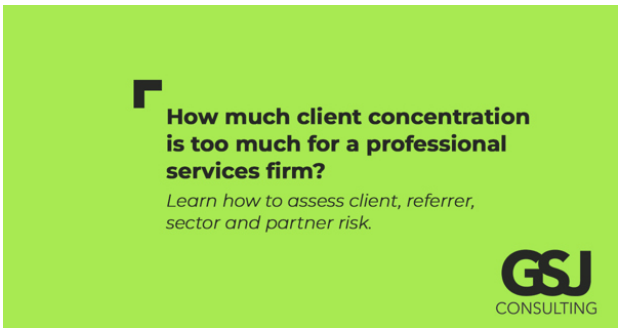


How much client concentration is too much for a professional services firm?

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Client concentration is too high when a foreseeable drop in work would leave a firm struggling to cover its commitments before it could replace the income. There is no universal safe percentage. The answer depends on how profitable the work is, how much cash the firm has available, which costs it can adjust and how long it takes to win new work and collect the fees.

Most firms start by looking at how much revenue comes from their largest clients. That’s a useful first step. But several smaller clients can be exposed to the same event if they come through one referrer, operate in the same sector or rely on the same partner for advice. These four hypothetical firms show how each kind of dependence can affect a practice.

What does client concentration look like in practice?

An accounting firm with one dominant client

A 15-person accounting firm earns 32% of its fees from one corporate group. The client pays promptly, the relationship has lasted ten years and the firm has recruited three staff primarily to service the account. If the group is acquired and its new owner brings some of the work in-house, the firm could lose a substantial share of its fees even though the client is happy with the service.

The partners should model what would happen if the client halved its spending. Which costs would remain? Could the three staff move to other accounts? If there isn’t enough work elsewhere in the practice, the firm has a specific business development priority. It needs to find other clients who value the same skills and can provide work for that team.

An architecture practice with one dominant referrer

A suburban architecture practice has no client accounting for more than 5% of fees. However, one town planning practice introduced clients who generated more than 40% of its fees from new clients over the past year. If the planner who makes those

introductions retires or the practice merges, existing projects might keep the architects busy for months while new enquiries fall away.

The principals should track where new commissions come from and establish which referred clients now approach the practice directly. The loss of the referrer could slow the flow of new projects even if existing clients keep coming back. Building relationships with other planners, project managers and past clients gives the practice more ways to bring in its next commission.

A bookkeeping firm exposed to one sector

A bookkeeping firm earns 65% of its fees from residential building businesses, although its largest client contributes just 9%. Its experience with job costing, payroll and subcontractor payments helps it win work in the sector. But if several builders come under financial pressure at the same time, the firm could face slower payments on existing invoices as well as fewer instructions.

The owner should look at how much income depends on builders with similar exposure to the housing cycle. One option is to pursue maintenance contractors and other service businesses that value the same bookkeeping skills and earn more of their income from recurring work. That gives the firm a way to diversify without having to develop an entirely new service.

A law firm dependent on one relationship partner

A 30-lawyer firm’s largest client accounts for 7% of its fees, but clients who generate 58% regard one senior partner as their principal adviser. Other lawyers deliver much of the work. If the partner retires, leaves or takes extended leave, the firm may discover that those lawyers have had little direct contact with the people who decide where the work goes.

The partners should ask which clients would already feel comfortable instructing someone else at the firm. A senior associate may know an account inside out and still be a stranger to the general counsel. The time to give that lawyer a meaningful role in the relationship is while the partner is there to introduce them and work alongside them.

How do you assess client concentration risk in a professional services firm?

Start with the past 12 months of fees and look at them by client or corporate group, referral source, sector and relationship partner. Compare the figures with prior years to see whether a single large engagement has distorted the picture. Then look ahead at where the next six to twelve months of work is likely to come from. If the same fees appear under more than one heading, count them once when estimating the loss from a particular event.

Pick a plausible event and work through the financial effect. If a client accounts for 30% of annual fees and halves its spending, the starting point is a 15% fall in annual fees, assuming everything else stays the same. Then estimate when the fall would affect cash receipts, which costs the firm could adjust and how long it would take to win, deliver and collect payment for replacement work.

That timing can change the decision. If the firm can absorb the shortfall for three months but usually needs six months to win comparable work and collect the fees, it has a reason to act now. Test the same question against the firm’s most significant

referrer, sector and relationship partner.

How can a client account management plan reduce the risk?

Put a client account management plan in place for clients that account for a substantial share of fees or rely heavily on one person. Identify who decides where the work goes, which people at the firm the client already trusts and where the relationship depends on a single partner or principal. Then agree who else should get to know the client, what role they can play and when the team will review progress.

Give those people a role that makes sense to the client. An accountant might bring a colleague into a budgeting discussion, or an architect might ask an associate to lead the next project review. At the next account meeting, ask who the client has actually contacted for advice and whether they would be comfortable calling that person if their usual adviser were away.

Where the main risk is the amount of revenue tied to one client, pursue other work alongside the account plan. A broader team can make the relationship less dependent on one person, but the client can still cut spending or change providers. Agree which new clients or sources of work the firm will pursue before making another hiring decision around the account.

For help assessing where your firm’s revenue and relationships are concentrated and putting account plans in place for key clients, speak to GSJ Consulting.

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