

HOW TO ACQ

Are you ready to expand? Buying out or merging with another rental company can be a quicker path to new revenue than opening up a brand new store—if you can avoid the pitfalls going in.

BY JIM TENNANT

You can probably remember the days when there were eight separate, standalone national car rental companies. There are still eight separate brands visible to the public, but behind the back walls just four companies (as of this writing) own the eight brands. The companies have realized substantial savings through combined fleets, employees and support infrastructure, and have probably strengthened the industry by keeping the eight brands alive in the public's eyes.

Merging operations have worked for the large national companies. Can it also be a winning strategy for much smaller, local or regional companies? Can you strengthen your company and improve your bottom line by merging with or buying another car rental business?

WHY TAKE OVER SOMEONE ELSE'S BUSINESS?

In order to get into a new geographic area. Opening a store from scratch in a new area can be very time consuming and costly. You need to find a suitable location that presents a good face to the public and has a place to clean and store your cars—not easy in some areas.

You will need to spend money on leasehold improvements, signs, furniture and equipment, computers, etc. You may have to deal with zoning and licensing issues. You will need to hire and train employees or take them from your existing locations.

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AN AUTO RENTAL COMPANY

The day you open, you will have zero business. You will face a long building process before the store is covering its overhead and putting money toward your bottom line.

Is there an existing business in the prospective new area? Would it be better for you to take it over instead of starting from scratch? In the early days of our company, we operated a small location near San Francisco International Airport (SFO), and we had dreams of opening in downtown San Francisco, an area with great tourist and local business potential. It was probably not as difficult an area as Manhattan, but close. It was too much for our limited resources, so it did not happen for the first three or four years we were in business.

One day we spotted a classified ad offering a small downtown car rental business for sale. We were able to buy it on good terms and instantly had a downtown location complete with parking, a wash bay and, most importantly, a steady stream of existing business.

2 To grow your business much faster than organic growth allows. The major companies realized significant savings by combining back room operations and fleet. Economies of scale exist in almost all businesses and a 20 to 30 percent or greater increase in your revenue might be much more valuable than the same revenue operated as a standalone business.

Buying another business in your present area could make a lot of sense. You can expect that the combined businesses will lose some existing revenue to the competition in a merger, but handled correctly the loss can

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be minimal. Additionally, under the right circumstances, you can capture new revenue from the merged company by offering a wider range of vehicles, newer vehicles or additional services, such as customer pickups from a wider area.

3 To get into a new market segment. Have you wanted to offer luxury vehicles or large passenger vans? Have you been looking for a way to get business from a large corporate account or government business in your area? Like a new geographic area, you can enter these segments on your own and suffer the missteps and startup labor and costs that go with it. But what if there is a business already in that segment? Would it make sense to buy this business? Those business owners have already done the work and made the mistakes that you might make.

When we bought the little downtown business, it not only had the steady stream of walk-in business because of its excellent location, the staff also had good contacts with hotels and local corporate accounts. We offered a wider range of newer and much nicer vehicles and were immediately able to increase this business.

Jim Tennant and the Tennant Group Roundtable return to the Car Rental Show for a two-hour, pre-conference seminar (Tuesday, March 8, 10 am – noon). This year's session will feature a confidential, one-on-one analysis of your company's operating and financial data by an experienced, non-competing roundtable member. Free, pre-registration required.

CAR RENTAL SHOW
CAR & TRUCK RENTAL CONFERENCE & EXPO

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WHAT DO YOU GET WHEN YOU BUY A BUSINESS?

You might buy a business for any number of reasons, some of which are outlined above. However, when you buy it, you inherit certain things that you need to think about carefully.

Location. The physical location might be your main reason for buying or you may unwillingly acquire a location as part of the deal. If you plan to keep it, be sure you can.

When we bought the downtown business, the sellers were on a month-to-month lease because they were not sure of the future of the business. Before committing to buy, we met with the landlord, who was delighted to have stable, experienced operators as tenants. We were able to lock up the location in a very favorable long-term lease.

On the other hand, if you do not plan to keep a location, the cost of getting out of the lease, if any, is part of the acquisition cost of the business.

