

## GOODWILL - THE KEY TO VALUING A PROFESSIONAL PRACTICE

### Professional vs. Practice goodwill

“Professional” goodwill derives from the individual practitioner’s reputation and personal success in the profession, and the trust and respect that the individual practitioner has engendered in his or her clients.

“Practice” goodwill relates to the firm’s ability to continue to generate earnings without the presence of any particular professional. Location, computer systems, staff, operating procedures, and a recurring client base are all elements of practice goodwill.

Much of the value of a professional practice consists of goodwill; its reputation, client base, knowledge, technical skill, research, brand awareness, and associations that the firm maintains. The goodwill of a practice is the most intangible of all assets. It can only be valued in terms of a going-concern business and cannot be separated from the business as a whole.

**NOTE:** You should be aware at all times that valuing goodwill is not an exact science, rather, the weighting given to many of the factors which makes the worth of your practice differ from apparently similar firms, can only be accurately predicted by a valuer with a great deal of experience. For example, the impact on the value of the goodwill of a practice which has no time recording system in place or is not registered for VAT or has recently been the subject of an adverse JMU report, can only be deduced through empirical experience. Make sure your valuer has the experience you need.

### Methodology

There are many factors impacting on the value of the goodwill of a practice, but in all cases the value relies on the principle of willing buyer, willing seller at a given time. The value of the goodwill will not necessarily be the same if, for instance, it is being purchased as an integral part of a practice being sold on the open market as a going concern, compared with a block of fees being sold unencumbered by any overheads such as staff, leases, or as a result of insolvency or the death of the principal. Additionally, investment in computer systems, key staff, etc could reduce current profitability but increase considerably ‘the hope value’.

For partners who want a valuation for internal reasons, where a partial sale is not being contemplated, APMA normally suggests the practice be valued as if it were being offered, together with the relevant members of staff, computer systems, etc., on the open market, sold for a capital sum on a ‘going concern’ basis. We would make the assumption that the principal(s) would be prepared to stay or leave, and the practice would remain in situ, or be moving into a purchaser’s own offices, thus giving the market flexibility. If your circumstances require other factors to be taken into account, be sure to advise us accordingly.

There are 3 methods which APMA uses for valuation purposes, each is charged at a different rates. Phone Jeremy Kitchin at APMA for further information on 01623 883300 (usually up to 10.30 p.m.):

**1. The summary valuation – given free of charge.**

The first is for me to produce a summary valuation which will give you a multiple range and can usually be given over the phone after the principal / partner / director has answered some simple questions on his / her practice statistics.

**2. The Desk Top valuation (a short written valuation) – cost on application.**

This is a two or three page report which draws some conclusions from the stats which you will provide using a less comprehensive (chopped down version) of the below VALUATION QUESTIONNAIRE, which can be obtained by contacting APMA. This valuation will be given without dwelling on the background to our findings and will place your goodwill in a range of two multiples, taking into account the following criteria:

- A. With up to 80% of accounting firms having two or less partners, small parcels of fees command higher multiples .
- B. Larger practices are more attractive if in towns or cities.
- C. The greater the density of firms in the immediate surrounding area, the greater the demand.
- D. If the average fee per client is small, it will attract small practices and first time buyers.
- E. A below average charge-out rate will attract a below average multiple.
- F. A recent adverse JMU report spells problems!
- G. If key members of staff are not bound by restraints of trade, particularly self-employed and sub contractors, purchasers will disappear.

**3. The full written analysis and valuation – cost on application.**

Using the completed VALUATION QUESTIONNAIRE (below), this will be a comprehensive report detailing your firm's comparative position in the market place, its current value and the reasons behind the valuation. We will expand on the mechanism used for the value obtained and draw distinctions between the valuation of your goodwill and that of a commercial corporate business. From that comparison we will set out ways in which the value of your firm can be enhanced and detail how the firm may be developed using different forms of marketing, signposting you towards a low cost way of consistently increasing the firm's fees, year on year. A comprehensive 9-page valuation thesis, which is copyright, is available to purchase from the Documentation page on our website. It covers the valuation of goodwill, will give you a useful understanding of how the goodwill of an accountancy practice is valued and will enable you to track the evolution of your practice over the years to come.

