The 10 tenets of running a firm

Maureen Broderick tracked down the chairmen and CEOs of the Big Four, as well as more than 100 other leaders, to shed light on the art of managing a professional service firm

Operating a professional service firm (PSF) is very different from running a product-based business. Infrastructures, governance, talent management, compensation and profitability vary significantly from traditional corporate environments. Leaders will tell you that managing a successful PSF is challenge that requires a delicate balance between structure and autonomy, and a unique leadership style – not to mention the enormous challenge of managing an organisation of extremely smart, highly autonomous, and somewhat quirky professionals. It's definitely not a job for the faint-hearted.

In researching my new book, *The Art of Managing Professional Services*, I conducted more than 130 interviews with leaders of the world's top firms – including Jim Turley, chairman and CEO of Ernst & Young; Jim Quigley, CEO of Deloitte; Tim Flynn, chairman of KPMG; and Dennis Nally, chairman of PwC. What emerged were their proven practices on how to tackle the 10 critical areas that leaders must monitor to build and maintain a strong organisation: vision, values, and culture; people; clients; services; finance; positioning; partnership; strategy; structure; and leadership style.

To keep the firm operating at maximum strength, leadership must constantly tinker with each of these critical pieces of the organisational puzzle. But even the best firms in the business can find themselves out of alignment at certain times. And virtually all of the leaders interviewed admitted that many areas of their organisation need attention and improvement. The key is maintaining a vigilant focus on the firm's vision, values, and culture – the anchor and core of every successful professional service firm.

1 Vision, values and culture

The leaders of the professional service firms interviewed were passionate about their firms' values and culture. Values are the bedrock of the organisation – the rules that govern behaviour toward colleagues, clients and the communities in which they serve. In successful firms, adherence to the values is cultivated and rewarded: failure to comply can result in expulsion.

The organisations we studied devote an enormous amount of time and resources to embedding their values and reinforcing their culture. In fact, the leaders we interviewed agree that the preservation and nurturing of their firm's vision, values and culture is their number one job.

2 People

You might expect that professional services would be good at talent management. After all, people are the product. Without committed, highly skilled people, there is nothing to sell. Some impressive best practices are discussed in the book, but perhaps the most important lesson is that people are treated with respect. Their opinions are valued, they are trusted to interact with clients early on in their careers, and their contributions are expected and rewarded. Successful firms invest significantly in recruiting, career management, training and mentoring of their professionals.

