Practice Management

Elixir Consulting's Sue Viskovic talks to advisers about the impact of the Future of Financial Advice (FoFA) reforms on the valuation of their business, and how risk-focused practices continue to maintain their value...

What's your business worth now?

With most advisers getting their head around the implementation of the FoFA reforms, there continues to be a lot of interest in what impact the reforms have had, and will have, on the valuation of advice firms.

Last month, I invited Steve Prendeville of Forte Asset Solutions to conduct a joint webinar with me, to discuss what effects FoFA is having on business valuations, and to share our knowledge on what an advice business owner can do to maximise their ultimate return for their years of hard work.

Let's take a look at what happened in the mergers and acquisitions space for individual advice practices in the last year. Steve shared with us:

"Throughout my 11 years' experience, demand has been constant until the last quarter of the financial year 2013. For the first time, we are seeing what can be described as a buyers' market. Buyers are able to dictate terms and conditions that are without precedent.

"The reason for the sudden and quite dramatic reduction of buyers is a direct impact of FoFA – a combination of the difficulty in meeting Fee Disclosure Statement (FDS) requirements, the potential threat to revenue as clients receive their FDS, and the resulting increase in compliance and operational expenses. The threat to volume overrides will also reduce the potential aggregation synergies for buyers.

"The 12 month experience to 30 June 2013 has witnessed the greatest spread of buy/sell ranges with the largest number of variables impacting the valuation of a practice. The primary variables influencing pricing have been, in no specific order:

- Client service segmentation – specifically engaged or active clients versus non-active (with the latter decreasing the value of the business)
- Platform choice – in-house or mainstream, and the ease of movement of FUM to achieve synergy benefits
- Investment management philosophy – the use of direct versus managed funds, performance, and the ability to duplicate or scale Intellectual Property
- Product segmentation – risk versus super/investment versus corporate super (in descending order of value)

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"The range experienced over the 12 months to 30 June 2013 was from 2.5 times to 3.5 times recurring annual income, with the broad historical assumption of 3 times being challenged as we enter the new financial year."

Steve shared that recurring income from risk insurance is still attracting premium returns, with multiples around 3.5 times recurring revenue, in light of the retention of risk commissions, post FoFA. Quality of data is still being assessed within a risk book. According to Steve, the key determinates to value are:

- Age of the client base (preferably less than 55)
- Lapse rates coming in under 8%
- Product type (life, trauma, TPD, etc)
- Compliance history
- Quality of electronic client files
- Referral relationships - the preference is for consistent new business generation
- Relationship strength - with a preference for regular two-way communication with clients, rather than transactional policy holders

Interestingly, while risk businesses are currently still attracting strong multiples, there are some who question whether the carve-out of risk commissions from FoFA is a permanent situation, or merely a stay of execution. The longevity of commissions on insurance will have a direct impact on the valuation multiples applied in future.

By far, the biggest influence in achieving maximum value for your business is the quality of the relationships your firm has with your clients, with a close second being the quality of the data you can provide a potential buyer. A clearly segmented client base, who receive well-documented services that are directly aligned to the revenue they generate, backed up by efficient processes, will not only achieve healthier profit margins but also provide high quality data that you can supply to a potential

buyer. A business that has engaged clients who actively participate in the ongoing services provided by their adviser, and which has a successful marketing strategy that results in a steady flow of new clients, will attract a greater premium.

Whether you're looking to improve your business purely for your own satisfaction, or to increase your immediate and eventual returns from it, here are five key questions to ask yourself in order to provide clarity on where you can best focus your energy:

1. Are you clear about the types of clientele that you want to work with, and have you designed your services to suit their needs? If not, get specific about who you're looking for and enhance your services and engagement processes to suit their needs. Can you position yourself as an expert in a certain niche?
2. Is your client base getting older as you are getting older, or do you have an effective way of generating regular new business, particularly attracting more of the right type of clients for your firm?
3. Are your current clients actively engaged with you, or do you have a large book of transactional policy holders and customers? Once you're clear on who you'll best work with in future, determine which clients in your current base are likely to fit these criteria and actively seek them out to discuss their current needs. Even if they haven't responded to previous approaches to review their affairs, make a personal phone call to discover if they do, in fact, have greater needs that you can now solve, and aim to re-activate your relationship. For risk-only clients, in the very least, you should confirm that their needs are the same and that the risk solution provided is the best available and reflects their current circumstances. Provide what clients want most of all: peace of mind that their families are protected, in a cost effective manner, and with the knowledge there is someone in their corner who cares.

recurring income from risk insurance is still attracting premium returns

4. Do you have quality data on your current client/customer base? Is it managed effectively with the use of technology, and can you easily access information by client segment? If not, get serious about improving your systems and processes. While this may be seen as an administrative cost, it will likely generate financial returns as you gain greater clarity on your customer base, which will enable you to re-engage clients and better service their needs.
5. Finally, can you clearly articulate the various service levels you offer clients, and are they compelling enough for clients to sign ongoing service agreements on a regular basis? The bottom line is that if your clients continue to enjoy and benefit from your ongoing relationship – if you are continuing to have a truly positive impact on their lives – you will enjoy greater sustainability of revenue, and a greater return when the time comes for you to exit. Whilst risk-only businesses have not yet had to think in these terms, it's a wise move to do so, in case you need to move to a fee model for risk advice too.

A recording of the Elixir/Forte Asset Solutions webinar is available from the Elixir Consulting website: www.elixirconsulting.com.au/

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