NOTEBOOK OF IDEAS FOR

DIVESTITURES
OF SECURITY GUARD COMPANIES

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A periodic informational letter published by Robert H. Perry & Associates - Dedicated to Buyers and Sellers of Security Guard Companies

TIMING IS EVERYTHING . . . .

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For most business owners, their closely–held company represents a major part of their net worth. It's no wonder then that they want no mistakes when the time comes to sell. And that time will come since eventually every closely–held business will be liquidated (not a viable option for a security guard company), passed to a future generation (also not usually an option), or sold to a third party.

The problem comes in knowing the best time to sell and the preparation that has to be done in order to achieve the maximum value. The preparation process involves a series of positive changes that make a company more profitable and more attractive to a buyer. It starts when the company is established and continues up to the time of sale. It's often called "grooming" and that's the term we will use for this article.

There's a lot being said about grooming. However, there's a wide difference of opinion as to what it means, how it is accomplished and how much needs to be done. Some business owners look at grooming as a last minute gloss over technique that changes mediocre companies into super producers. And, as pointed out later in this presentation, it's not as important as most owners think.

Grooming can be done, as a conscious effort to build resale value, or with the single purpose of enjoying the profits while the company is owned. In other words, if changes need to be made to make a company more attractive, they should be done regardless of whether a sale is being considered.

With that in mind, one would think that the ideal time to sell is when the owner has the business running like a well–oiled machine; and that's partly true. For instance, an ideal security guard company is one with <u>no</u> armed guards, all accounts over 168 hours per week, no high liability accounts, good account retention history and no low bid work – and other characteristics that we will discuss in future issues. Of course, in the real world of competitive bidding and having to accept less than desirable work, this ideal security guard company does not exist – and never will.

Given this astounding revelation that a security guard company is never perfectly groomed, how does an owner determine the best time to sell?. . . . The answer is TIMING.

TIMING is everything! Unfortunately, most owners miss it because they are too busy running the business to know when the proper time has arrived or they are too emotionally attached to the business and cannot let go when the opportune time comes. They fail to realize that proper timing is not about selling when the owner thinks the company is ready, but rather selling when there exists in the market place a generous buyer(s) who has a strong present need to purchase a company.

This generous buyer population changes frequently and oftentimes, quickly. A mediocre or poorly groomed company can command an attractive price, if a generous buyer exists that has aggressive growth plans calling for an acquisition in that market. If buyers do not exist for a given market, no matter how well groomed a company is, it cannot be sold. If buyers do exist, but they are "bottom fishers", the company can be sold, but at a much lower price.

It's easy to talk about timing, but it's much more difficult, if not impossible, to know how to recognize it. However, the uncertainties can be lessened somewhat by a knowledge of prior market conditions, which is a good yard stick by which to measure a present market. Another way guesswork is lessened is through frequent dialogues with intermediaries who specialize in selling security guard companies.

Consider these real life sellers with whom we've recently worked (the names and amounts have been changed to protect their identity):

Alan was forty-five years old and had owned his security guard company for about ten years.

We had been talking to Alan for almost a year about his acquisition plans. One day, I made a casual call to him when he was having one of his "blue Mondays"; which is not unusual for security guard company owners... He complained that "the guards were not covering their posts, competitors were hitting on his accounts and the paperwork was overwhelming".

On this particular day, Alan was more interested in talking about selling than in buying, which had been the subject of all our prior conversations. I told him that if he wanted to pursue a sale, now was an opportune time. I knew a very generous buyer who was interested in his operating area. The buyer was paying better prices and giving better terms than any I had seen.

Alan had not been very successful in the grooming process. On the other hand, he had not planned on selling his company this early. On a scale of one to ten, I would have rated his company about a six.

He contemplated the thought of selling for a while and went through periods of saying yes – then no. After all, he was only forty-five years old, what was he going to do after the sale? But, the business wasn't fun anymore and it was only marginally profitable. With these two good reasons in mind, he finally agreed to a meeting with me to discuss the possibilities.

Through a series of negotiating meetings that followed, his security guard company was sold to that buyer, at what was then an unprecedented price. It's been almost ten years since the sale, and I frequently talk with Alan. He's convinced that his timing was perfect . . and he almost missed it. Shortly after this sale, that purchaser stopped making acquisitions and the prices for security guard companies in Alan's area dropped.

Looking back at that sale and analyzing the market that existed at that time, I'd say he only had a six-month window of opportunity in which to sell at an optimum price. Of course, there have been other sales in his area since then, but the prices have not been as good.

Then there was Bill. Bill was sixty-two years old and for several years had pegged this age as the time he would sell his security guard company and retire. Bill had been doing some conscious grooming for the past five years in anticipation of this eventual sale. There was still a lot of improvements that needed to be made, but time had run out. He was ready to sell and that's exactly what he wanted to do, whether his company was ready or not. On a scale of one to ten, I would rate his company as a seven.

He contacted us to represent him. He, like most sellers, had some unrealistic expectations about a sale, but we agreed to take the assignment.

About this time, a foreign company contacted us about buying a security guard company in the states. For their initial acquisition, they would pay a very good price, hire all the employees and continue operating under the seller's name. For Bill, this was a buyer sent from Heaven. The terms and conditions offered by the buyer were exactly what he wanted. We closed that sale in short order and Bill walked away happy (and wealthy).