2 Employees. You may or may not want to keep the business's existing employees. Our experience in taking over a number of businesses is mixed, to say the least. Some of the best and some of the worst employees have

come from businesses we have taken over.

When you take over a business, the seller should discharge all employees and take care of any sick time, vacation or other pay owed and any other commitments to the employees. You will start fresh. If you need employees, the previous employees are obviously a good source, but there are many potential pitfalls. Do not hire all the employees. If you took over the entire staff, employment regulations may view you as merely new owners of an existing business, and you would then be liable for their years of service and other employment obligations.

The seller should first explicitly terminate the employees, and then you should have them apply, just as they were coming off the street. Plan on retraining and spending time orienting the new employees—you will have bad habits to break. If possible, move employees around so that old and new employees are working side by side. There are pitfalls, but the old staff knows the area, has a relationship with the customers and knows the market segments that are new to you. You'll want to take advantage of this while not degrading your existing business.

With the recent turmoil in the industry, loss of financing, insurance or sources of affordable vehicles can all be great motivators for prospective sellers. For someone facing these types of issues, a potential buyer, willing and able to put together a fair deal, could be the best thing that ever happened to him or her.

3 Vehicles. It is difficult—if not impossible—to get out of vehicles in the middle of their lifecycle, so often the seller's vehicles are a big part of the deal. When we bought the downtown business, the sellers were running older vehicles. We ordered additional vehicles, but they would not be delivered for a few weeks. The sellers were able to sell off some of their fleet immediately, but as part of the deal we leased the balance of their fleet at their carrying cost while they sold them off one or two at a time. It was a small price to pay to let them

get out cleanly and for us to have sufficient vehicles to keep the business running.

We bought a much larger local company many years later and the vehicles were the major consideration. The seller's vehicles were all financed through Ford Motor Credit, which was delighted to have our company, with its perfect history with Ford, take over the financing. We worked out an equitable arrangement to cover the difference between the amount owed and the actual value of the vehicles, taking into account that we would hold and sell the vehicles at the end of their normal life cycle.

The seller's vehicles will often be the most difficult part of the deal. It is important to understand the seller's problems and then get creative in coming up with an equitable solution.

4 The Business Name. You will probably want to switch the new business to your name, unless the old name is better or has value itself. However, when you make the switch you should do it in such a way that you don't lose the goodwill and existing business of the old name. Sometimes a gradual, two- or three-step conversion is best.

THE ACQUISITION CHECKLIST

Before making an offer, go through this checklist:

● **Price.** What is the business worth to me? Everyone focuses on price and it is obviously important. But if the deal is right, price is just one part of it, and you can afford to pay a fair price. If the fit is wrong, you don't want the business, even if it's free.

The most common valuation method is a multiple of adjusted earnings — net earnings before taxes, but with all the items extracted that are not really part of the business. This includes owners' salaries greater than what you would pay an outside manager. It also includes family vehicles and other goodies that you draw from the business. A normal multiple would be three to five times, depending on the situation.

● **Employees and Management.** Is your management strong enough to oversee a larger number of employees? Are you capable of running a larger company? How does your company handle change? In our experience, this is where you can go wrong most easily. It will be more difficult than you think.

● **Financing and Cash Flow.** You will need more vehicles, of course, but you also should anticipate increased operating cash needs during the takeover period — they will probably be greater than you think.

● **Accounting and Computers.** This is critical. You need computers up and running in all offices the day you take over. Be sure your accounting system can begin billing new customers immediately.

● **Personal.** At this point in your life, are you looking for new challenges or are you satisfied with the status quo? This should be the last question you ask just before you make an offer, but it is perhaps first in importance. You will be leading your company into new territory and you need to be sure!

● **The Transition.** The best deal can be made much worse by poor planning and execution of the takeover. Who gets the revenue from cars on rent on the takeover date? Who is responsible for damage and third-party claims on vehicles on rent at takeover? What is the procedure for receivables during the transition? How will you handle the announcement to the employees, existing customers, vendors and the public? All these and many more questions should be addressed as part of the agreement, but some details will be missed. Trust and the ability to compromise will be necessary.

The seller has to give up all rights to the name. Usually, the seller can assign the county fictitious name registration to you, and if he holds a state or federal trademark, it must be assigned as well.

