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

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Need Cash?...Why Not Sell Part of Your Company?...The Part You Don't Want.

(Written by Robert H. Perry)

Partial Divestitures. Spin-Offs. Split-Ups. Downsizing. Partial Sales. Redirecting Assets. These, and other catchy phrases, are used to describe the selling off of parts of a company.

To some, it means loss of jobs. To others, it means enhanced profits, receipt of needed cash and increase in shareholder wealth.

And those companies in the security guard industry who have used it have had profound results.

Take the case of Chambers Waste Management, a large American Stock Exchange company, who used the sale of their security guard subsidiary as a way to regain investor confidence after the auditors revealed large charges to the year-end financials.

The first mention that Chambers was having difficulty came in the March 18, 1992 issue of the *Wall Street Journal*.

The article, in repeating a quote from someone within the Chambers organization, went on to say that "...Chambers said it changed its accounting method to immediately recognize indirect expenses, resulting in an after-tax charge of $27 million, or 45 cents per share, against 1991 earnings."

On April 10, 1992, another *Journal* article stated that "...Chambers may have difficulty raising capital and meeting its expansion targets... with estimates that adjusted year-end debt-to-capital ratio would be about 45 percent."

These announcements would be a prelude to numerous *Journal* articles on Chambers over the following several months, which would result in a dramatic decrease in stock prices.

Actually, all this bad publicity was over some arguable accounting rules that dealt with when development expenses should be written off for income statement purposes. It was never clear whether the write-down was necessary, but the facts didn't matter any more. The media criticism was getting out of hand.

With the adjusted figures, the debt to equity ratio was reaching unacceptable levels and shareholder confidence had greatly diminished — as was reflected in the depressed stock prices. Chambers needed to pay down some of this debt. To do so, they had to sell off some valuable assets and they needed to do it quickly.

Chambers turned to Security Bureau, Inc., their wholly owned security guard company subsidiary, which they built from scratch to an annual volume of almost $80 million in just four years. Security Bureau had a very talented executive management team in place and was well positioned to eventually become a major force in the U. S. security industry.

However, it was not Chambers' main line of business and was a source for quick cash. On October 30, 1992, Chambers made the announcement that they had sold Security Bureau to Borg-Warner for $34 million.

Unlike many AMEX companies, Chambers was not a conglomerate with several unrelated business units. It was primarily a waste management and development company who just happened to get into the security guard business.

Like several other examples we will mention throughout this article, Security Bureau was a fairly insignificant part of Chambers' total volume — about 25 percent.

Although Chambers had not planned on selling Security Bureau so quickly (if ever), they were fortunate that the company was valuable and could be sold without affecting the core business.

The Partial Divestiture Works For The Large Company...

There have been other security guard companies who have been a part of or used a partial divestiture, or split-up plan. Consider these public company transactions which have been announced through the media:

- In 1988, American Brands sold Pinkerton's Security to CPP. Pinkerton's represented an insignificant five percent of American Brands' annual billings.
- In 1987, National Guardian, then a public alarm and security guard company, sold their security guard division to Stanley Smith Security. The security guard division represented approximately 25 percent of National Guardian's business.
- In 1993, Stanley Smith sold selected offices to Pinkerton's. This partial divestiture represented approximately 20 percent of Stanley Smith's business.
- In 1990, Walter Kidde (NYSE) sold their Globe Security division. Globe represented less than seven percent of Walter Kidde's annual gross volume. Kidde's goal in divesting Globe was to get rid of their service businesses so they can concentrate on their manufacturing units.
- In 1994, Figgie International sold Advance Security to Chuck Schneider and Ken Oringer, two well-known security guard industry executives; who were backed by the Chicago-based investment group, Golder, Thoma, Cressey and Ranier.

The names of large security guard companies who have used the benefits of the partial divestiture continues... Intercon would sell part of its alarm division; Mayne Nickless (Australia) would sell all their security guard units around the world. And the list goes on and on.

