

Successful Business Combinations

Mergers, Clusters & Acquisitions

Joe Vincent Management Seminar
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OAK & ASSOCIATES

Bill Schoeffler, CIC
PO Box 2047
Glen Ellen, CA 95442
Phone: (707) 935-6565
bill@oakandassociates.com

**Mergers, Clusters & Acquisitions
Seminar Outline**

A Definitions

Mergers: Two or more firms that join together to become one agency.

Acquisition: One firm buys another agency. The seller usually loses its identity.

Clusters: Two or more firms that share something – almost always markets as a minimum. The firms retain some level of autonomy.

B When you need to do something

- Pending retirement or other major life changes
- Major problems with carriers and/or company plants
- Major staffing issues
- Major management issues

Goal - Make business moves when in a position of strength not weakness

C Good reasons to consider a merger, acquisition or cluster

- Increase clout with carriers
- Expand sales
- Add new locations
- Add management depth
- Share common vision
- Reduce expenses
- Perpetuation planning
- Lower risk in business

D Single reasons never to do a MAC

- Good friend
- Family obligations

E Does a Business Combination make sense for you?

1 Step One Know your own Agency

- What is your goal?
- What is your timeframe?
- What are your resources?
- What are your strengths & weaknesses?

2 Step Two What is the rest of the world doing that is beneficial?

- What markets can you use?
- What market relationship do you need?

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- What client services are available
- What type of staffing do other firms have?
- What specialty services do other firms offer?
- What is the productivity or profitability of other firms?

3 Step Three Assess if agency can meet goals through internal growth/change

- Do you have the time?
- Do you have the skills & talent?
- Do you have the capital?

4 Step Four Review your options

- Which option will let you reach your goal quickest with the smoothest transition in the most cost effective manner?
- List merger options, cluster options, acquisition options and selling business options.

F Compatibility

- Philosophy
- Book of Business
- Goals
- Financial Approach
- Growth Potential
- Improved Clout and Market Share
- Contingencies
- Management and Operations
- Comparing Strengths and Weaknesses

G Defining the Ideal Candidates

- Adding Agency Resources
- Blending Operational Structures
- Matching Market Resources
- Compatible Profiles of the Book of Businesses
- Similar Financial Profiles
- Common Agency Goals and Expectations
- Contrasting Strengths and Weaknesses

H How to attract candidates

- Networking
- Company Reps
- Consultants
- Advertising
- Mailing

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I Review process

- 1 Information Exchange
 - Confidentiality Agreements
 - What Each Party Needs to Know About Each Other
 - Meeting of the Minds
 - Wish Lists
 - Satisfying Mutual Needs
 - Dealing With Problems
 - Family Issues
 - Perpetuation Issues
 - Establishing a Time Frame

- 2 Analyzing the Deal
 - Compatibility Review
 - Financial Projections
 - Carrier Considerations
 - Management and Operations

J Agency Value

The value for most insurance agencies is based primarily on earning capacity

1. COMPONENTS OF VALUE

- A. Sustainable earnings
 - The potential earnings stream that the firm can sustain over a period of time – pro forma profits

- B. Risk
 - The likelihood that the earnings stream will continue in the future – strengths and weaknesses of the agency, the book of business and management

- C. Tangible Net Worth (Equity)
 - What is left in the balance sheet after all doubtful and intangible items have been removed and remaining assets are used to satisfy actual and contingent liabilities.

K Creating or Analyzing the Offer

- ❖ Agency Value
- ❖ Terms of the Deal
- ❖ Equity in the New Entity
- ❖ Defining Management Roles
- ❖ Owner Compensation
- ❖ Streamlining the Operation of the New Entity
- ❖ Agency Name
- ❖ Letter of Intent

L Closing the Deal

- ❖ Counter Offers and Negotiations
- ❖ Terms and Payments
- ❖ The Use of Attorneys and CPAs
 - ❖ Legal Documents
 - ❖ Tax Consequences
- ❖ Due Diligence
- ❖ The Closing

FINAL RECOMMENDATION

- ◆ Have a honeymoon period. Don't jump into anything.
- ◆ Have the appropriate documentation in place, as well as a way to terminate the relationship, if necessary.
- ◆ Are you missing any provisions in the deal because the appropriate amount of time to scrutinize the deal has not been taken?
- ◆ There are few, if any, true reasons to rush, so examine why either party feels compelled to rush into things. Is one of you short of cash and desperate to lower/consolidate expenses? Is there some fundamental problem with the business?
- ◆ Often, the principals are so happy with each other that they can't imagine anything going wrong -- beware of "being in love."
- ◆ Ask the tough questions
 1. Compensation
 2. Management Roles
 3. Business Philosophy
- ◆ Do your proper due diligence. Do you really know the other party? Check references. Find out problems before it is too late.

