

Selling Your Child Care Business: Laying the Foundation

by Keith Stephens

***Editor's Note:** In researching for an article on how to determine the value of your child care business, we realized that what we needed were two articles. Not only did we need to address how to determine the selling price of your business, but also how to prepare organizationally and emotionally for the selling process.*

In addressing the latter point, we reviewed an article written by Keith Stephens based on his successful experience in selling his child care business, Palo Alto Preschools. We discovered that his advice is as helpful today as it was when we published it in our September 1986 issue.

So, in this issue, we are reprinting Keith's article with some insights from current buyers and sellers inserted. In the next issue, we will publish the article on how to calculate the dollar value of your business.

The time to prepare for the sale of your business is now. In order to secure a satisfactory sale price, you need to do your homework. How you organize and manage your business today determines its salability tomorrow.

Have a sound record keeping system in place.

When it comes time to sell, potential buyers will be interested in not only what your bank balance is today but also how your business has

performed over time. If you want to get a good price, you have to be able to make the case that you have a growing business with a solid track record. Without sound records, you have no case.

Keep financial information in standard formats.

In the sale of your business you need to communicate serious financial information to potential buyers. You need to present your information in a format that can be quickly understood by the recipient. Most buyers will not have the time, or the desire, to learn how to interpret information presented in a new or unusual way.

Keep the components of a financing package on file.

At Palo Alto Preschools, because of our ongoing need for capital for expansion, we always had a package of information about our business on file to present to bankers, mortgage brokers, and venture capitalists. Having the components of this package on file enabled us to respond quickly to unexpected needs and opportunities. Information you may want to start accumulating in your files will include:

- Overview on the status and trends of the child care industry;
- Current structure of your organization;
- Profiles of your key management personnel;

- Key strengths and unique features of your business;
- Detailed financial information;
- Enrollment records; and
- Summaries of mortgages and leases.

\$ Build a management team.

Many child care businesses have prospered due to the toil and talent of the owners. However, even if these businesses are extremely successful, potential buyers may be scared away, fearing that the business will fall apart once the original owners leave.

The development of a management team in a closely held business cannot be left to the last minute. It is a slow, sometimes painful, process. First, you must adjust to the idea that you do not need to do it all. You must be willing to let others make some of the decisions. Second, you need to identify people with management talent. Finally, you need to bring them along slowly but steadily by giving them increasing amounts of responsibility.

\$ Develop relationships with potential buyers.

In looking back, I find one factor about our sale to be especially interesting. All the companies that in the end were seriously negotiating with us were companies with whom we had a long-term relationship. All our other efforts to attract buyers produced nothing.

I cannot stress enough the importance of being visible in the industry. Building relationships now will pay off when the time comes to sell your business. If potential buyers already know who you are, who your people are, what your

strengths are, and where your business is heading, you stand a much better chance of attracting their interest. Otherwise, you are just one of many faces in the crowd vying for their attention.

Know Where You Stand

Before you start actively promoting the sale of your business, it is vital to determine what you hope to accomplish. Once you start negotiating, you can easily lose control of the process if you aren't clear in your own mind as to what constitutes favorable terms and conditions.

"You must be realistic about potential buyers. National chains are primarily interested in large, commercial grade facilities in major metropolitan areas. If you do not meet these criteria, you need to approach smaller local chains as well as new players looking to get a start in the business."

◆ Henry Tiberi, Children's World Learning Centers, Golden, Colorado

\$ Set a value on your business.

Once we decided to sell Palo Alto Preschools, we sat down and worked out a sale price that we believed accurately reflected the net worth of our business. This was not a value that we plucked out of thin air, but one that we arrived at through a set of standard calculations for determining the value of a business. It was a price that would provide us with a favorable return on our investment, but also one that we could reasonably defend.

In dealing with potential buyers, we gave out this price right away. Serious buyers, of course, ended up generating their own numbers, based on their own calculations. But having our numbers on the table gave us a position to negotiate from, rather than forcing us to respond defensively to their numbers and their method of calculation.

In setting your sale price, you've got to be reasonable. You should expect a reasonable return on your investment, not a windfall. If your expectations are too high, you will be engaging in a futile effort.

