Good, the Bad and the Ugly of the Australian Accounting Profession (The Good Bad Ugly) is the longest running publication of its kind in Australia, with this 2015 edition being the publication’s 14th edition. These fourteen years have earned the Good Bad Ugly a reputation as the most established, credible and reliable benchmarking report available to Australian accountants.

This report has been prepared on the basis of the data provided by the firms that participated in the Good Bad Ugly survey this year. This selection of firms is a cross-section of city, suburban and regional firms of all sizes, ranging from sole practitioner firms through to large multi-office, multi-partner firms. The data provided is based on the financial year ended 30 June 2015. Whilst we do not audit the data, we review each data set as it is provided and, where any data appears unusual or to be an outlier, the firm is contacted to verify the data in question.

**Get more insight**

This year’s Good Bad Ugly report presents the results from this year’s survey of key performance indicators in Australian accounting firms over the past financial year. As accountants especially will understand, when analysing firm performance, it is imperative that all key performance indicators are considered together rather than viewing individual results in isolation. When reviewing the results presented in this report, firms should ask themselves, “What actions do we need to take to improve performance across specific key indicators in our firm?”

To complement this valuable data, we have introduced our GBU Insight polls which puts the spotlight on current challenges the Australian accounting profession is facing. As a part of the profession, it is important for you to understand the challenges and how they can often present key opportunities for improvement and competitive advantage. The first step is to identify the challenges. The second and tougher step is to identify the opportunities and plan your next steps.
Foreword

By Stuart Spalding, CEO

The intention of our Good Bad Ugly editions over the last few years has been to showcase the digital revolution within the accounting industry, and convince the often stubborn number-crunchers of the nation to waste no time in transitioning to a more modern way of doing business.

We think our industry is past that. Past being told that a revolution is coming, past being told that it’s already here, past being told that it’s time to change. It’s not a question anymore.

The real question is how? How do we transition to the speed, the need for mobility, the new cost expectations and the shifting power balance between accountant and client that characterises our industry in this day? How will accountants do more with less, deliver what their clients’ actually need, leverage the opportunities of the global market, and stand out amongst fierce competition?

Already, we’re seeing process automation lead to a decrease in partner revenue, a declining average fee per client and a drop in staff productivity. Yet this extra capacity and revenue is, contrary to what the spruikers may say, not yet being replaced by business advisory services, which clients apparently desire but are unwilling to pay for.

And what should accountants be focused on in the new year? This year’s GBU highlighted three key areas of focus for the determined accountant: re-utilising or eliminating the extra capacity created by process automation, reducing the costs of compliance, and providing additional niche services.

At Business Fitness, we too are adapting to the rapidly fluctuating demands of the accounting industry. The new format and structure of the 14-year-strong Good Bad Ugly reflects this. With the consumption of knowledge becoming all the more in demand and easier and faster to obtain, we’re switching to a new structure. Each month, a new poll, themed around a trending topic in the accounting industry, will be available for online participation. The results of each poll will be published in mini-reports, which will be made available at no cost, for one month only, on our new website.

We will still publish a main report at the end of every financial year – however, as you’ll notice, we are updating the information across regular reports. We’ve cut down on all the bells and whistles to bring you nothing but the hard facts - the ones we know you skip straight to.

Welcome to the new and improved 2015 edition of The Good, the Bad and the Ugly of the Australian Accounting Profession.

Stuart A Spalding, CA
Chief Executive Officer, Business Fitness
Profile of a typical Australian accounting firm (based on median results)

- **Debtors**: 56 days
- **WIP**: 28 days
- **Write-offs**: 5.4%
- **Average hourly rate**: $174
- **Net profit (bps)**: $680,612
- **Net profit (aps $200k)**: $201,686
- **Revenue**: $1,983,511
- **Expenses**: $1,302,484
- **Productivity**: 70.1%
- **Partner return on effort**: $171 p/h

**Team profile**
- **Number of equity partners**: 2
- **Number of chargeable FTEs**: 7.3
- **Number of non-chargeable FTEs**: 3.0
- **FTE team members (inc partners)**: 12.3
- **Leverage**: 5.0
- **Chargeable vs non-chargeable ratio**: 3.6