3 Portfolio

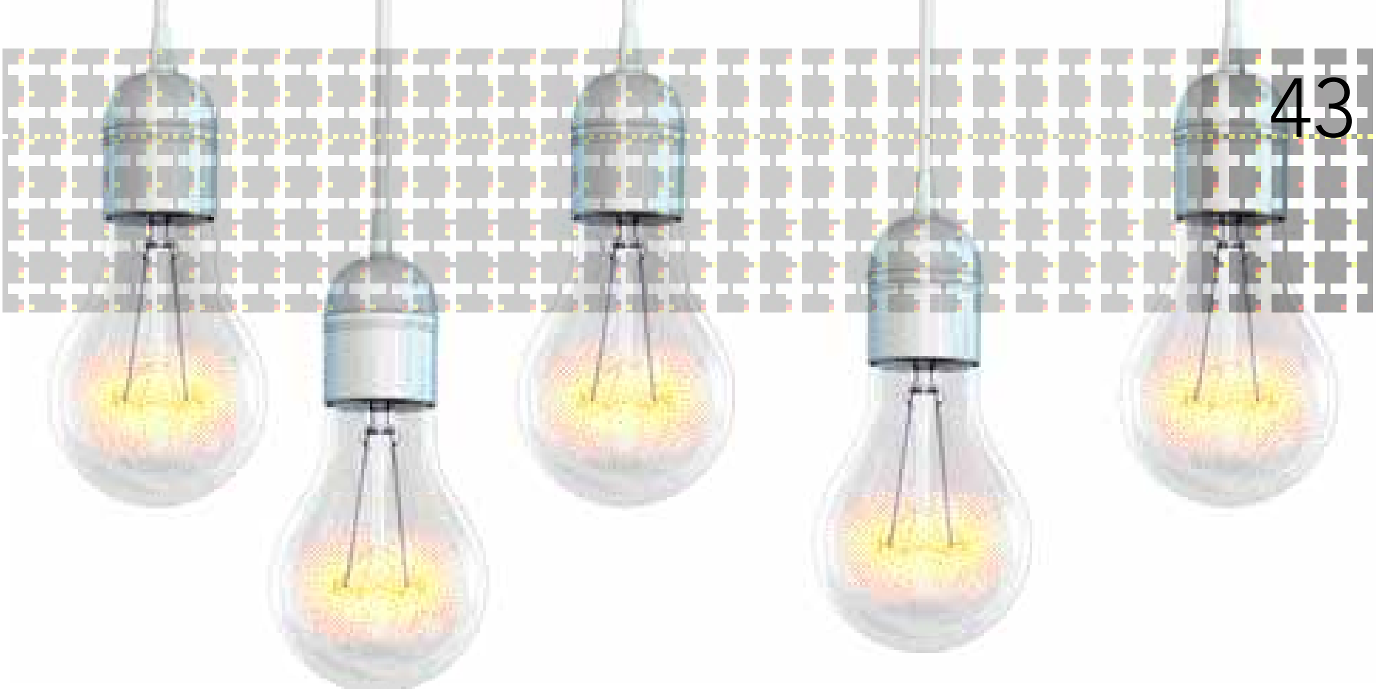
For PSFs, the client base, in effect, defines the business. Clients represent much more than a revenue stream: they are the magnet that attracts other desirable clients as well as top professionals to the firm. The client base helps shape a firm's brand and has a powerful influence on its reputation and standing in the marketplace.

The best-run firms follow five steps to effectively manage the client cycle from concept through acquisition, retention, and renewal. The cycle begins with strategically planning and regularly reviewing the client mix.

As clients come on board, they are carefully introduced into the firm and are nurtured and managed throughout the relationship via a well-defined process to sustain, grow, solicit feedback and improve the client relationship. The cycle is completed with regular reviews of client profitability, partner management and relationship status. Each step in the cycle is integral to building a profitable client base that sustains and nourishes the firm and its professionals.

4 Services

If talent is a firm's lifeblood, then an effective service portfolio strategy represents the arteries through which that talent is channelled – and innovation keeps the whole system healthy and energised. Leaders agree that successfully managing service development and renewal is a continuous cycle of activities



that begins with a portfolio review to identify gaps and retire services that are no longer relevant. It continues with 'ideation', the often complex task of stimulating and capturing new ideas.

The next step is selecting the best candidates for development. And finally, ideas are transformed into viable service offerings, the troops are trained on delivery, and the services are launched. Gathering and sharing knowledge and client experiences is integral to the ongoing success of a service strategy. Each step of the cycle is important in creating a consistent engine of innovation.

5 Finance

On the surface, professional services seem like simple businesses to manage financially. As one leader told us: 'It's mostly a time and materials business driven by rates, revenue, utilisation, realisation, and expenses.' But there are nuances that make it challenging. In the short-term project-based PSF environment it is almost impossible for many leaders to see beyond the window of a few months, which makes revenue forecasting a distinct challenge. The top firms have a clearly articulated financial strategy that establishes revenue and earnings goals, and responsibilities for financial performance. They are rigorous at tracking key financial metrics – both lagging and leading indicators – and invest in the people and the analytical tools that provide timely, action-orientated financial information. Cash flow is king, as one CEO told us: 'If a firm has cash, it's a well-run place. If it doesn't, it isn't.'