\$ Determine how you will respond to various offers.

In addition to determining what your business is worth, it is also important to decide in advance what position you will take on various terms and conditions a potential buyer may propose. For example, the buyer may agree to your price, but recommend that payment be made over a period of years. Or the buyer may propose implementing the transfer of ownership by swapping stock in their company for stock in your company. To intelligently respond to alternatives such as these, you will need to consider your personal cash needs as well as to investigate the tax implications of each of these alternatives, both for the buyer and yourself.

During negotiations, the nature of your involvement after the sale will undoubtedly become an issue. From the outset, you should have a position that covers under what conditions, if any, you will continue working for the business after the sale, either as a long-term employee or as a short-term consultant.

Prepare for the Process

The process of selling your business can be a draining experience, both

physically and emotionally. If you are not fully prepared, your bargaining position may erode as your energy and emotions wear down.

\$ Make an irrevocable decision to sell.

If you enter into the sale process only partially committed to doing a deal, you will not be as aggressive nor as effective a negotiator as you should be. You must be committed to following through until a deal is done or you will find too many excuses to back out, or equivocate, when the going gets tough.

\$ Decide how much to inform staff and parents.

Once you have made the decision to sell, you need to decide when and how to inform the staff and parents. Some would argue that you should tell them as little as possible until the deed is done. The argument here is that if staff and parents know the center is on the blocks, they will become apprehensive and start abandoning ship.

We decided to take this approach with parents and did not officially inform them until after the sale was completed. Inevitably, of course, parents started finding out via the rumor mill. However, there were no serious repercussions.

With the staff, we chose to be completely open from early on. Shortly after we started receiving serious offers, we held a meeting of all the center directors to discuss what was taking place. We told them who we were negotiating with and how we thought things would change for them under each of these companies. We tried to stress the career opportunities they would have in each case.

We decided to be up front about

all this because we figured that, with all the visitors going through taking pictures and asking questions, the staff would soon put two and two together, but would come up with the worst possible interpretations. Staff members accepted the news surprisingly well, and in the end no one quit over this issue.

“The best time to sell is when you don’t need to. If you wait until you have no choice but to sell, you have limited negotiating options. But if you can walk away from any deal and continue to operate your centers, you are in a strong position.”

◆ Richard Goldman,
Another Generation Preschools,
Fort Lauderdale, Florida

\$ Set up your business to run without you.

Don’t underestimate the demands that will be placed on you from the day you decide to sell your business. Much of your time will be consumed with preparing reports, meeting with your accountant and your lawyer, meeting with potential buyers, giving tours of the center, and tracking down endless pieces of information. In order not to frustrate potential buyers, you will need to drop whatever you are doing and find answers to their many questions.

Meanwhile, your business needs to keep operating in top form. If your business falls apart while you are preoccupied with making a deal, you may lose the deal and your business, too.

Therefore, you need to delegate, in an orderly fashion, the day-to-day operation of your business during this period. If you are a small child care operation owned by a husband and wife, possibly one spouse could take over the operation of the business and one the sale negotiations. In a larger operation, you will need to entrust operations to your management team.

\$ Be prepared for the extreme emotions of the process.

One day you will be sky high about the prospect of receiving a high return on your investment, and the next you will be depressed because you are giving away your baby. One day you will be as proud as can be showing your excellent facility off to a prospective buyer, and the next you will be down in the dumps when they call back and say they’re not interested in what you consider to be your centers’ strengths, or that your centers aren’t big enough, or they cost too much to operate.

You’ve got to be prepared for this emotional roller coaster. If you’ve cared enough about your business to make it a successful venture, inevitably you will have a difficult time letting go, and a difficult time accepting negative assessments of your business.

This is all very natural — there’s nothing wrong with you if you experience these emotions. But you can’t let these emotions preclude you from conducting the negotiations effectively.

One of the hardest issues to deal with will be when potential buyers start proposing changes they will make. For example, they might observe that they will have to bring in a new director to replace someone you have worked closely with for many years, someone you care about deeply. Or they may propose

tearing out some walls to make the classrooms bigger, or doing away with the infant component, or closing your favorite center.

