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The Case for Accountancy: Why Private Equity Investors Are Targeting the Sector

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Accountancy has become one of the most attractive areas for private equity investment, with numerous recent high-profile deals making headlines. Several key business fundamentals make accountancy practices appealing to PE investors:

1. **Revenue:** Accountancy firms generate a highly predictable revenue stream, with approximately 70-80% recurring revenue from annual services such as audits and compliance. This is supplemented by 20-30% advisory work, offering opportunities for one-off revenue spikes. This combines recurring income with potential for revenue growth from higher margin specialized services.
2. **Up-Sell Opportunities:** Once a firm is engaged with a client for core services, such as accounts preparation and advisory, there is a significant opportunity to expand into payroll management, tax, advisory and corporate finance services. This approach increases revenue potential without significant new client acquisition efforts.
3. **Fragmented Market:** The Big 4 accountancy firms primarily focus on servicing large global companies, creating a space for mid-size to small firms to pick up under-served clients. Recently the Big 4 have actively shed smaller audit clients due to increased regulatory scrutiny, risk and operational efficiency concerns, opening market space for smaller accountancy providers. This fragmented market not only enables organic growth but also provides ample buy-and-build opportunities for PE investors pursuing roll up strategies.

The Big Risks

There are clear advantages to investing in accountancy, but what makes good accountancy practice and what are the big risks for investors?

Accountancy is a relationship driven industry, making it susceptible to keyman risk. If critical partners who hold key client relationships leave post-acquisition, there is a risk that revenue streams could be significantly impacted. This issue has previously arisen in wealth management roll-ups, where client departures post-deal weakened some firms. To mitigate this risk, investors should consider including enforceable non-compete obligations, proper manager incentivization and strong leaver terms to retain talent.

In addition, as part of their due diligence investors should ensure the business has good quality management who can hit their targets, meet their ambitious business plan, and grow the business both organically and inorganically. They can keep managers focused by asking them to rollover a significant stake in the business into the new structure and align their interests with the investor's through a good equity incentivization plan.

Integration should be a top priority during the due diligence phase, as it often poses the greatest challenge in accountancy roll-up strategies. It is crucial to verify whether the target has properly integrated the businesses it has acquired, across areas such as corporate structure, CRM systems, line of business apps, data management, terms of business and PI cover. Effective integration ensures seamless collaboration, allowing an employee in one office being able to assist a partner in another location without operational friction.

Regulatory

Accountancy transactions present unique regulatory challenges, particularly for firms offering audit services. ICAEW regulations require these firms to be controlled by appropriately qualified individuals, which can complicate standard corporate structures. Businesses offering probate or other non-standard accounting services may face additional regulatory approvals and governance requirements. Investors will also need to carry out merger control & NSIA analysis and make a post-completion notification to the regulator. Accordingly, expert professional advisers with industry-specific experience is key for deals in the accountancy sector.

What's Next?

The UK accountancy market remains highly active, but with increasing competition, many private equity sponsors are now exploring European bolt-on acquisitions. The lower entry multiples in certain European markets, combined with a high standard of work, present attractive investment opportunities.

While accountancy remains a promising sector for PE investments, success requires careful risk management, leadership, retention strategies and regulatory awareness. As the market evolves, exploring European expansion strategies and partnering with expert advisors will be critical for maximizing returns.

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