Preparing for Bank M&A in a Sluggish Environment

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Abdul R. Mitha

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While bank merger and acquisitions activity in the U.S. is at historic lows — **the slowest pace since 2009** — there are deals getting done. Additionally, banks are positioning themselves for when the market improves.

Until then, the deals that are getting done are in “slow motion” from conception to conclusion. Parties are taking longer to come to pricing terms and buyers are digging deeper into diligence. In some cases, the regulatory approval timeline has increased, particularly if a seller has any “hair” on it or the buyer is “nontraditional,” such as an investor group, fintech or credit union, which can invite increased regulatory scrutiny.

If your institution is looking to participate in today’s M&A market, you should be aware of the increased importance to protect yourself and the transaction during a possibly lengthy process.

Employee Retention

When a deal is announced, the seller’s employees become understandably nervous about their uncertain job future. Longer deal times create greater risk that key employees will leave, damaging the seller’s franchise value. Sellers and buyers should work together to implement strategies like retention bonuses to keep essential talent on board through closing or data conversion. Engaged and motivated employees will contribute to a smooth post-merger integration, better ensuring customer retention at closing.

Termination Fees

Termination fees in bank M&A transactions are payable in rare instances where the seller accepts a superior offer after a deal is announced. A definitive agreement may also provide that liquated damages be paid if a party willfully breaches the definitive agreement. Due to the increased regulatory risk when attempting to partner with nontraditional buyers,

sellers should also consider negotiating a break-up fee if a transaction does not receive regulatory approval or if there are burdensome conditions attached to the approval. While generally not a standard item in bank-to-bank transactions, we have seen sellers successfully negotiate material termination fees with nontraditional buyers.

Transaction Expenses/Data Deconversion Fees

In many transactions, each party is responsible for its own expenses related to the transaction, such as legal, accounting and financial advisor fees. Another common expense is data conversion or deconversion fees, which are charges incurred when switching from the seller's core processing system to the buyer's platform. While closing conditions pertaining to closing equity may have an effect of putting these onto the buyer, if transaction never closes, the seller is typically stuck with these costs. To the extent a seller is responsible to pay these items prior to closing, they should consider negotiating a reimbursement of these expenses if the transaction is terminated.

Deposit Levels/Run-Off

With the tightening of deposits in the banking sector, financial institutions are increasingly fighting to keep and gain deposits. Unsurprisingly, deposits are a key factor in today's M&A environment.

We are seeing more buyers requiring the seller to maintain a minimum deposit level as a condition to closing, as a way to ensure the buyer is "getting what it's paying for." If the deposit level fall below the minimum, the buyer has a right to terminate and walk away from the deal. Longer closing windows create greater risk for deposit run-off between signing and closing, especially in today's hyper-competitive environment. Run-off can occur for many reasons outside of the seller's control, such as the customer's concerns about changes in the buyer's policies and fees, loyalty to local institutions, market competition or a general unfamiliarity with the new institution or buyer. Sellers should keep these factors in mind when negotiating the level of any required deposit minimums; buyers should be aware that this will likely be a sensitive point for sellers.

Transition Matters

While a buyer is prohibited by the regulators from exerting control over the seller before the transaction closes, practically speaking, the parties will begin preparing ahead of time for a smooth operational transition. For example, buyers often will want to speak to employees to assess post-closing employment, install equipment at the seller's branches, train seller's employees on the buyer's systems or enter into data sharing arrangements.

Some sellers have voiced concerns that longer closing time frames give more opportunities for buyers to “lean in” to the selling bank, leading to frustrations. Buyers and sellers should understand that the engagement period may be longer than expected and should be thoughtful on how to approach transition matters, while not causing undue disruption at the seller’s operations.

Even in today’s environment, deals can get done, but parties must understand the elevated risks and plan accordingly.

To read the article on Bank Director’s site, visit: https://www.bankdirector.com/issues/bank-ma/preparing-for-bank-ma-in-a-sluggish-environment/

About the Lawyer

Abdul Mitha is a partner in the financial institutions group at Barack Ferrazzano Kirschbaum & Nagelberg LLP, composed of over 30 lawyers dedicated to representing public and private financial institutions, investors in community banks, fintechs and non-bank financial services companies. Mr. Mitha focuses his practice on capital raising transactions, mergers and acquisitions, securities regulation, fintech agreements and partnerships and general corporate matters.