

# 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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## ABOUT OUR FIRM . . .

Written by Robert H. Perry

*The activity in buying and selling security guard companies is very intense and it's getting the attention of a lot of owners. They're calling our office to check us out and ask questions about the sale process.*

*Here's our response to some of those questions:*

***Who is Robert H. Perry & Associates, Incorporated (RHPA) and what do you do?***

We are an intermediary firm that represents sellers of security guard companies.

Some people use "broker" to describe what we do, but we prefer to use intermediary because it seems to describe our higher level of professionalism.

Instead of representing all kinds of companies, we just represent security guard companies. And we do much more than most

brokers or intermediaries. We get heavily involved in the sale process, which begins with the get acquainted and fact gathering meetings with our seller/client in their office and continues through the conclusion of the successful negotiations and closing procedures.

We spend a lot of time traveling to meet with and qualify potential buyers for our clients and handle on-going negotiations. We've represented almost 100 sellers located in North America, South America, the Caribbean and Western Europe.

By design, we're not members of any brokerage associations. We never share our

assignments with other intermediaries (also known as co-brokering). We prefer to work this way because it enables us to keep everything we work on confidential . . . an aspect that is very important to security guard company sellers.

### ***How did RHPA get started selling security guard companies?***

When RHPA was started back in 1977, there were no plans for it to be a firm that specialized in selling security guard companies. It really started out as a general business brokerage company, which seemed a likely business, after selling my interest in an accounting firm – a profession I had been in for 13 years. In 1981, we sold a local security guard company to a New York Stock Exchange conglomerate. As a result of our involvement in that sale, we learned a lot about the security guard business.

We learned that the security guard industry was starting a period of consolidating, which we anticipated would last for several years. We also learned that there were no intermediaries who knew enough about the industry to help the privately held sellers deal with the larger consolidators, who were usually also their competitors.

The sellers were vulnerable to these competitors when they talked with them about selling. They didn't know how much their business was really worth, so they were at the mercy of their buyer. They didn't know how much information to give the buyer prospect. They were concerned that if they gave an unscrupulous buyer too much information, the buyer would use it to solicit their accounts instead of buying their company.

In short, the sellers did not want to deal with the buyers directly, yet they wanted to get in on the attractive prices.

We recognized that security guard company sellers needed a professional on their side. Someone who knew how to establish realistic seller favorable prices, who knew how to "package" their company – giving enough information, but not too much. And just as important, they needed someone who could

reduce the buyer population down to the two or three most qualified prospects.

RHPA then became this intermediary firm that would only represent sellers of security guard companies.

### ***What does RHPA look for in determining what is best for the seller?***

There are four things we concentrate on when we represent a seller: **price, guarantees, terms** and **security**. We strive to make sure our seller is obtaining the best possible price for the company. At the same time, the price should not be eroded because of buyer-favored guarantees, terms or inadequate security.

Most buyers require that the accounts remain with them for a period of time after closing in order for the seller to receive all of the agreed to purchase price. We do not particularly like this type of deal and strive to structure transactions where there are no guarantees by the seller. We do not think the seller should have to depend on the buyer giving the same level of service after the sale as the seller did before the sale as a condition to receiving all of his money. However, it's often impossible to sell a company without some guarantees. When there are guarantees, we try to make them as seller favorable as possible.

We do not get involved in transactions where the buyer is weaker financially than the seller unless, of course, the buyer is not requiring the seller to take back financing. In most of the transactions we have arranged, the seller received 50% - 80% of the price at closing and received the remainder in no less than six months. Since the buyers were public companies or large regional companies, we were able to verify before closing that the seller was not going to have any problems getting paid.

### ***What size companies does RHPA represent?***

We represent sellers . . . we have handled transactions for companies with annual sales

as low as \$300,000 and divisions of companies with sales as large as \$3 billion.

We are presently working on businesses with sales as small as \$1 million and as large as over \$50 million.

***Some security guard companies have other divisions such as alarms, investigative, patrol and armored vehicles. Can you handle the sale of these divisions as well?***

Yes. We often find security guard companies that have these auxiliary services. Sometimes, the security guard and patrol business can be sold to one buyer.

The alarm and armored operations normally require separate buyers. We have the expertise to sell these operations as well.

***How many potential buyers are there for security guard companies?***

If we include in the definition of "potential buyers," the companies who say they would like to buy a security company . . . then there are several hundred prospects. If we are talking about companies who have demonstrated their ability to do a deal by actually consummating a purchase or several purchases, then we are probably talking about a hundred (domestic only).