When we look more closely at these transactions, we see that the seller divested the unit because it no longer fit their long-range plans or was the most logical source of quick capital. In most instances, the unit, although large as security guard companies go, was actually a rather insignificant part of the seller's total volume.

The remaining business was unaffected by the sell-off. The cash the seller received for the unit was put to better use in other areas.

The unit was usually only marginally profitable or actually losing money in the hands of the seller. The price the buyer would pay was several million dollars and represented, in some cases, 50 to 100 times what the seller was earning. Which made the decision to sell easy.

Most of the sellers had owned the security guard unit for several years, but could not make it profitable. The decision to sell was made by the Board of Directors whose mission was one thing — enhance the shareholder value.

If it meant down-sizing the company in order to accomplish this goal, then they will downsize.

It Also Works For The Small Company...

For the smaller company, the decision to sell or not to sell part of the company is often driven by emotion, rather than practical judgment. Smaller companies are owned by entrepreneurs who make all the decisions for their company and tend to measure their success in terms of gross volume.

The entrepreneur is infatuated with bigness. Making the company smaller is usually not an option. Instead of selling unprofitable units, the owner keeps trying to fix them by infusing borrowed funds.

This is expensive and has to be paid back. Such a rigid fixation on size often leads to the demise of the company.

But there have been many small companies who managed to break the mold of the traditional entrepreneur who refused to downsize, even if it meant risking the well-being of the company.

They proved that the advantages found in the partial divestiture is not a secret lost in the large conglomerates. They were able to recognize the value in selling off part of the company — whether it was a need to come up with quick cash or divest an unprofitable unit.

In preparing for this article, we reviewed the 80 plus security guard industry transactions for which we represented the sellers.

We have represented sellers of entire companies with annual sales as small as $300,000 and as large as almost $100 million; and we've handled partial divestitures for clients with sales over $2 billion. Many of our seller/clients had multiple offices or divisions, even though their annual volume was less than $8 million.

We were reminded from our review that approximately 50 of these 80 plus transactions had something to do with a partial divestiture; in spite of the fact that many of our seller/clients were small.

Here are some of our large and small seller/clients who have sold parts of their company. Since no public announcement for these partial divestitures was made, we will not disclose the identity of the parties:

- An international alarm company sold all their security guard offices in the Western U.S. They never intended to get into the security guard business. They inherited these units through several alarm company acquisitions. They didn't understand the business. They didn't like the business and they wanted out.
- A Midwestern-based security guard company sold all their commercial accounts and kept their more profitable strike business.
- An international janitorial company sold all of their U.S. security guard offices.
- A California-based company sold all of their standing guard accounts and kept their patrol accounts.
- An East Coast company sold their guard accounts and kept their investigative business.
- A European-based temporary help company sold their guard accounts in the Northeast U.S.A.
- A New England-based security guard company sold their Florida accounts.
- A Midwestern-based security guard company sold all of their commercial accounts, so they could specialize in the government sector.
- An East Coast company sold all of their guard accounts and kept their investigative

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business.

- A large Dutch conglomerate sold their Montreal security guard subsidiary.

- A small, $4 million (CN) temporary help and security guard company in Edmonton, Alberta sold their $2 million security guard division.

Be reminded that many of these companies had annual sales of less than $8 million.

But size is not the key to a successful partial divestiture. Whether a company is successful depends on what they do with the proceeds from the sale.

A Company Must Have A Divisible Unit In Order For The Partial Divestiture To Work...

We learned from looking at these partial divestitures that there are certain things that must exist in order for the transaction to work.

The existence of a buyer for the unit is the most important factor.

If one does exist, the company then determines if there is a divisible unit; that is, a group of assets that can be divested without adversely effecting the remaining business. A divisible unit can be:

- All of the accounts in a geographic area.

