NOTEBOOK OF IDEAS FOR

DIVESTITURES
OF SECURITY GUARD COMPANIES

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SEVEN HABITS OF HIGHLY SUCCESSFUL BUYERS . . . *OF SECURITY GUARD COMPANIES*

Stated simply – companies make acquisitions in order to increase shareholder value. However, this increase does not come with every acquisition. It only comes if the acquisition is successful. One that through increases in sales and profits, enhances the shareholders' investment ratios, with a prospect of continuing for a long time in the future.

Acquisitions are not successful by chance. They're a product of a plan, one that includes prompt responses, a proper due diligence, management of the transition, and an awareness of the important role the employees and customers have in the process. The plan also provides for the buyer to stay in contact with the seller for many months (and years) after the deal is consummated. The way the plan is executed will change many times as the successful buyer perfects the process.

Most of the acquisition activity in the security guard industry today involves large financially qualified companies buying smaller, closely held companies. Sometimes the seller has sales as small as one percent of the buyer's. Some acquisitions are successful while others are not.

Here are seven habits of the successful buyers of closely held security guard companies:

1 SUCCESSFUL BUYERS PLAN FOR THE ACQUISITION

Successful buyers do not buy companies simply because they're available. They buy according to the criteria established from a plan and they are disciplined about sticking to it. This prevents the buyer's decision-makers from reacting out of emotion, which would likely result in an unsuccessful acquisition.

The plan outlines the characteristics that they are looking for in an acquisition candidate. In general, the characteristics ensure that the seller's philosophy is compatible with the purchaser's and that the business does not diminish the company's profitability or standards.

The plan specifically outlines the types of accounts that are acceptable; the geographic area (city, state or country in the case of cross border transactions) into which they want to expand; the price the buyers are willing to pay and the terms they will require – both dictated by their target return on investment.

Also, an important part of the plan is having the financial, personnel and system resources necessary to handle the acquisition and transition. This may require additional executive and/or clerical personnel if enough qualified people do not come over from the seller. It may also require upgrading the computers to handle the increase in payroll, billing and auxiliary reporting requirements.

2 SUCCESSFUL BUYERS RESPOND PROMPTLY

A very important aspect of successful negotiations is creating a deal momentum in the initial stages and keeping it going throughout the process.

If the buyer prospect finds out about the seller through an intermediary, chances are there are several other buyers being considered. For this reason, the successful buyer moves quickly but prudently. By doing this, the buyer is sending a message to the seller that it is very interested in the company. It doesn't want to lose the opportunity to a competing buyer and it will get the deal done quickly. This is what the seller likes to see happen.

Successful buyers do not require all the information on the seller before they decide to take the negotiations to the next level. They promptly evaluate the initial information and if interested, they communicate their interest orally and set up a get acquainted meeting with the seller. As soon as they have gathered enough information to make an intelligent decision and have developed a rapport with the seller, they make an oral offer, then promptly confirm it through a letter of intent. Their goal is to get an exclusive negotiating period by pushing their competitors aside, so the sellers will not become distracted from competing offers.

The prudent buyer knows that even though the company may be off the market for other buyer prospects, there is still one very large competitor in the deal - the seller.

The buyer is now dealing with the seller's emotions. If the process loses momentum, the seller will become impatient and have second thoughts about selling; this may cause the seller to terminate the negotiations.

3 SUCCESSFUL BUYERS PERFORM AN ADEQUATE DUE DILIGENCE

Most buyers' due diligence processes do not fit the selling company. They examine too much or not enough information because they take a "one due diligence list fits all" approach to their acquisition program.

Successful buyers, on the other hand, customize their due diligence process to fit the characteristics of the seller. They know that the due diligence for a stock purchase has to be approached differently than one for an asset purchase.

They prepare a list of the documents they need to examine, then send it to the seller far in advance of the due diligence date. When the due diligence day arrives, the process is expedited greatly by this advanced planning.

Successful buyers spend a lot of time examining the more important documents pertaining to profitability and risks – such as billing invoices, payroll registers, account contracts, post orders, employee files, etc. They also spend a lot of time evaluating the managers and other employees who are needed after the acquisition. They spend less time (or no time) examining corporate charters and forecasts (which are usually meaningless for closely held companies).

Successful buyers do not expect accurate financials from the seller as a basis for determining the price. They recognize that small security guard companies can't afford elaborate systems. The financials presented are often inaccurate because of improper matching of revenue with expenses. The buyers overcome this by building their own financial model based on their experience in running similar operations.

And one of the most important aspects of the due diligence is its confidential treatment. If the seller is not ready to announce the negotiations, the buyer performs the document due diligence off-site or in the seller's office at night after the clerical employees leave - so they will not become suspicious.

