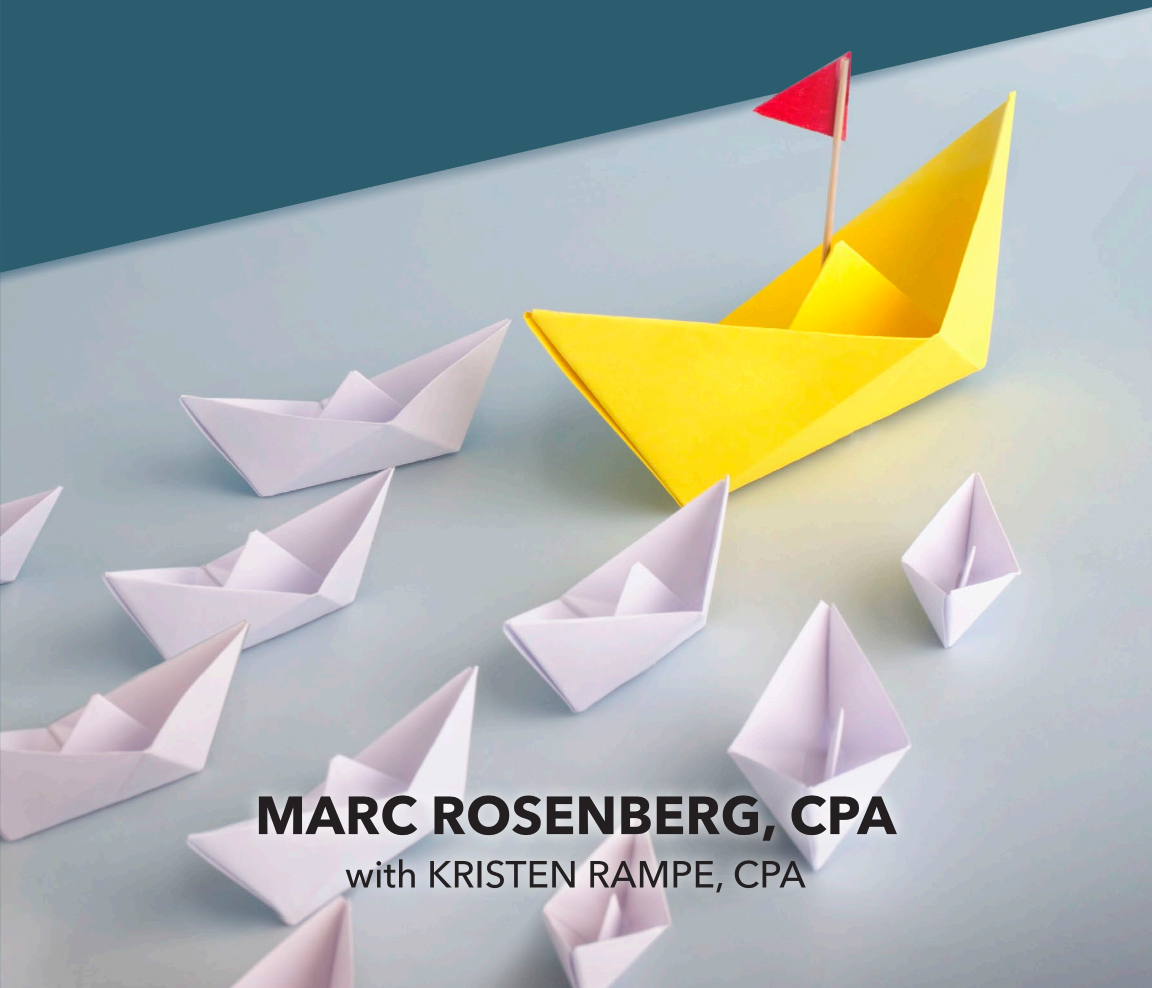
THE ROLE OF THE MANAGING PARTNER

The Definitive Guide to CPA Firm Leadership



MARC ROSENBERG, CPA

with KRISTEN RAMPE, CPA

THE ROLE OF THE MANAGING PARTNER

The Definitive Guide to CPA Firm Leadership

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1

Introduction

"Few things are more important to human activity than <u>leadership.</u> It helps countries prosper. It makes businesses successful. Parents help children become successful adults.