**Distribution of survey participants**
- **NSW/ACT**: 29%
- **VIC/TAS**: 24%
- **QLD**: 21%
- **WA**: 16%
- **SA/NT**: 8%
- **NEW ZEALAND**: 1%
- **SUBURBAN**: 39%
- **CITY**: 31%
- **REGIONAL**: 28%

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GBU 2015
### Client profile

- **250 Clients per partner**
- **Average client group fee**: $3,327
- **40.4% SMSF clients** firms have more than 100 funds
- **Average SMSF fee**: $2,500

### Service profile

- **10.3% Other services**
- **6.9% Tax planning**
- **10.3% SMSF**
- **2.0% Other business advisory services**
- **60.4% Compliance (tax & accounting)**

### Over the past decade

<table>
<thead>
<tr>
<th>Area of focus</th>
<th>2005</th>
<th>2010</th>
<th>2015</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Revenue</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Revenue per partner</td>
<td>$543,050</td>
<td>$717,322</td>
<td>$821,663</td>
</tr>
<tr>
<td>Revenue per FTE</td>
<td>$97,964</td>
<td>$116,564</td>
<td>$131,808</td>
</tr>
<tr>
<td><strong>Net profit</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net profit % (BPS)</td>
<td>35.2%</td>
<td>45.0%</td>
<td>33.3%</td>
</tr>
<tr>
<td>Net profit per partner (BPS)</td>
<td>$176,212</td>
<td>$254,550</td>
<td>$272,122</td>
</tr>
<tr>
<td><strong>People</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Leverage structure</td>
<td>4.3</td>
<td>6.2</td>
<td>5.0</td>
</tr>
<tr>
<td>Salaries as a % of revenue</td>
<td>36.0%</td>
<td>29.0%</td>
<td>38.9%</td>
</tr>
<tr>
<td>Productivity – all FTEs</td>
<td>57.2%</td>
<td>64.0%</td>
<td>52.0%</td>
</tr>
<tr>
<td>Productivity – equity partners</td>
<td>56.9%</td>
<td>46.8%</td>
<td>48.6%</td>
</tr>
<tr>
<td>Partner return on effort</td>
<td>-</td>
<td>-</td>
<td>$152</td>
</tr>
<tr>
<td><strong>Other statistics</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Average hourly rate – after write offs</td>
<td>$106</td>
<td>$124</td>
<td>$146</td>
</tr>
<tr>
<td>Lock up days</td>
<td>100</td>
<td>66</td>
<td>94</td>
</tr>
</tbody>
</table>
Revenue & profits per partner plunge to 2012 levels
For the first time in 14 years of conducting the Good Bad Ugly benchmarking survey, revenue per partner has tumbled. A fall of 8.9% is quite significant. The story is not as grim when analysing the revenue on a per-firm basis which has declined by 4.5%. This goes against our recent GBU Insight Poll conducted in May 2015 where firms suggested they would achieve a 5% increase for the 2014/15 year. Revenues (per partner) have fallen from $1,017,922 in 2014 to $934,608 this year.

It is important to understand the reason behind such a fall in revenue, and the answer might be quite simple. This year, the Good Bad Ugly survey grew by 20%: that is, the number of contributing firms increased compared to 2014. In what we believe is a reflection of the profession, the increase in contributors was from firms earning revenues of below $1.5 million. Is this the future of the profession, smaller start-up firms embracing technology, minimising costs and therefore maximising profitability? It could also be that firms are thinking of future growth and added additional partners, which therefore has an effect on revenue and profitability per partner.

The second (and possibly more relevant) cause of such a revenue decline could also be due to the notion of digital disruption, cloud computing and consequently client fee resistance. Over the past few years the themes of the Good Bad Ugly report have been, “On the Precipice Change”, “Remaining Relevant” and “Digital Disruption”. Are we now seeing signs of a significant downturn in the profession? One of the major challenges identified by the contributors of the survey was ‘client fee resistance.’ This is the first time this has been identified as being a major challenge.

Average client fee nosedives for second year
Another first in the 2014 Good Bad Ugly revealed a fall in the average client fee by 10.2%. The results of the 2015 analysis show it has continued to nosedive a further 8.0%. The number of client groups per partner remains stable at approximately 250 per partner. Does this prove the theory compliance fees are falling and firms are not replacing these fees with other additional services? We believe this is to be the case.