## VALUATION QUESTIONNAIRE

### 1. BASIC INFORMATION

Practice Name

Practice Address

Telephone No: .....

Contact Name

Contact Address

Telephone No: .....

Contact E-mail Address

Location of additional offices:

Details of any trading companies owned by the practice:

Reason for the valuation request:

### 2. DETAILS OF THE PARTNERSHIP / COMPANY

A. Chartered Registered Auditor? FSA?

B. Details of partners / directors, ages and qualifications

1 ..... 2 .....

3 ..... 4 .....

Does the firm employ any relatives of the partners or directors? Please explain.

Please attach a copy of a partnership agreement / director's employment contract –

### 3. SUMMARY FINANCIAL ANALYSIS

A. Summarise below your last 3 yrs results projections for the ongoing year.

YEAR ENDED (oldest first)	GROSS FEES	Gross payroll cost	Overhead	Salaried Partners	PROFIT (after rent & Salaried Partners) BEFORE PARTNERS SHARE
200					
200					
200					
Projected					

#### BALANCE SHEET SUMMARY

YEAR ENDED (oldest first)	DEBTORS	DEBTORS DAYS	WIP at full charge out	WIP Days	LOANS And Overdraft
200					
200					
200					
Projected					



Rent	Rates	Heat	Lights	Insurance	PI	Other Business Expenses

E. If the property is rented:

What Type Of Lease Is There?	How Long Is The Present Lease?	When Is The Next Rent Review?	What Accommodation Does The Property Have?

F. What car parking facilities are there?

G. If it is vital that your clients should be serviced from your existing offices, please state

why: ..... **Not vital\*/Vital\*** because.....

**\*circle**

## 6. HOW CONTACT IS MAINTAINED WITH YOUR CLIENTS

A. What percentage of your work is carried out on the client's premises?

B. In general terms, where are your clients located?

C. What percentage of your clients deliver their books/accounts to you?

## 7. PRACTICE LOANS

Give details of the loans to the practice, security and interest rates and repayment terms.

## 8. EXTENT OF COMPUTERISATION

Which of these do you use and what percentage is computerized?

A/CS PREPARATION	PERSONAL TAX	TIME & FEES
IRIS?	IRIS?	Minuteman?
SAGE?	PTP?	IRIS?
Auditman?	Taxman?	Star?
Other	Pertax?	SAGE?
	Other?	Other?

## 9. CONTINGENT LIABILITIES

Describe any claims or potential claims, against the practice in the last 3 years and state the position on professional indemnity insurance cover, i.e. total cover, any excess and current premium charged.

**11. CLIENT ANALYSIS**

A. No of clients split between

B. Split of clients by fee range:

Below £250			Sole Traders	
£251 - £500			Partnerships	
£501 - £1000			Limited Cos	
£1001 - £5000			Tax Only	
£5001 - £10000			Others	
£10001 - £20000			<b>TOTAL</b>	

**12. CLIENT SCHEDULE.**

The key component in the valuation of an accountancy practice is its goodwill, which is vested in its clients. For this reason it is necessary for the clients to be comprehensively analysed, preferably under the below headings.

1. Name (or code number) of client
2. Industry type (fish & chip shop, financial services, club, building sub-contractor, light engineering, etc.)
3. Type of Business: sole trader, partnership, limited company, PLC, tax only, etc.
4. Estimated turnover of client.
5. Gross Fees rendered to them per your accounts, etc.
6. Gross Fees likely to be invoiced, where different from 5. (above) by the new owner, in the first 12 months following acquisition, which you are prepared to warrant.
7. Method of invoicing: annually, quarterly, monthly, etc
8. Type of Work Done: audit, accounts preparation, management accounts (quarterly/monthly) cash flows, tax work, payroll, etc.
9. Location of Client (a broad indication is sufficient) i.e. North Staffs, etc
10. Length of Time as your Client (if known).
11. If known, is the Principal over 60 Yes\*/No\* \*circle
12. Year End

Compiler's signature .....

Date compiled .....