Since we always represent sellers, we look for a buyer willing to buy a company on our price and terms. At any particular time, the number of buyers fitting our criteria is around ten (sometimes a lot less).

The buyer population is always changing. Some of the buying companies we used to work with have merged or sold their company and are no longer in the market. Others have bought as many companies as they can operate for now and are no longer active. Still others have changed their pricing and guarantee policies, and their new policies do not come up to the expectations we require for our sellers.

At the same time, buyers who used to depend only on organic growth have started looking to grow through acquisitions. New buyers have emerged as a result of large multi-national companies deciding to expand into the United States security market.

***Are all buying companies alike in their approach to price, guarantees and terms?***

No. Although there's a notion going around the industry that the basis for valuing security guard companies is some multiple of gross monthly billings, the truth is that prudent buyers approach the price from a return on investment standpoint. Which means the price is determined by what the buyer can make with the company, not a set multiple of gross billings.

There may be several offering prices for one seller if there's several buyer prospects involved; since each buyer has unique return on investment requirements, as well as ways of computing it.

Of course, after they go through their return on investment computations, they usually express the total price in terms of multiples of gross monthly revenue. This is done in order to have a convenient way of handling post closing adjustments for any guarantees or paying for new business.

For the seller prospects who are trying to value their company based strictly on some multiple of gross monthly billings they've heard in the industry, I would like to mention that I have seen the multiple as low as one times monthly to as high as seven.

To make the pricing issue even more complicated, some companies will settle for a lesser return on investment (which results in a higher price to the seller) if the seller operates in certain, very desired areas. Again, the desired area for one buyer may be different from that of another.

Also, some buyers will be more generous if they know other buyer prospects are talking to the seller - through the intermediary, of course.

To summarize this pricing part of the question – we find our seller/client the best price by working only with the buyer prospects that really want or need to buy our client's business. If this need is not present, a buyer will be inflexible on their price and terms.

The guarantee and terms are also different from buyer to buyer.

We've handled deals where there's been no guarantee of accounts and some where the buyers required three months or six months. We've handled deals where only some of the accounts required a guarantee.

We've talked with some buyers that required a two-year guarantee, but we passed on doing a deal with them. I feel that, except for very unusual circumstances, a guarantee longer than a few months is too long.

***What about pending business, do I get compensated for that?***

It depends on the buyer. Most buyers are not willing to pay for pending business except in the form of a sales commission.

We have negotiated deals where the seller was compensated for business that came in within 30 days after closing at the same multiples that were paid for business in place at closing.

We are doing some deals with buyers who are willing to extend this period for two to three months after closing.

***What about foreign buyers?***

I frequently travel to Europe to meet with buyer prospects. There are some now with eventual plans to get into the security guard business in North America, and there are some already here.

The foreign buyer usually needs a large company (\$25 million plus) for their first acquisition. They usually pay better prices, but it takes them much longer to consummate a deal.

***What about the tax consequences?***

The tax consequences of a sale are just as important as the gross sales price and terms. The astute sellers are more interested in the amount of money left after paying taxes than they are with the gross sales price. The tax structure of the transaction determines what the difference between the two will be.

Since the allocation of the purchase price to the various assets will have an impact on the taxability of the sale, the allocation should be carefully thought out and negotiated before the closing.

The Tax Revenue Act of 1986 changed the way the taxes are computed on the gain in a business transfer. Under the new rules, it is very easy to fall into a tax trap of being taxed twice on the transaction. Hence, the tax planning techniques are more important than ever.

However, there was a recent tax break for sellers. On August 5, 1997, President Clinton signed a tax bill, which, among other things, gave sellers of companies a tax decrease. For sellers of qualified "S" Corporations, this tax break was the equivalent of getting about 11% more for the company.

We advise sellers and buyers to get qualified tax counsel involved early in the negotiation process.

***Your office is in North Carolina. How can you represent sellers who may be hundreds or thousands of miles away?***

We spend a lot of time on airplanes. Because our office is located close to a major airport, we can leave our office and be in almost any major East Coast city in about an hour and a half. We can be in California in less than five hours. With the short connecting times through major airports, we can be in South America or Europe in about a day.

Our first step in deciding whether to take on a representation assignment is to qualify the seller. We look at the quality of the business and determine the seller's sincerity factor.

When we feel that the business is saleable and the owner is serious about selling, we start buying airplane tickets and making hotel reservations.