The <u>absence</u> of leadership is equally dramatic. Without leadership, organizations move slowly, stagnate and lose their way. We are taught that if decision-making is timely and correct, things will go well. <u>Yet a decision by itself changes NOTHING.</u> More important is <u>implementation,</u> and that's where organizations often fail.

Implementation is about how leaders influence behavior, change the course of events and overcome resistance. Leadership is crucial to implementing decisions successfully."

D. Quinn Mills
Harvard Business School Professor

Success Starts with Management and Leadership

Think of it. Whether it's countries, governments, businesses, education, sports teams, charities or nonprofits, when their histories are written, their successes and triumphs are attributable to strong, effective management and leadership.

- For the United States, it's founding fathers like Washington, Adams, Jefferson, Monroe, Franklin and Madison.

- For governments, it's Lincoln, Teddy Roosevelt, Angela Merkel, FDR, Golda Meir, Winston Churchill and Ruth Bader Ginsberg.

- For cultural change, we turn to Martin Luther King, Gloria Steinem, Gandhi and Mandela.

- In sports, the names of Vince Lombardi, Red Auerbach, Scotty Bowman, Pat Summitt and Tony LaRussa are forever linked with getting overpaid, undereducated athletes to sacrifice self for the sake of winning and their team.

- Titans in business such as Gates, Jobs, Ford, Bezos, Disney, Kroc, Welch and Watson built dynastic organizations that know no boundaries.

And yes, great managing partners of CPA firms, large and small, have led and built fantastic, growing firms by discovering the Holy Grail of accounting firm management: successful cat herding of CPA firm partners, showing them that the firm can achieve greatness by performing as a team rather than as a group of individuals.

My point is not to make MPs feel unworthy if they are not mentioned in the same breath as Jobs, Gandhi and Lincoln. Instead, I want you to see that the biggest factors in achieving organizational success are strong management and leadership. In a CPA firm, the leader is the MP.

Management Is Often Maligned

Regardless of the organization—CPA firms, manufacturing companies, sports teams, governments (especially!), you name it—management is often maligned. It's a shame, but it's hard to prevent people from thinking this way. Management is an easy target.

Humans have a natural dislike for being told what to do. CPA firm partners often feel they have an inalienable right to do whatever they want whenever they please (also known as lack of accountability). Effective leaders get people to follow without making them feel they are being *told* what to do.

Many top management people are indeed ineffective. CPA firms' managing partners have little or no management training or experience, so it's not surprising that their performance is unsuccessful. Besides, many MPs carry a significant client base in addition to their MP duties. How can they excel as MPs if managing the firm is not their #1 focus, both mentally and time-wise? They can't.

People tend to have a healthy skepticism of management decisions. CPA firm partners have a heavy dose of this cynicism because they often think they know more about managing the firm than the MP does.

I'll give you an example in the abstract art world. Most of us have seen some art that, on the face of it, appears strikingly simple. A Jackson Pollock canvas that looks as if someone randomly spilled paid on it. A Mondrian piece that looks like art any fifth-grader could create. I recently saw a pair of coffee cups in an art museum gift shop that nails this sensation to a T. The cup on the left says, "That's not art. I could have done that." The cup on the right says, "Yeah, but you didn't." The moral of this story is that many partners think they can manage the firm better than the MP, but they never step up and try.

Many firms have negative nellies who love saying, "That will never work" or "We've tried that before and it failed" or the ever-popular "Goal setting is a waste of time." If not dealt with, these negative people infect the minds of others, thereby preventing management from doing its job.

Leaders are often tempted to make self-serving decisions. Unfortunately, throughout all walks of life, we've seen countless examples of this, including the most visible of organizations: government. (My apologies; remember, I'm from Chicago!).

As a result of these challenges, leaders have to build a sense of trust by the governed before they can do their jobs effectively.