- Certain types of accounts — as in the case of the Midwestern company who sold all their commercial customers and kept their strike business.

- A division — as in the case of the California company who sold their guard division and kept the patrol division; or the company who kept their investigative division and sold their guard division.

Even Owners Who Don't Need Cash Can Benefit...

We need to mention one last reason, although not as frequently used, for the owner to sell part of the company:

The owner may just want to slow down but not want to get out of the business entirely.

Unfortunately, most owners do not think of the partial divestiture as a possibility when the time comes to slow down. They think that the entire company has to be sold. As a result, they often wait until it is too late to reap the full benefits of proper timing.

A few years ago, we sold part of a company that had total sales of approximately $5 million. Actually, the sales of the security guard division was around $4.5 million and the other $500,000 was investigative services.

In this case, the owner kept the smaller investigative division and sold the security guard business. The owner wanted to slow down. He was tired of borrowing money to meet the large payroll that goes with a labor intensive business.

He liked the fact that he could handle the investigative business with very few employees. He now works when he wants to and makes more money than he did when he had both divisions, although with a much smaller volume.

The moral of this story: this seller knew the value of the partial divestiture technique which provided him with a more comfortable lifestyle and enhanced his wealth.

The Partial Divestiture Often Results In A Larger And More Focused Company...

In summary, there is no company too large and few companies are too small to take advantage of a partial divestiture. The only requirement is that the company have "divisible units." The partial divestiture provides needed capital in the form of equity, as opposed to loans that are expensive and have to be paid back...and helps the company reach their financial goals — first by downsizing through getting rid of unwanted separate units — then taking the proceeds and redirecting them into more profitable areas.

The resulting company is usually built back to one larger than its original size — more focused, therefore more profitable.

NEW BUYERS FOR SECURITY GUARD COMPANIES RAISE SELLERS' EXPECTATIONS...

This past year brought a dramatic increase in the number of new buyers for security guard companies and accounts. As a result, we represented a record number of sellers. Only two of the buyers were public companies. The rest were large regional or international privately-held companies and many were first time buyers.

For the smaller company (with billings less than 2,000 hours per week), this meant a market for their accounts that previously did not exist. In the past, very few, if any, of the aggressive buyers were interested in looking at the small company. The amount of sales volume involved just did not justify the expense associated with the buy/sell contract preparation and the salaries for the due diligence personnel. However, these new buyers are more organized in the due diligence process, thus reducing the time it usually takes to consummate a transaction.

This increase in buyer population also meant better prices and terms for our larger seller/clients. Here's an overview of some of our transactions — note that there were ten transactions with eight buyers.

Seller	Buyer
Northern California security guard co.	*International publicly-held security services co.*
New York-based security guard co.	*Regional New York-based security guard co.*
Pennsylvania-based security guard co.	*Regional Pennsylvania-based security guard co.*
Virginia-based security guard co. (operations in VA, DC, MD and PA)	*International privately-held security services co.*
Michigan-based security guard co.	*Regional Michigan-based security guard co.*
Northeast-based security guard co. (sold their Florida office)	*National privately-held security guard co.*
North Carolina-based security guard co.	*(Same as above)*
Cleveland-based security guard co.	*(Same as above)*
Chicago-based security guard co. (sold selected accounts)	*National publicly-held security guard co.*
Toronto-based Canadian security guard co.	*National U.S.-based privately-held security guard co.*

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1996 — Volume 2, No. 1	VALUE — It's determined by the characteristics of a company.
1996 — Volume 2, No. 2	CHOOSING THE PROPER METHOD TO SELL A COMPANY There are three methods to use when selling a company.

This periodic informational letter is published by:

ROBERT H. PERRY & ASSOCIATES, INC.

Established in 1977, we are the recognized specialist in the sales and valuation techniques for security guard companies. We have successfully represented over 80 sellers of security guard companies located in the U.S.A., Canada, Western Europe, The Caribbean and South America.

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