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BankNews

MERGERS OF EQUALS

and Other Mistakes

By Shahin Clark

Mergers and acquisitions are highly attractive to banks that seek to expand while reducing overall costs. There are considerable opportunities to save through a reduction in workforce, consolidation of operations and eliminating overlapping or unprofitable branch locations. Other significant costs, such as the core system, can often be cut in half. Although mergers and acquisitions present opportunities to ensure the financial health of banks, they should pay attention to several areas that affect costs and revenue, such as grandfathered accounts, mergers of equals, hidden labor costs and a lack of quality control.

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During a merger or an acquisition, some financial organizations decide to declare certain account types as grandfathered accounts, either contractually or verbally. These accounts stay intact with no changes during the conversion. Going forward, if accounts are in waived status, or are not subject to certain fees because they were established prior to current practices, these accounts can be carried forward with no changes after the merger. However, depending on the number and size of these accounts, the cost to the bank and the loss of revenue can be extensive. Additionally, the bank often ends up with too many account types, forcing personnel to overextend themselves to service these accounts according to different requirements. Many times, the information pertaining to these grandfathered accounts is not readily available to all bank personnel, especially branch staff, making these accounts even more difficult to manage.

When undertaking a merger or acquisition, the mergers of equals process is complex and presents many opportunities for errors. Keeping two equivalent C-level executives for an extended period of time after a merger slows down the decision-making process and adds significantly to overhead costs. These are the highest-paid positions at the bank; hence maintaining this redundancy negatively affects the bottom line. During the merger process, some tough decisions have to be made affecting personnel and department eliminations. With two CEOs, important decisions are not always made in a timely fashion because the executives may have different perspectives.

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Many banks ignore hidden labor costs during mergers. It is very common, especially in smaller community banks, for personnel to perform many tasks outside of deposit or loan operations. Often during a merger, when the most obvious departments are consolidated, only a deep analysis of the tasks performed by bank personnel would reveal other hidden labor costs. The correct process is to identify and consolidate these roles to reduce costs and improve efficiency. For example, four years after a $200 million asset bank was acquired by a $1.1 billion asset bank, management conducted a workflow analysis and discovered that more than $750,000 in unnecessary labor costs was spread throughout various departments of the acquired bank.

Mergers offer a multitude of ways to lose annual revenue, one of which is a lack of quality control during a core conversion. Analysis of a $25 billion asset bank in New York City showed that numerous accounts were not accurately linked to the bank's existing pricing structure during an M&A core conversion. This lack of quality control cost the bank more than $1.5 million in recurring annual revenue. An extensive and systematic analysis of all of the bank's products to see how each was performing ultimately generated $1.5 million of additional revenue.

During the M&A process loan review quality control should be given more attention. To avoid increasing loan loss reserves and writing off loans shortly after the acquisition, bankers should spend enough time on reviewing loan quality and accurately assessing loan deterioration.

Many of these mistakes are avoidable with the correct precautions. Any bank executive who has been involved in the M&A process knows that finishing a successful merger and getting back to regular operations is foremost on everyone's mind. This is understandable, because the process is very time-consuming and requires cohesive interaction among all levels of expertise. In order for banks to experience the greatest success, bankers ought to take the time to analyze each of these facets of the merger and acquisition process. BN

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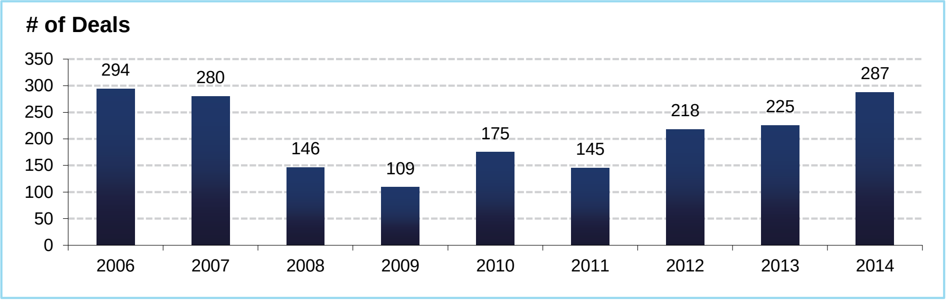
MEDIAN M&A MARKET STATISTICS