Cashflow is the big winner
With the decline in profitability, the big winner from the 2015 Good Bad Ugly Survey has been cashflow. Firms have obviously put significant effort into WIP and debtors: debtors in particular where we have seen an improvement of five debtors days to 56. This equates to a $50k improvement in average debtors per firm. This could well be due to firms now collecting a portion of the client fee in advance and also implementing fixed fee arrangements and collecting monthly.

A quarter of the profession make a loss in 2015
When a notional partner’s salary of $200k is assigned, as with previous years approximately 25% of firms make a loss. We do this to provide a more of a realistic comparison of business performance rather than one based on a partnership model.

Automation causing falling productivity levels
For firms still focussed on timesheets and monitoring chargeable hours (approximately 90% of the profession), productivity for all staff is falling based on standard hours. One conclusion could be that automation is allowing staff to complete jobs faster but firms are then unable to use this additional capacity, therefore causing lower productivity levels based on chargeable hours. The other alternative is not to replace staff when they leave which seems to be a true measure of efficiency of doing more with less. Consequently, a more appropriate measure of efficiency would be profit per FTE, which is currently $17,249 after equity partner notional salary. Are firms who are not using timesheets more efficient using, this measure of efficiency?

How is your firm managing the additional capacity in your firm: reducing staff or providing additional services to your clients?

When analysing the 14 years’ worth of data relating to high-performing firms, we can conclusively say that productivity based on chargeable hours has no correlation to profitability.

New generation expenses
Operating expenses remain stable at approximately 63.5% of revenue. The most notable change in expenses items in this years survey was online subscriptions, which essentially doubled over the past 12 months, now comprising on average 1.4% of revenue. The number of firms who still do not have online subscriptions has
decreased to 28.6%. This has fallen from 61.7% of firms in 2011 when the average was 0.6% of revenue.

Interestingly, even with ‘finding new clients’ as the number two challenge for 2016, firms are spending less on marketing now than they have over the past three years.

**Business advisory services failing to increase revenue**

It seems the only firms benefiting from business advisory services are the industry providers and commentators suggesting it as a replacement for declining compliance revenue. As a whole, business advisory services fell to 12.1% of revenue. The two revenue groups reversing this trend were at either ends of the spectrum: the small firms earning fees of less than $500k and the larger firms generating $10m+ in revenue.

Survey after survey reveals that SMEs want these advisory services from their accountants, but the real question stemming from the 2015 Good Bad Ugly is “Do they want to pay for them?” The other relevant question is “Do accountants have the expertise and skills to be able to provide these services?”

Recent research would indicate otherwise, with accounting firms now hiring experts outside the profession to deliver such services. This goes against the 2014 GBU findings where 67% of firms were confident they could profitably deliver advisory services. On the other hand, it also revealed that a lack of marketing skill and expertise was the reason firms were not successfully delivering these services, with just 45% of firms confident of generating demand for advisory services.

So the question still remains: how will firms fill this revenue decline? Will it be through acquiring new clients through mergers and acquisitions? It is interesting to see the Big 4 accounting firms acquire businesses such as technology and data analytics firms. Will there be a mass exodus of baby boomers from the profession providing the opportunity of purchasing fees?

If winning new clients or providing additional services is too difficult, the other option is reducing operating costs.

Now is the best time to implement advisory services on your own business.

**Focus on reducing your compliance costs**

With falling revenues and additional services failing to compensate for these losses, the smart firms are reviewing their costs of compliance. Some predictions have firms minimising these costs by 25-30%.

With salaries obviously being the largest cost to your business, will there be an increase in offshoring of labour? Over the past 12 months we have seen an increase of 6% of firms who have recorded an expense for outsourced labour. At the moment this is still at low levels (just 1% of revenue).

The other alternative is to continue the path of efficiency improvement through process automation: Understanding and utilising the latest technology providing you a more cost-effective solution to efficiently and effectively servicing your valued clients.

**Insights from high-performing firms**

One of the most frequent questions asked of Business Fitness Client Managers is, “What do high performing firms do differently?” In a nutshell, high performing firms develop systems to ensure that they actually do more of what everyone knows they should be doing.

How does that translate into performance results?

- Partners are achieving $1.5m in revenue with seven people per partner;
- 55% of fees are through compliance services, with the average client fee being $6,938;
- Expenses comprise 58.6% of revenue, giving partners $350,183 profit after notional salary.