6 Positioning

In professional services, positioning is what you stand for. Positioning defines what the firm does, how it does it and why it is different from other organisations. To succeed, a PSF must identify a credible position to occupy in the market.

Determining positioning involves decisions on a number of fronts. Will you be a lower cost/higher-volume provider, or will you offer high-cost, unique solutions to unique problems? What specific services will you sell? Which segments, geographies, companies and buyers will you target? What is the service experience the firm will create for the client?

The best firms know who they are and what they do, and are masters at communicating their positioning, both internally to staff and externally to their market.

7 Partnership

The term partnership has a very special meaning in professional services. Much more than a type of ownership structure, the concept of partnership is both an industry mindset – a core belief that everyone is in it together, united by a common vision and cause – and a distinctive set of governance characteristics.

A successful partnership-driven governance model is based on shared values, collaboration and teamwork, peer relationships, highly participatory decision-making and equity sharing with partner/owners.

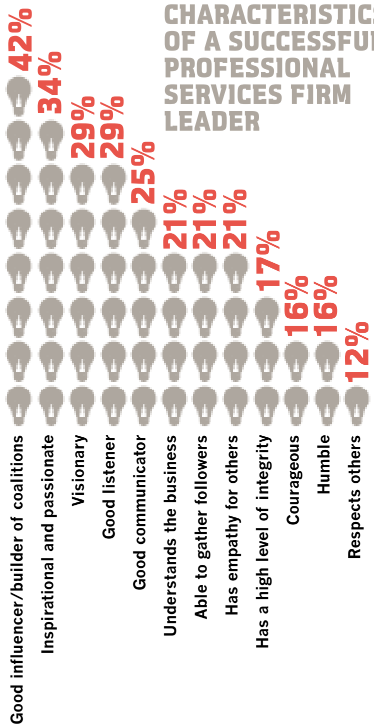
8 Strategy

Some view strategic planning as an art, some as a science – and some as an inspired combination of the two. Leaders described their strategic planning processes as everything from intensive brainstorming marathons over weeks or even months to routine annual budget exercises. The best firms view strategic planning as a continuous cycle, not a one-time event. Long-term strategic plans are integrated with annual plans, and progress is regularly reviewed and communicated to all stakeholders. As the Ernst & Young example overleaf illustrates, successful firms invest senior time to develop, track and manage the planning cycles.

9 Structure

The choice of the organisational structure and governance model has critical implications for professional service firms. Together they form the internal architecture of a firm – the invisible scaffolding that supports everything, from day-to-day operations to strategic planning and effective execution. The structure delineates the organisational layers and management reporting hierarchies within the firm. Governance is the leadership style – collaborative, dictatorial, or corporate – and the policies, systems and procedures that underpin the enterprise. Organisation design choices can reinforce or undermine culture, endanger or enhance performance and service quality, and enable or diminish profitability.

CHARACTERISTICS OF A SUCCESSFUL PROFESSIONAL SERVICES FIRM LEADER



10 Leadership

Of all the ingredients in the professional service mix, leadership is probably the most essential to success – and often the most elusive. The matrix structure that most professional service firms have embraced is a dynamic business model; it's flat, fluid, fragmented, and often unruly.

We asked interviewees for the most important characteristics of a successful service-firm leader (see chart above). By a wide margin, the traits that for them define successful leadership – good influencer, listener and communicator; inspirational; passionate; visionary – fall under the umbrella of strong interpersonal skills and emotional intelligence. As one CEO summed up: 'There's an under-appreciation of what it takes to lead businesses like this – better be darn sure you want to do it.'