We keep the number of sellers we're representing to a manageable size. After we qualify the seller, we only accept assignments for which we feel we have a very high likelihood of success. We're in different stages of negotiations for each deal, so we're usually not needed at two places at the same time.

There are professionals who stay in our office and handle the administrative functions, prepare our client presentation books, use our many resources to locate buyer prospects and keep up with our traveling schedule.

When we're traveling, we correspond with the office through e-mail, receive documents at our hotel through overnight packages and fax messages. We track our activities through our custom-made software package and have a worldwide web page so buyers and sellers can learn about us. We have a large financial commitment to our resources, but it's all necessary to staying organized and efficient.

***How long does it usually take to sell a security guard company?***

We have consummated deals from start to finish in as short as two weeks. Normally, the process takes about three months, but much longer for European or South American sellers.

***What about confidentiality?***

I don't know of any business where the sale has to be handled as discreetly as that of a security guard company. As mentioned in an earlier question, our office is small by design and that enables us to handle the confidentiality aspects effectively. We don't have anyone outside our office we have to let know about the pending sale.

Sometimes we rent hotel suites to handle our meetings so the employees will not become suspicious. When we get to the due diligence stage of the transaction, we have the seller

bring the records to the hotel room; again so as not to create alarm among the office personnel.

Because we specialize in the security guard industry, we always know who the potential buyer will be. We do not have to advertise a company as being for sale or resort to mass mailings.

Some sellers have companies they do not want us to contact. We always get the seller's approval before we talk with a buyer.

***Have you ever been unsuccessful in closing a transaction for a seller/client?***

Yes – but this rarely happens. Our close ratio is over 90%. This means that we are successful in selling over 9 out of every 10 companies we represent. Which is probably better than any other intermediary firm.

When a transaction doesn't close, it's usually for reasons we can't control. Although we are very careful when we work with our client's competitors as buyer prospects, we had one client who would not allow us to contact a couple of competitors who were the best prospects for his company. Unfortunately, these were the only prospects that would pay our price – so the business was not sold.

Occasionally, we find out something about our client's business that we did not know before we agreed to take on the assignment. It may be that the geographic location is not attractive enough for the buyers or it may have something to do with the quality of our client's accounts. Such as; bad account contract indemnification clauses, too many contracts that require permission to assign or there may be several accounts that have been awarded under some "set aside" program.

We've learned a lot from the nearly 100 deals we've consummated. I know we'll learn something on our next transaction. We'll carry all these experiences to our future deals and help those sellers be more prepared for some negative aspects of their company. We'll get the negative corrected before we start the sale process or advise the owner that the company may not be saleable.

***We know that the psychology of a deal is very important and the initial meeting usually determines the tone for the remainder of the negotiations. What do you do to make sure the sale of a company gets started in the right direction?***

On this point, our firm does not believe in pinching pennies. We spend a lot of effort and money to make sure everyone is comfortable in negotiating meetings, especially that first meeting. For instance, we make it a policy to always arrive at the airport before a buyer gets there even if it means coming in the night before. We rent large cars so the buyer will be comfortable on the trip from the airport to the seller's office or our hotel. If we decide to set up the meeting in a hotel suite, we make sure we have a 4-A rated hotel that provides for a suite arrangement so we can have the meeting in a comfortable living room atmosphere. The first meeting should not last more than two hours.

***When is the best time to sell my company?***

It goes without saying that the best time to sell is when the aggressive and generous buyers are in the marketplace at the same time the owner has a real need to sell – such as retirement considerations, declining health, or personal problems. Also, this need to sell may be brought about by the owner not enjoying the business anymore or having financial restraints.

A company may be profitable but still have difficulty meeting payroll. This is usually brought about by fast growth and slowing down is not an option for most entrepreneurs. Banks are reluctant to give working capital loans to security guard companies because there are not enough hard assets to support this loan.

Selling is often the best option available to the owners of these companies short on working capital – although they're profitable and growing. Running the company on insufficient working capital causes unhappy employees and clients – which eventually leads to a diminution in the value of the business.

Many companies we have sold have been for owners who were too young to retire. They realized they could not make as much money owning the company as they could by selling it. They were able to keep their emotional attachment to their business in check. To them, the sale was just another economic transaction.

***I get three calls a week from someone wanting to buy my guard company. If I want to sell, it wouldn't be hard to find a buyer. Why do I need RHPA?***

Sellers who negotiate with the buyers and do not retain an intermediary think they are saving money. But the money they save is usually more than offset by the lower selling price they receive; not to mention the additional time they, their attorneys and their accountants have to spend dealing with the buyer.