5 Other Assets. Computers, furniture, counters, office equipment, shop equipment and other assets have little market value but can be quite valuable to you because they are expensive to replace. Each situation will vary, but these items should be addressed as part of the deal.

WHO ARE POTENTIAL TAKEOVER CANDIDATES?

Supposedly everybody has his or her price, but a young, vigorous owner, making consistently high profits with no need to finance, and who is self-insured and has no personal or family issues will have a much higher price.

Good candidates are veteran owners, especially if they do not have anyone in the next generation willing or capable of taking over. With the recent turmoil in the industry, loss of financing, insurance or sources of affordable vehicles can all be great motivators for prospective sellers. Divorce, death of a family member, health or other personal issues could play a role as well.

Keeping your eyes open for any of these potential candidates could pay back in a big way. For someone facing these types of is-

suues, a potential buyer, willing and able to put together a fair deal, could be the best thing that ever happened to him or her. Don't think that you are unfairly taking advantage of a bad situation.

HOW DO I APPROACH A DEAL?

In our experience, trust is the first and most important key to putting together a deal. Some are good at playing business hardball, but that is not our style. A low-key, win-win approach has worked well for us. Get involved with the business's advisors early on. Accountants and attorneys often have a more realistic and less emotional view of the business than the owner, but that will not always be true.

1 Ask questions and listen. Ask all the questions you can at this point. What is the seller's motivation? What are his problems? What does she really need? How are vehicles financed? How much equity is there in the vehicles or how much are they upside down? What debts are personally guaranteed? What are the terms of the location leases? What are the seller's plans after the sale? Does he or she want to retire and travel? Would he or she want a role in the company for a while?

2 Know your benefit. Ask yourself these questions. What will buying the business do for you? Are there economies of scale? Are the locations valuable to you? Are they in market segments that would help you? What is the business worth to you?

3 Analyze the value. How much does the seller want? It may be that the seller would be satisfied with less than you thought, so you should always ask this. In our experience, though, the seller is factoring in a lifetime of work, sentimental value and other things that are of no value to you. Do not react to the price. Just ask more questions as they come up and say you will get back with them.

4 Structure the offer. Be as creative as possible in structuring an offer. The terms are in some ways as important as the price. A percentage of revenue may be a good approach, because the seller may have a high regard for his business, and you are protected if the revenue comes in lower than expected. You pay a commission to a travel agent — why not pay the seller?

When we purchased the local business, the terms were that we took over the financing of the vehicles, with an adjustment for market value at the end of the holding cycle, plus 10 percent of the revenue from the acquired locations for six months. The vehicles are probably an important issue to the seller, so try to come up with an approach that, while not harming your operation, gets the seller out of his vehicles cleanly.

5 Show respect. Above all, show the seller and his or her business respect for the lifetime of work he or she spent building it.

Obviously, mergers and acquisitions in the local and regional end of the car rental business will not keep Goldman Sachs in business, but it can be a great opportunity under the right circumstances. 🚗

A HISTORY OF BUYING AND SELLING

Jim Tennant was the founder and partner of car rental businesses based in the San Francisco Bay Area from 1982 to 2001. During that time, his company completed the following sales and purchases:

- Bought a small, local downtown San Francisco franchise using a small down payment and a three-year note. Leased a few of the seller's vehicles for carrying costs until they were sold. The location (which later became a Payless franchise) had a very strong manager and the office paid for itself much faster than anticipated.
- Sold the Payless franchise and business to a sophisticated buyer with no car rental experience. The price was based on a multiple of adjusted earnings, plus two years paid consulting assistance. Gave buyer rights to Ford repurchase vehicles, plus leased

buyer a small number of vehicles to help in transition. After takeover, spent considerable time with the seller, who is very successful today.

- At the same time as the Payless sale, purchased the money-losing but much larger Thrifty Car Rental franchise and business, with a down payment plus a five-year note.
- Purchased large local, multiple-location rental business. Very little overlap between new and existing business offices; closed only one office. Paid 10 percent of acquired offices' revenue for six months, plus took over vehicles that were not yet ready for sale. Ran into many unanticipated problems, in no small part due to broken promises from the telephone company, resulting in a delay in having all offices online.



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