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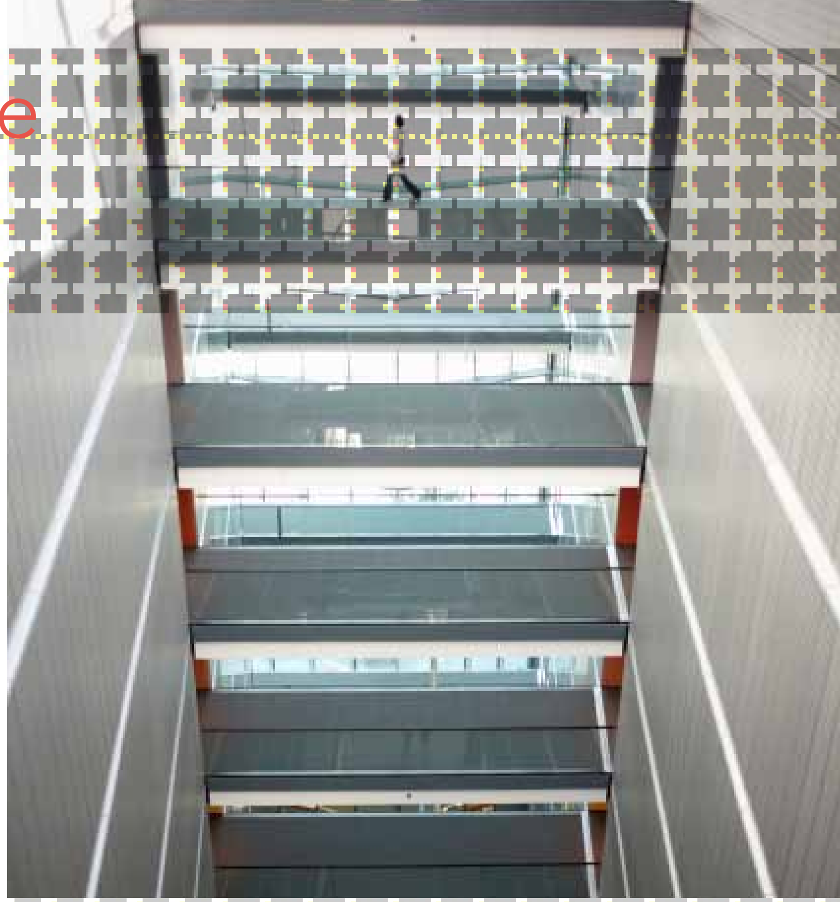

*ANNUAL PLANNING AT ERNST & YOUNG

Annual planning at Ernst & Young is a disciplined and methodical process. According to Mark Gaumond, former Americas senior vice chair, markets, all partners throughout the organisation participate. 'It's a very comprehensive process,' he says, 'but it gets everyone to buy into and execute on the goals we set.' There are two components to the planning process that run in parallel each year:

* **Financial planning** – The financial plan deals with the operational side of the business. Assumptions on existing and future headcount, utilisation, production and rates per hour expected from the various markets are calibrated into annual revenue, cost and earnings targets.
* **Revenue planning** – The revenue planning is top-line focused and aspirational. It starts with the individual partners coming forward with their views of what they may be able to achieve and deliver in the marketplace. Partners are encouraged to think broadly about client needs that might be addressed by Ernst & Young's four service lines: assurance, tax, advisory and transactions. The plans roll up to a revenue target that is typically higher than the financial plan target.

The process of developing the plans is transparent, collaborative and iterative, beginning four to five months before the start of the fiscal year. Using a standardised template and toolset, individual partners prepare plans that are rolled up by client, office, sub-area and area, and are ultimately approved by an area operating committee and board. All geographies and service lines have input into the plans, and each unit's assumptions and goals are shared openly.

Once plans are approved, results are monitored monthly and are reported quarterly. At mid-year, a comprehensive review is conducted, and plans are updated as necessary. On an individual partner level, adherence to plans is built into partners' individual goals, and results are considered in compensation decisions.

Gaumond says that Ernst & Young essentially runs the business off the financial plan and 'pushes hard to make the revenue plan'. He describes a healthy tension between the two plans: 'If you are not careful, excessive focus on operation – or the bottom line – can limit top-line growth. On the other hand, you cannot be out generating business for new business's sake without any financial discipline. You have to keep it in balance.'