4 SUCCESSFUL BUYERS PAY A FAIR PRICE

Paying a fair price does not mean overpaying. It means giving the seller its due, a move that will keep the seller motivated to help the buyer if problems or issues arise during the transition. An even more important reason is that it turns the seller into a valuable reference and ambassador for the buyer in future deals.

Successful buyers arrive at the price by going through a return on investment computation rather than using some street formulas based on multiples of gross units (monthly billings, dollars per billable hours, percentage of annual sales, etc.). The computation allows for a premium for quality accounts, good retention history and capable management, even if the premium takes the pricing far in excess of what it would be by using some multiple of gross units method.

These buyers offer their best pricing in the initial stages of negotiations. They are aware of the probable consequences of alienating the seller by submitting a low initial offer, then playing drawn out “guess what the price is” games in order to find the seller’s real price level. They also know that they are probably competing with other buyer prospects and they do not want to lose the opportunity.

Successful buyers that intend to make several acquisitions pursuant to some “roll-up” or “consolidation” plan know that their pricing and the way they conduct themselves during the negotiations are important for future deals. Their reputation as a good or bad buyer quickly spreads throughout the industry.

5 SUCCESSFUL BUYERS MANAGE THE TRANSITION

Getting to the closing is just one step in a successful acquisition. Another very major step is deciding whether the seller’s operations will be integrated with the buyer’s or continue as a stand alone.

Regardless of the decision to integrate the companies, the customers and employees must be contacted before they hear about the sale from the street rumor mill. Successful buyers quickly notify the employees and confirm their continued employment, pay rates and benefits. High-ranking executives of the buyer make themselves available to answer questions from nervous employees.

The seller and a representative of the buyer visit the most important clients quickly. They assure the accounts that there will be no changes in the service – the bill rates will not change and the present guards will continue at the account.

If the companies are to be integrated, the account billing and payroll processing information is promptly entered into the buyer's computers. The buyer knows that accurate billing and paying the guards timely is essential in keeping an account satisfied. If the seller has an adequate system, the buyer may run the billing and payroll on this system for a while after closing, then gradually make the change over.

As mentioned in some of the habits listed above, the successful buyer keeps the seller involved after the acquisition. The seller, in most instances, has a relationship with the accounts. The seller can help to ensure a smooth transition.

6 SUCCESSFUL BUYERS DEAL FAIRLY WITH THE SELLERS ON POST CLOSING ISSUES

Most transactions provide for some type of contingency to the seller receiving the entire purchase price. It may involve paying the seller for additional business brought in after the closing or an account retention condition. It’s impossible for a buy/sell agreement to address all the eventualities that may effect the computations.

This means that some aspects of the negotiations may carry on past the closing. The buyer and seller may have to face each other again to resolve some of these issues. The seller has to rely on the buyer’s sense of fairness in dealing with these situations.

Successful buyers are very protective of their reputation in dealing fairly with sellers and how this reputation is spread throughout the industry through the “circle of influence” principle. This principle involves the widening dissemination of a message from a few persons to many people. Here’s how it works: a satisfied seller tells two other seller prospects how he was treated in a deal. Each of these two prospects tell two other prospects; each of these tell two other prospects – the message travels exponentially. If the buyer mishandles some post closing issues, the word spreads faster, and to more prospective sellers. Negative stories spread more quickly and are harder to control than positive ones.

7 SUCCESSFUL BUYERS RESPECT THE SELLER/INTERMEDIARY RELATIONSHIP

Some buyers consider the seller's intermediary as an unnecessary cost to the deal – which, although compensated by the seller, is passed on to the buyer through an increased asking price. Also, some buyers do not want a seller's intermediary involved since they stand in the way of the buyer getting a bargain by taking advantage of the seller's inexperience in the acquisition process.

The successful buyer on the other hand realizes that the intermediary has invested several months (or years) developing a relationship of trust with the sellers before they make the decision to sell. The intermediary has gone with them through the emotional decision making periods.

The relationship cannot be duplicated between the buyer and seller because the seller maintains a barrier of defense that keeps the buyer from getting too close.

The seller will be looking to the intermediary for advice on price, which will not be a bargain, but will be realistic. The seller will also solicit the intermediary's advice on terms.

Successful buyers recognize this special relationship between the intermediary and his client/seller. And that through keeping the seller realistic on price and terms, and adding other valuable assistance to the transaction, the relationship actually benefits both sides. Therefore, successful buyers make sure they go through the intermediary to obtain information and set up the meetings.

Successful buyers want to be put on the intermediary's preferred buyer list for future sellers the intermediary may represent. To do this, the buyers respect the seller/intermediary relationship.

This periodic informational letter is published by:

ROBERT H. PERRY & ASSOCIATES, INCORPORATED

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

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