11 QUESTIONS COMMUNITY BANK ACQUIRERS SHOULD BE ASKING

Welcome to the Age of the Creative Deal

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Creative merger transactions. That is the buzzword for the present.

As I have noted in prior blogs, some folks who do bank acquisitions are singing the blues that there is no activity. Those of us who work exclusively with community banks, however, have pretty full plates with interested parties "buzzing" about combinations of community banks.

While I am a staunch supporter of independent community banks, I also realize that boards have a fiduciary duty to consider alternative opportunities and allocations of capital on a regular basis. This is the basic question of: Do we buy another bank? Do we sell our own? Or do we maintain the status quo and allocate the capital in a different direction?

Creativity now a dealmaking essential

If the board determines to buy another bank or to sell itself or combine with another equally sized or larger-sized bank, then creativity will be the byword.

Many of the banks looking to combine still have some minor amount of impairment in their loan portfolio. That impairment translates into risks for the potential buyer. As we all know, many of the impaired banks that were severely impaired have failed. Many banks that are currently on the market, at least based on the experience presently in our office, are mildly impaired "dirty banks" whose boards have had all the fun they can stand, are generally out of compliance with their regulatory order, and are looking for an exit.

These banks are well beyond trying to find the cheese and are simply interested in getting out of the trap.

Questions buyers should ponder

From a buyer's perspective, however, these deals will not happen unless the buyer is willing to be creative. Consider these questions:

1. How do you deal with the risks in the target's loan portfolio?

2. What do you do with the debt or trust-preferred securities at the holding company level which, if you simply do a straight merger, a buyer assumes or is required to pay off?

3. Will the bank stock lender, to protect its investment and its collateral, be willing to cooperate or discount the note?

4. Will the bank stock lender be willing to purchase some of the impaired assets as a way to protect its own collateral?

5. How is the pricing going to be established with the selling shareholders?

6. Do they get anything upfront, or is this a total earn-out, depending upon the ultimate liquidation value or collectability of the assets?

7. What does it take to get the transaction done, both at the board level and with the shareholders?

8. If the purchasing non-problem community bank holding company is willing to give up some of its stock, how do you value the stock in this type of transaction?

9. As I have heard said in many negotiations, "If you think your impaired bank is worth book value, then my healthy bank must be worth two times book value." Relative values need to be determined.

10. How do you handle employees who are under employment contracts with change in control/parachute payments if the target bank is "impaired" or formally designated a troubled institution by its primary federal regulator?

11. If that is the case, then the regulators get to say whether the parachute payment is paid or not. If it is not going to be

paid, will the deal still go forward, or will the senior officers who are not going to receive their payment do something to scuttle the deal, or simply take off--and impair the bank further?

Lots of considerations in the current acquisition environment, particularly with a mildly impaired target. Creativity is clearly the watchword of the day. Be creative and understand your alternatives, particularly as a buyer.

About the Author

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