Bank Acquisitions: An Overview
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Mergers and acquisitions for smaller community banking institutions are heating up! Although there is not much activity happening for the larger banks, there is significant activity happening for community banks with less than $500 million in total assets. While some directors and officers are experienced in acquisition transactions, others have never witnessed the process first hand. These individuals have not seen an acquisition from start to finish and may not know each of the steps that are involved.

A bank acquisition transaction is a multi-step process. The steps are summarized below:

1. Marketing of Selling Institution – A bank acquisition process begins by a bank marketing itself for sale. This marketing process can occur through bankers, outside professionals or via a large-scale marketing process. Although the process for each bank sale is unique, it generally involves the identification of potential acquirors, the execution of confidentiality agreements and the provision of confidential marketing materials that contain detailed information about the seller.

2. Acquisition Analysis – Once an institution has indicated it is available for sale, the next step in the acquisition process is for potential acquirors to complete a preliminary analysis of the acquisition. This will involve "running the numbers" on the potential transaction to determine at what price the transaction will be accretive to earnings per share and otherwise enhance shareholder value. Acquisitions that provide an increase to earnings per share generally warrant further consideration. Acquisitions that are not accretive to earnings per share are generally not a good deal for an acquiror.

3. Offer Analysis – The selling institution's Board of Directors will work with their outside professionals to evaluate each of the offers received. The analysis will focus on the amount of consideration, the type (cash, stock or a mixture) and the various other offer specific details that affect the desirability of the offer. The Board will typically determine which acquiror has presented the best offer and choose to move forward with them.

4. Draft Term Sheet – The fourth step (which oftentimes occurs simultaneously with the offer analysis) is for the acquiror to draft a transaction term sheet that sets forth a summary of each of the material provisions of the transaction. The term sheets are generally three to four pages in length and summarize the material terms of the deal, including the expected structure, price, due diligence requirements, confidentiality requirements and handling of target employees. The proposed term sheet, which is non-binding, is negotiated between the parties and serves as the basis for the Definitive Merger Agreement.

5. Execute Term Sheet – Once the material terms of the transaction have been agreed upon by both the buyer and seller, representatives from both parties will execute the non-binding term sheet. The execution of this term sheet does not contractually obligate either side to complete the transaction. It merely sets forth in writing the

material terms of the transaction and evidences there is a meeting of the minds so that the acquisition may proceed.

6. Due Diligence – Following the execution of a term sheet, the acquiror will perform due diligence on the seller. If the transaction involves the acquiror's stock as consideration, the seller will perform due diligence on the acquiror. The due diligence period presents an opportunity for the acquiror to complete a comprehensive review of the seller's business operations and condition. The due diligence review is typically completed by both the acquiring bank employees and outside professionals, and includes a comprehensive review of the selling bank's loans, business operations, fixed assets, contractual agreements and other material components of its business operations. During due diligence, it is common for the acquiror's accountants to begin to evaluate the projected Fair Value of the target's assets and liabilities, since FASB141R requires the assets and liabilities to be transferred to the acquiror's books at their Fair Value as of the date of acquisition.

   If due diligence reveals no major deficiencies in the seller, the acquisition typically proceeds under the conditions set forth in the term sheet. However, if due diligence uncovers issues or problems, the acquiror has several options, including amending the terms of the deal (such as lowering the purchase price or requiring an additional provision to the target's ALLL) to account for the problems revealed during due diligence or simply walking away from the transaction.

7. Draft Merger Agreement – During due diligence, the acquiror's counsel will draft a Definitive Merger Agreement. This is a lengthy document that acts as the actual contract for purchase. The document includes a number of representations and warranties of both the buyer and seller, conditions to closing, termination provisions and the like. The Merger Agreement will also incorporate any specific requirements the acquiror may have as a result of due diligence.

8. Negotiate Merger Agreement – The Merger Agreement is presented to the selling institution and its counsel by the acquiror's counsel. Seller's counsel will review the proposed Merger Agreement and will undoubtedly request a number of changes to the document. Counsel for the buyer and seller will negotiate these changes and will eventually arrive at an agreement that is acceptable to both parties.

9. Execute Merger Agreement – Once counsel for both the buyer and seller have agreed to the terms of a Merger Agreement, the Agreement is presented to the Boards of Directors for both the buyer and seller for their approval. The Board's receipt of the Agreement is typically accompanied by a detailed analysis of the Agreement provided by each Board's counsel. This assures the Board is fulfilling its fiduciary obligations to its shareholders by fully considering and understanding each of the various components of the Merger Agreement. Assuming both Boards approve the negotiated Merger Agreement, representatives from each party will execute the Agreement. Once executed, the Agreement represents a legally binding contract that binds both parties to the transaction. This is the first time either party is legally bound to the deal.

10. Regulatory Approval Process – Following the execution of the Merger Agreement, the acquiror will draft and submit all required regulatory applications. The appropriate federal or state regulators will then review the application and undoubtedly provide comments and additional questions. The buyer will work with the regulators to resolve any issues and get the transaction approved. The regulatory application approval process typically takes two to four months, but can last longer if more serious issues are present.

11. Shareholder Approval Process – Shortly after all required regulatory applications have been submitted, the next step in the process is to submit the acquisition to the shareholders for their approval. If the transaction is an all-cash transaction, only the seller's shareholders will vote on and approve the transaction. If the deal is structured to include stock consideration, the buyer's shareholders may be required to approve the transaction. It will depend on the number of shares being issued in connection with the transaction and the applicable state law. Shareholder approval process typically involves the distribution of detailed proxy materials that fully explain the material terms of the transaction and an annual or special shareholders meeting.

12. Closing – Following regulatory and shareholder approval and the expiration of any mandatory waiting periods, the acquisition transaction is closed through the filing of the Articles of Merger or other appropriate documents and the exchange of purchase consideration.

A bank acquisition in this environment typically takes six months, but can last longer. The usual suspects for the lengthening of the time period include the uncovering of unusual issues during due diligence and an extended regulatory review process.