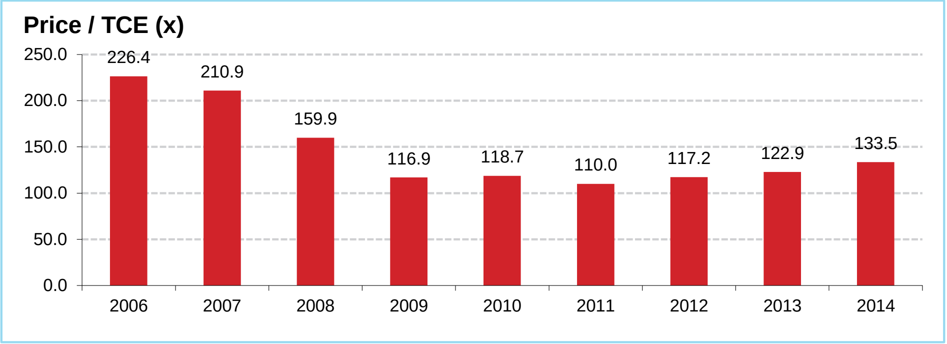
As of December 31, 2014

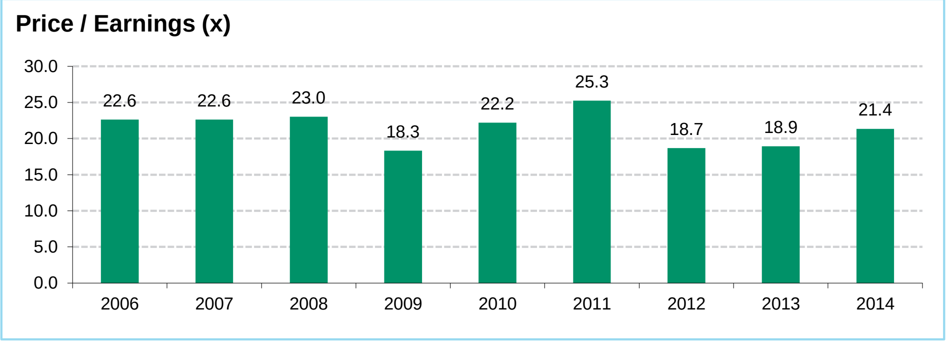
Prepared by The Capital Corporation, LLC

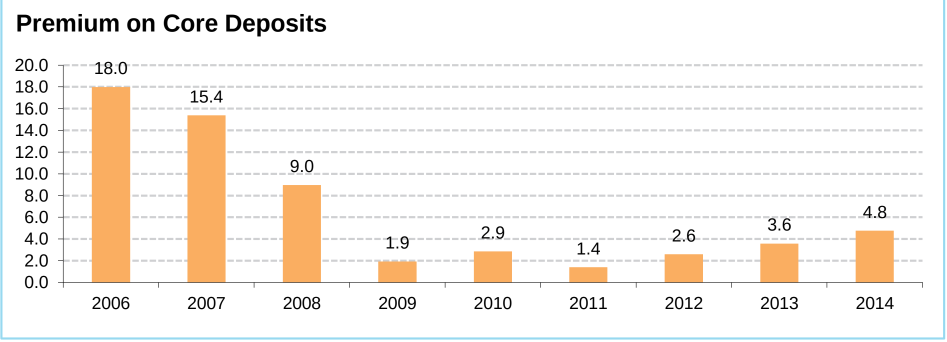
All data is for based upon nationwide statistics

Target Assets Range Min ($M)	Target Assets Range Max ($M)	# of Deals	Price/ TCE (x)	Price/ Earnings (x)	Prem on Core Deposits
Below	**100**	95	113.63	26.59	1.52
100	**250**	82	117.20	20.64	1.95
250	**500**	48	141.94	22.36	5.89
500	**1,000**	36	151.51	19.02	7.51
Above	**1,000**	26	172.06	21.82	10.32









These statistics include both C Corp and S Corp banks with no adjustment for taxes to the Price to Earnings Multiple

Provided by SNL Financial