

Selling? Make sure the price is right

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On paper, Avalon Woods Health Club appeared to be the ideal acquisition. To make certain, however, prospective buyer Carmen Tanious "secret shopped" the west-end Toronto gym to determine whether she would indeed be getting good value for her investment.

Ms. Tanious slipped into the club on a couple of occasions, without disclosing her interest, to get a better feel for the place. She conducted surreptitious drive-bys and found that, no matter the time of day or night, the upscale club, which caters primarily to baby boomers, was always humming.

Ms. Tanious had examined the revenue figures and could see that the equipment was top of the line, the property was immaculately maintained and the decor was "stunning."

But to gauge the potential for expansion and earnings growth - a key consideration - Ms. Tanious knew she had to get a handle on the more intangible aspects that can make or break a small service-oriented enterprise: the employees ("amazing people, dedicated staff," Ms. Tanious found), the customers ("I could see they were enjoying themselves") and "the vibe."

What clinched it was author Catherine Gildiner's fireside reading in the club's lounge one December evening. Ms. Tanious was in the audience. "Being an avid reader, I just so fell in love with that. I thought, what a brilliant, brilliant concept" - a health club that caters to its members' intellectual interests as well as their physical fitness requirements, Ms. Tanious said.

She stayed behind and introduced herself to Avalon Woods founder Cleo Chmielinski, who was selling the business. "The deal was struck that same night, and we signed the papers," said Ms. Tanious, a businesswoman who owns a small catering operation. "I think we both did quite well, actually. We're both happy," she said.

Ms. Chmielinski, a chartered accountant who also has a demanding workload as a business consultant and academic adviser, told Ms. Tanious that she could not devote enough time or energy to position the company for the next phase of growth as the economy emerges from recession. Consumers remain cautious, Ms. Chmielinski said, but a full-time operator with more time to invest should be able to drive up the value of the business.

Ms. Chmielinski was candid: The health club, launched in the spring of 2007, "has been able to demonstrate a continuing growth in revenue, despite the recession ... but it certainly didn't meet our targets."

There is no question that the economic downturn adversely affected the profitability of Canadian businesses - including her own - and dampened valuations, said Ms. Chmielinski, who, as the

former chief financial officer of a large home health-care provider, has had plenty of experience acquiring small businesses and determining their value "from the other side of the table."

But not all business owners are prepared to acknowledge the toll the recession has taken on prices, said Suzanne Loomer and Priti Mehta-Shah, chartered accountants and valuation specialists with BDO Canada LLP. As a result, there is sometimes a "disconnect" between what sellers think their businesses are worth and what buyers are willing to pay.

Pre-recession, when financing was readily available, "multiples were very high," Ms. Loomer said. It is too soon to say whether credit conditions have loosened enough to spur much of a renewal in merger and acquisition activity, she added, but buyers and sellers are emerging to test the markets again.

Coldwell Banker business broker Steve Skrlac, who worked on the Avalon Woods transaction, estimated, as a broad rule of thumb, that small- to mid-sized businesses are being valued at multiples of two to three times cash flow today.

Because of her professional background, Ms. Chmielinski was better equipped than most to determine the value of her own enterprise. "I did my homework, I spent a lot of time researching recent sales in the industry."

In the case of Avalon Woods, the fact that the club owned all of its equipment was an advantage when it came to the valuation, she said.

Given the times, Ms. Chmielinski listed her company in November at what she describes as "a realistic" price and resigned herself to waiting six to nine months before the business sold. To her surprise, the business sold to Ms. Tanious within three months - for close to the listing price, which neither woman will divulge because it was a private deal. (Current listings for Toronto-area fitness businesses range from as low as \$60,000 for some franchise operations to \$250,000 for higher-end businesses with more amenities.) The BDO accountants, who were not involved in the Avalon Woods transaction, consider many of the same factors when determining the fair market value of a company: assets, cash flow, future earnings potential, risk, and general economic conditions.

At Avalon Woods, Ms. Tanious and Ms. Chmielinski pretty much saw eye to eye on the value of the business from the outset. For the past month, as part of the deal, Ms. Tanious has been job-shadowing Ms. Chmielinski, learning the ins and outs of the operation and getting to know the customers.

Over coffee in the lounge of Avalon Woods, shortly before the transaction officially closed, Ms. Chmielinski outlined some of the initiatives she introduced to get more prospective members through the door: the authors' nights; financial planning workshops; seminars on dating strategies for single boomers; informal networking sessions with local entrepreneurs, who meet at the club and swap referrals. (Ms. Chmielinski related that one of her business network buddies, a funeral home director, recently referred a prospective client who had gone to him to pre-plan her funeral. He suggested that she might want to check out the health club, in the interim.) "You might want to continue this, Carmen," she said.

Ms. Tanious nodded, taking it all in. "There's a lot to absorb, that's for sure. I'm totally immersed, and I am loving every minute."

VALUATION TIPS

Leave enough 'runway'

Advice from a valuator will help maximize the price and salability of a business, says Suzanne Loomer, a Toronto-based partner with BDO. In addition to "cleaning up the balance sheet," this could involve formalizing verbal agreements with key managers, suppliers and landlords.

"A lot of value can actually be created before the business is put up for sale," said Howard Johnson, managing director at Veracap Corporate Finance and a chartered business valuator. However, many business owners wait too long "and give themselves very little runway."

Reduce the tax bite

There are three parties to every deal: the buyer, the seller and the government, Mr. Johnson said. "It's not how much you sell the business for, it's how much you get to keep in your pocket that's important."

Do a reality check

If a business is not priced appropriately buyers simply won't look at it, says Coldwell Banker business broker Steve Skrlac.

Some business owners withdraw from the market when offers don't meet their expectations, says Priti Mehta-Shah, a Winnipeg-based partner with BDO Canada LLP. "There's a real danger in doing that, because you don't want to go to the market too often ... and you may have given a lot of trade secrets to somebody doing due diligence."

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