The Flawed Operating Model of CPA Firms

This section is bound to raise the hair on your neck. I'm going to expose the traditional model of operating a CPA firm for what it is, deeply flawed. The message of this section is that it's the MP's job to *correct* the flaws.

The points I make primarily relate to multi-partner firms with annual revenue under $20M, which represent more than 99% of all firms. Understand this: Larger firms *became* larger firms because they overcame these flaws.

1. Leaders of firms—the managing partners —are often burdened with a significant client base to manage, limiting their ability and time to focus on what should be their #1 client: the firm.

   Advice: New MPs should delegate a minimum of 50-75% of their clients to others. The better MPs never worry about what will happen if they stop being MP.

2. Too often, partner groups require votes to be taken on minor decisions before they can be enacted.

   Advice: Businesses cannot be effectively run like a democracy. MPs must have broad authority to make daily decisions without having to take votes.

3. The following are examples of the wrong people assuming the mantle of leadership:

   - The founding partner is the MP. Obviously, this is an intuitive choice. But often the people who use their entrepreneurial skills to create a CPA firm are lousy managers. We've seen many firms flatten out after an initial startup surge when the firm becomes too big to ignore management.

   - The rainmaker is made the MP. What made the rainmaker successful? You know the stereotype: Outgoing personality, charm, a drive to make everyone happy. But often, they lack organizational and planning skills and are not good at administering tough love or discipline.

- A retiring MP is automatically succeeded by the next oldest partner. I think you can see the folly in this without my expounding on it.

Advice: Install MPs who are qualified for the job due to their leadership and management skills, period.

4. The firm is run like a group of sole practitioners practicing under one roof, sharing staff and overhead. Each partner has his or her different way of doing things. This focus on the individual is reinforced by (a) antiquated compensation systems that place excessive weight on Finding, Minding and Grinding to the detriment of intangibles such as teamwork and developing great staff and (b) little or no partner accountability.

   Advice: Embrace the word "synergy." A firm can achieve so much more by working as a team than by relying on individuals to carry the day.

5. Michael Gerber's *E-Myth* encourages business owners to work *on* their business, not *in* it. Partners are really executive vice-presidents and should function like executives who delegate and develop people under them. Unfortunately, many CPA firm partners never got this memo. They commit the following sins:

   - Post high amounts of billable hours (over 1,000), many of them for staff-level work, and wear this dubious accomplishment like a badge of honor.

   - Firms often *say* their staff are just as important as their clients, but they rarely walk the talk. Successful executives in any business are driven by the need to develop personnel and help them learn and grow.

   Advice: Arguably, the MP's most important job is to get the partners performing like executives, not glorified doers who are guilty of the above excesses.

6. Strategic planning is nonexistent. Because everyone is so busy with client work and all are rewarded with compensation that most would consider extraordinary (partners earn $300,000 to $600,000 on average), firms have a strong tendency to operate like a factory: Get work in and get it out, endlessly repeated. Focus on today and forget about tomorrow. Fatal flaws of this dynamic include these:

    - The firm evolves into a high-volume/lower-priced firm instead of the higher-priced/lower-volume shop that it should be.

    - There is little succession planning.

    - The firm focuses on compliance work while ignoring the tremendous consulting opportunities with *existing* clients who need these services and will pay premium prices to get them.

    Advice: The MP must be the *one* person in the firm who *never* loses sight of the big picture—what the firm should be tomorrow that it is not doing today.

You might say: "How can our model be so bad if partners earn $400,000, $500,000, $600,000 or more?" Here are my responses:

- Many CPA firms earn handsome profits in spite of themselves. If they were managed more effectively, they might increase their earnings by 25% to 50% or even more. They are leaving money on the table.

- Just because life (and profits) is good today, there is no guarantee this will continue in the future. As someone who has consulted to a thousand CPA firms over 20 years, I can testify to the many once-great firms that were mired in mediocrity when they hired me. Mistakes, poor judgment and short-sightedness came back to haunt them, dooming their firm with fatal problems.