Your reaction to such proposals may well be one of anger — “They’re going to tear apart in months what it has taken years to build up!” But you have to keep in mind that once you sell your business the new owners will inevitably want to put their stamp on it, to make changes to fit their goals, their style, their mode of operations. If you cannot accept such changes, you should not be selling your business.

\$ Negotiate Openly and Knowledgeably

Now it’s time to get serious. In actively seeking to sell your business, you need to find the most likely candidates, to give them a clear picture of your business, and to maintain your energy until the deal is done.

\$ Hire a broker and a lawyer experienced in the sale of businesses.

You will want the best possible players on your team. The lawyer who has been handling your real estate deals and writing your contracts may not be capable of representing you properly in negotiating the sale of your business. You need a lawyer who is experienced in handling mergers and acquisitions, who is knowledgeable about the legal and tax questions you will encounter, and who is familiar with the up and down emotions of the acquisition process.

Next you need to find a good broker. You may be tempted to try to save some money by selling it yourself. But selling a business is a complicated process. You need to turn it over to someone who is trained to

do it right. You also need someone on your team whose only interest is in keeping the deal moving. You will want a business broker, not a real estate broker. Selling a business is vastly different than selling a piece of property.

\$ Aggressively approach potential buyers.

Sit down with your broker and draw up a list of any and all parties who may be interested in buying

“Your strategy as an ongoing business owner may be in direct conflict with your interests as a seller. You may aggressively act to minimize your tax exposure by running personal expenses through the business, expensing capital investments, and occasionally under-reporting your income. While this may increase your current income, it may make it difficult for you to convince potential buyers that you have a profitable business.”

◆ Clark Adams,
Mulberry Child Care Centers,
Needham, Massachusetts

your business. This list will include child care chains known to be operating in or interested in your community, as well as any individuals and organizations that have expressed an interest in educational ventures in recent years.

Organizations looking to jump into the child care business in a big way may also be worth pursuing. These will, of course, be harder to locate; but contacts you have established

through state and national organizations may help give you some leads.

\$ Be open.

Don’t be afraid to give people information. You’re not going to make a deal unless you give the buyer a complete picture of what you are selling. A natural tendency is not to give away your company secrets. But in this industry there aren’t that many secrets — it’s really a matter of who works the hardest.

In selling Palo Alto Preschools, we gave out detailed information to all interested parties. In one case, a company looking to expand in the child care business came back to us over and over again with requests for more information. In all, we devoted over 100 hours to educating them about our company. And we never heard from them again. I felt that we had been taken advantage of. But this was a risk that we decided we needed to take. If we hadn’t been completely open with everyone, we wouldn’t have maintained the interest of the three potential buyers.

\$ Be honest.

Don’t try to fudge the facts. Companies that are in the business of acquiring other companies have better accountants, better lawyers, and better business people at their disposal. There is no advantage in trying to make your numbers look better than they really are because they are going to uncover this. And once they do, the deal is off. All you are doing is raising a red flag to mistrust all the information you are supplying.

\$ Be persistent.

Even in the smoothest of sales, it’s going to take a long time from start

to finish. In our case, it took seven intense months. There will be many times when you get frustrated, angry, or discouraged. There may be times when you feel like bagging the whole deal, or settling for a lesser deal just to get it over with.

However, if you have invested 10 to 20 years of your life building up your business, you don't want to throw this away because you can't hang in there to the finish. Your mental toughness in the final weeks of negotiating will pay dividends that you will appreciate the rest of your life.

“If you have built up a successful business from scratch, you will want to be rewarded for all the time, energy, and creativity you have invested. However, you must face the real possibility that your extraordinary contributions may not be an asset from the buyer’s point of view. If your center is dependent upon your efforts and talents to be successful, its value may seriously decline with your departure.”

◆ David Gleason,
CorporateFamily Solutions,
Nashville, Tennessee

From 1970 to 1986, Keith Stephens was president of Palo Alto Preschools which operated 30 child care centers in the southwestern states. He is currently CEO of World Timbers, Inc., and a CPA and consultant with Zephyr Management Services in Phoenix, Arizona.