Charlie was not as lucky as Alan and Bill. He first contacted us when he was seventy years old. At that time, he was preparing for a sale in about three years, and wanted to do some conscious grooming. We described the things that made a security guard company attractive to a buyer and he promised to call us in three years. The overwhelming obstacle to selling his company at that time was not necessarily the changes he wanted to make, but the fact that he was billing 16,000 hours per week and he wanted to grow it to 20,000 hours – then sell. He thought his price would be higher at that level which was a very important retirement consideration.

During our initial visit with Charlie, we told him about a generous buyer who was presently buying companies in his operating area. The price would have been around \$3 million for just his accounts (accounts receivable and equipment would have been added to this amount). Charlie wanted to wait.

About a year later, we contacted Charlie to share some information we learned about this aggressive buyer. We told him that we thought this buyer was going to quit buying soon, and there was not another buyer presently in the market that would give him as good a deal. But Charlie again said no, and the purchaser did indeed quit making acquisitions.

Then two years later when Charlie was seventy–three, he contacted us to arrange another meeting to talk about selling his company. Charlie was now ready to sell. During that meeting, we found that Charlie was now billing 14,000 hours per week; which was down from 16,000 three years earlier, and far short of his magical 20,000.

And not only had Charlie lost accounts, but he had also suffered operating losses from his business during those three years. The sad part was that Charlie's health had deteriorated, as had the financial condition of his company. Although, Charlie lost money from operations during those three years, his greatest loss was in the resale value of his accounts. This loss in resale value resulted from two things: the loss in hours and the decrease in the selling multiple that resulted from the aggressive buyer leaving the market.

We sold the company for $2 million, plus accounts receivable and equipment. With the decline in value and the operating losses for the three years . . . . Charlie lost over $1.5 million as a result of missing the opportune time to sell – not to mention the three years head start he lost on retirement.

There's a lesson to be learned from these three sellers:

Alan had not planned to sell his company. He was in the grooming process and had a long way to go. But he was open minded and very perceptive. He looked at the sale as just another economic transaction. He was able to detach himself emotionally from the business. He realized that the deal in front of him was unprecedented. If he kept his business for a few more years and continued to build and improve it, he probably couldn't get as much, albeit larger, as he was getting now. He knew the value of TIMING and acted on it.

Bill was just downright lucky. He ignored the concept that the buyer controls timing, not the seller. Instead, he chose a definite date (when he reached 62 years old) to sell; irrespective of whether a generous buyer would exist at that time. Luckily for him, the time he chose to sell just happened to be when the aggressive foreign buyer chose to enter the United States security guard market.

To use this method of picking a time to sell a company is like one saying they will sell their 100 shares of a certain public company's stock on July 3, 1998. How do they know what the price will be then?

What Bill could have done differently was to choose a "span of time" in which to sell rather than a fixed date. For instance, in anticipation of a sale date when he reached age 62, he could resolve that if an attractive buyer comes around while he's 60, he'll consider an offer. That is to say, he's under no pressure to sell, but he would consider it. Bill was so rigid in his approach, that if the foreign buyer had come around two years earlier, he would not have talked to them.

Charlie on the other hand, was not perceptive or lucky. He was too emotionally attached to his business to recognize the proper time to sell. He would not let go. The window of opportunity was missed. He ignored the signals that were telling him the market was right, but would get worse.

This article is not about owners who are happy running their business; and have the energy and resources to make it grow. Unless they're offered a price that borders on the ridiculous, they should not sell. Their company is worth a lot more to them than to any buyer.

It's also not about owners who are under pressure to sell immediately because of some unexpected financial, health or family crisis. They will have to rely on luck and hope that the grooming they've done will help overcome any bad timing that may exist. There are, however, ways to increase value under these circumstances and we will talk about this subject more in future articles.

This article is about owners who, having become dissatisfied with their business, decided to sell or are strongly looking at selling as a viable option. Once this decision is made, the next step is picking the right time. The unfortunate part is that if the timing is missed, the owner may be like Charlie, who did not get a second chance at the optimum time to sell.

There's one final comment to make about TIMING – selecting the proper time to sell just gets a good deal on the negotiating table; and it's there that a good deal is made or lost. If the sales contract is not properly written or the tax implications are not considered, the sale can become very disappointing.

We plan to discuss ways to overcome these pitfalls in future informational letters.

Here are some of the topics:

* *Saving taxes through the non–compete agreement*
* *Why some companies need to buy*
* *How to increase value*
* *The negotiating team*
* *How much (and how little) information to furnish*
* *The due diligence process*
* *How to handle the confidentiality problem*
* *How to announce the sale to employees and accounts*

MISTAKES SELLERS MAKE

- Not selling at the right time (see cover article, this issue)
- Handling negotiations alone
- Unrealistic price expectation
- Failing to qualify a buyer prospect
- Not leaving the business after the sale
- Not planning for taxes
- Not staying in touch with the buyer after the sale
- Assuming that buyers who make a lot of acquisitions pay the best prices
- Assuming the buyer will pay for potential
- Letting accountants and attorneys make business decisions

MISTAKES BUYERS MAKE

- Paying too much, or anything at all, for a mediocre business
- Integrating seller's business too quickly
- Integrating seller's business too slowly
- Believing what the seller says about the "real reason" for selling
- Making too many acquisitions too quickly
- Pinching pennies on insignificant issues
- Changing seller's name too quickly
- Changing seller's name too slowly
- Responding slowly to brokers
- Letting accountants and attorneys make business decisions

This periodic informational letter is published by ROBERT H. PERRY & ASSOCIATES, INC.

Established in 1977, we are the recognized specialists in the sales and valuation techniques for security guard companies. We have successfully represented over 70 sellers of security guard companies located in the U.S.A, Canada, western Europe and the Caribbean.

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