- Most firms would prefer an exit strategy of staying independent as they bring in new partners, thus preserving their legacy. But for most firms, this option doesn't exist because historically they have failed to focus on planning for succession and developing future leaders. As a result of neglecting these areas, they have little choice but to eventually merge out of existence. 80% of first-generation

CPA firms never make it to the second because their succession planning sucked.

This flawed operating model presents serious obstacles to the MPs' efforts to manage the firm like a real business—before they even start their jobs. The extent to which MPs can correct or avoid these flaws goes a long way to determining the success they will achieve in the future.

The Management Philosophy of a CPA Firm

The diagram on the next page is very powerful. Many firms (and their managing partners) make the mistake of managing the firm from the bottom up on the chart. They appoint a MP, adopt a governance structure (department heads, executive committee, partnership agreement, chief operating officer, etc.) and manage the partners' performance and behavior mostly with the "messages" sent when allocating partner income.

The correct way to manage a firm is, of course, to start at the top and work downward:

The bus. Jim Collins, in his legendary book *Good to Great,* writes, "Before a firm begins strategic planning, it must first get the right people ON the bus and the wrong people OFF the bus." Negativity and skepticism among partners can spread at the speed of light if unchecked. These people must be either dismissed or put in a position in the firm where their harm is neutralized.

The vision. Once the proper team is on board, it crafts the firm's vision. What does it want to look like in 5 to 10 years? What is the firm's mission? Its driving forces?

Firm goals. After the vision is firmed up, next is deciding the specific firm-wide goals needed to achieve the vision.

Partner goals. Firm-wide goals can't be accomplished without people to execute them. The partners and other firm personnel are the ones to accomplish the goals.

The Management Philosophy of a CPA Firm

Right People on the Bus,
Wrong People Off

⇩

Craft the Vision

⇩

Determine Firm Goals

⇩

Determine Partner Goals

⇩

Run the Engines

Leadership
Governance Structure
Accountability
Partner Compensation

The engines. Before the "Engines" level of the chart, the firm is like a car that has come off the assembly line but whose ignition has yet to be turned on. The four engines that propel the process and keep it running and finely tuned are these:

- **Leadership.** Every firm needs a champion.
- **Governance structure**. Establishes order and defines duties.
- **Accountability**. Makes people responsible for their role in the firm and establishes consequences for failures.
- **Partner compensation**. Incentivizes and rewards performance and behavior.

This chart illustrates the big picture of managing a CPA firm. It's the managing partner's job to never lose sight of this philosophy.

The Antithesis of the MP: Management by Committee

There is an intuitive notion that comes to partners that goes something like this: "Let's all get together and form a firm that will make us *all* more successful than any of us could be individually. We'll follow the principles of democracy by dividing up the management duties so that no one is overburdened. The partners will make decisions as group, thereby avoiding vesting too much power in one person."

Management by committee is doomed to fail. This chart refutes the excuses partners often give for favoring management by committee.

Why Management by Committee Doesn't Work

Reasons Given for Management by Committee	Why These People are Wrong
1. We don't want one person with too much power. As a democracy, we all want a vote.	A business cannot be run effectively as a democracy. Someone needs to be in charge. Management by committee waters down decisions and lends itself to endless procrastination.
2. None of us has the charisma to be the MP.	Jim Collins said, "Great leaders act with quiet calm & determination, relying on inspired standards, not charisma, to motivate."
3. No one has time to be MP. Splitting up the admin time spreads the burden to all of us.	When partners do admin work, they *lose* money for the firm because instead of partners doing partner-level work, they spend large chunks of time doing the work of a COO or firm administrator, who earns far less than a partner.
4. Our rainmaker would be our best MP, but we'll lose money if we take him or her away from selling.	A rainmaker who has the skills to manage the firm will make everyone else more effective at business development. Besides, MPs should continue wearing their rainmaker hats while they manage the firm.

Line partners should welcome the presence of a managing partner because it (a) ensures that at least someone is making the firm their #1 client, (b) keeps them out of tedious admin tasks that can be performed more effectively by lower-paid people and (c) allows them to focus on the two things that matter most: taking great care of clients and staff.