It would be difficult to prove, but we feel we give our clients at least three times as much value as the fee we charge.

We're familiar with most of these "so called" buyers who are contacting owners. They're promising attractive prices and quick closings. But many of them do not have the financial resources to handle the size deals they're going after and even if they do, they're only interested in bargains. The sad part is that many owners do not discover this until after they've spent a considerable amount of time and money negotiating. Or even worse, they may not find out about it until after the deal is closed.

The prudent seller knows that there's more to selling a company than just finding a buyer. A due diligence should be done on the buyer, just as the buyer does one on the seller. This should be started as soon as the buyer makes the first direct contact.

Since we are familiar with most of the buyers who contact the sellers direct, we've already done most of this due diligence – we know their financial strength, contract requirements and ability to conclude a deal.

And if we know these prospects are not the most compatible for our client/seller, we can further advise the seller on other buyer prospects . . . ones who may be much better than the ones who contact the seller direct.

The way we developed many of these buyer prospects has little to do with how good we are. It has to do with the fact that we've been representing sellers for nearly twenty years. To my knowledge, no one has been specializing in security guard companies as long as we have. Nor have they completed as many successful transactions.

The fact that we've been in the business of selling security guard companies for a long time is important to a seller because it means we have a large pool of pre-qualified buyer prospects. Although we spend a lot of our time on the road (mostly in the air) meeting with these prospects, many initiate the first contact with us. They find out about us through my speaking engagements, our publications or from one of our satisfied seller/clients.

Some of these buyers are very generous and aggressive and are not already in the security guard business. So, it would be almost impossible for sellers on their own or through another intermediary to find them. Other intermediaries get their prospects from security guard company directories or lists of investment groups, who, by the way, usually don't want to buy security guard companies because there are no hard assets to support their borrowings.

Finding and developing a working relationship with some of these buyers was very time consuming and costly. We spent a lot of money traveling to the buyers' offices. Some were outside the United States, but we felt this personal relationship was necessary in getting our client/sellers the best deal possible. In fact, we make these buyer visits frequently.

Even though we have a good relationship with several buyers our responsibility is to our seller/clients. A very active buyer recently paid us the ultimate compliment . . . he said "when we buy a company you're representing, we pay 40% more than we would pay if we were to find the company on our own."

We are also a very valuable resource when it comes to negotiating the buy/sell contract. There are numerous issues that pop-up at the last minute. As I mentioned before, we've been a part of the negotiations for about 100 deals, so we have seen many issues get resolved at the closing table. Although, we occasionally see issues that are unique, most are ones that have been resolved on prior deals and we take those experiences with us to every contract-negotiating meeting.

In fact, the seasoned seller realizes how important our role is in not only finding and qualifying a buyer, but also being a part of the entire sale process.

**I need to mention something else that's very important:** Sellers who find a compatible buyer on their own should still retain a competent business attorney and tax advisor, as well as an intermediary. For most owners, their closely held business represents a substantial portion of their net worth and they want no mistakes when the time comes to sell.

Many sellers cannot act objectively on their own because they are too emotionally attached to this major asset. They have unrealistic expectations, a fact that will keep the business from being sold. Or they are too sympathetic with the buyer, a fact that may mean they leave a substantial portion of their net worth at the closing table.

These professional advisors can help keep the seller's emotions in check and work in tandem to make sure their client gets fair value for the business.

Several times, sellers who were already in negotiations retained us to represent them. They knew that finding the buyer was not the hard part. Finding the right buyer was the hard part. Orchestrating the negotiations in such a way that the seller and buyer walked away as winners was important.

**When an owner sells a security guard company, they don't necessarily get what they deserve. They get what's negotiated for . . . and that's where we come in!**

WE'VE HAD SOME CHANGES:

AREA CODE:

Effective December 15, 1997, our new area code will be 336.

E-MAIL:

[rhpamindspring.com](mailto:rhpamindspring.com)

WEB SITE:

Please visit our web site after December 1, 1997  
[WWW.roberthperry.com](http://WWW.roberthperry.com)

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This periodic informational letter is published by:

**ROBERT H. PERRY & ASSOCIATES, INCORPORATED**

Established in 1977, we are the recognized specialists in the sales and valuation methods for security guard companies. We have successfully represented nearly 100 sellers of security guard companies located in the United States, Canada, Western Europe, the Caribbean and South America.

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