Exhibits

CLUSTERS

What clusters can share

- Markets
- Office
- Labor
- Purchasing power – share expenses
- Advertising & Marketing
- Specialized client services
- Management

Possible benefits of clusters

- More market clout
- More contingents
- Cost savings - more profits
- Added staff and support
- Management depth
- More client services
- Business succession
- Bigger appearance in marketplace

Types of Clusters

- Market based clusters
- Blended agencies
- Franchises
- Regional or National Groups

Clusters

- National and Regional Players
 - Iroquois Group
 - SIAA
 - Group Advantage
 - ISU - Franchises
- Texas and Local Clusters

What Insurance Companies Think of Clusters

- Usually cautious
- Less control of risks that get written
- Clusters might cause risks to get written in unwanted areas
- Benefit from consolidation of volume
- Might pay more in contingents

Comparison Matrix

Criteria	Merge	Acquire	Cluster	Sell
Markets				
Expenses				
Profits				
Improved client services				
Client relations/perception				
Management Support				
New sales production				
Sales Support				
Staff support				
Agency Identification				
Geographical Influence				
Automation				
Ease of establishing				
Market place				
Cost to establish				
Commitment				
Owner Personalities				

Key Areas of Each Agency to Explore

1. Agency Background

- i. History of the firm
- ii. Type of Business: Sole Proprietor, “S” or “C” Corp., Etc.
 - The type of business will have a big impact on transactions and estate planning
- iii. Owners
 - What is the status of the owners – health, retirement plans, book of business handled, role in management
 - What are the blocks of ownership – is there a majority owner?

2. Strengths and Weaknesses, Goals & Expectations

- i. Agency’s reputation
 - How do clients and companies perceive the firm?
- ii. Is focus on sales or service?
 - Is the focus to keep existing clients or sell new business?
- iii. Is there a perpetuation plan in place?
 - What would happen if the principals die or become disabled?
 - Is there life insurance?
 - Is there a contingent buy/sell with another firm?
- iv. Is the staffing adequate?
- v. What is the producer/client relationship?
 - Do the clients have an allegiance to the producer?
 - Does the producer over-serve the book of business?
- vi. How well is the firm managed?
 - Are any owners full time managers? Are there supervisors or middle managers that handle day-to-day issues?
 - Do the owners have a vision for the firm?
- vii. Review goals, projections and expectations with owners and managers
 - What internal changes are anticipated?
 - What external factors need to be considered?
 - How will sales go in near future?
 - What will happen with carriers?
 - What changes to the financial situation will happen?
 - Are there any staffing changes anticipated?

3. Inventory of Agency Resources

- i. Human Resources – List Producers, Service Staff, Administration
 - What is the experience level?
 - Is there under or over staffing?
 - Do the producers have contracts?

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- ii. Office Facilities
 - Are they rented or owned?
- iii. Office Equipment
 - Computers – How many and how old?
 - Agency Management System – is one used, if so how much?
 - Other office equipment, such as fax machines and printers

4. Operational Structure

- i. Middle Management
- ii. Service Structure
 - Producer Units
 - Alphabetical
 - Claims and Marketing

5. Market Resources

- i. Volume by company
 - How is the volume spread?
 - Any dependency on one or two markets?
 - Volume in MGAs or substandard markets?
- ii. Company relationship
 - Special relationships
- iii. Portability of book of business
 - Can the book be moved to a new company?

6. Profile of the Book of Business

- i. Volume by line of business
 - Is there a mix of business (CL, PL, Benefits, etc.) or is it niched?
 - Does the mix of business make sense for this agency?
- ii. Number of accounts and policies
 - What is the number of policies per account?
 - What is the average size of account?
- iii. Retention rates
 - What percent of accounts renew each year?
 - 80% to 95% for standard business
 - 50% to 65% for substandard
- iv. List of largest accounts
 - What is the dependency on large accounts?

Association Business Plan
Components of the Plan

Mission statement

Background

- ◆ Provide a brief history of each firm
- ◆ Brief description of efforts to put cluster together

Objectives of the cluster

- ◆ List several major objectives
- ◆ Talk about future of association and merger
- ◆ Buy/Sell contingent agreement

Book of Business Description

- ◆ Provide short narrative on each agency's book of business
- ◆ Describe the territory of the associations business
- ◆ Show historical table of premium and commission for each agency
- ◆ Show table of current breakdown by line of business of the association's book
- ◆ Provide table of concentration by class of business for each agency and a table of the combined book of business
- ◆ Provide table of largest accounts of each agency
- ◆ Provide list of producers and the size of book they are responsible for

Marketing and Sales Strategy

- ◆ Brief outline of marketing and sales strategy, which includes:
 1. Sales approach
 2. Target marketing
 3. Future opportunities and goals
 4. Approach of marketing & advertising (include the identity of advertising)

Organization

- ◆ Brief description of management of each agency and of the association
- ◆ Employee rosters of each agency with job titles and responsibility
- ◆ Employment policies (you may want to state you will follow common employee manual) include hiring and training procedures
- ◆ List of common association employees (e.g. accounting, marketing, etc.)
- ◆ Any unique servicing of clients because of association
- ◆ Automation
- ◆ Productivity of each agency and of association

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Accounting & Financials

- ◆ Describe how association will handle accounting (trust account, manager, etc.)
- ◆ Provide financials of each company and pro forma of association
- ◆ Projections
- ◆ Capital position of association

General Association Considerations

- ◆ Who will hold company contracts
- ◆ Responsibility of premium collection and trust account
- ◆ Overview of letter of intent or contract
- ◆ Association's management control
- ◆ Binding authority
- ◆ Claims/draft authority
- ◆ Admission of new members
- ◆ Withdrawal from cluster
- ◆ Non compete clauses
- ◆ Who do the producers represent, the association member or the association?
- ◆ E&O Issue

CONFIDENTIALITY AGREEMENT

The parties are engaged in negotiations on a possible merger or other business arrangement, and for this purpose they are exchanging material on their businesses and clients ("the material").

- Both parties agree that the material on the business and clients of the other is to be treated as a trade secret. Each party may be given access to certain information not generally known to the public or to the insurance industry and is to be considered proprietary to the originating party.
- The material is to be used only for evaluating the other's business, and for no other purpose. Under no circumstances shall the material be used by the receiving party for competitive purposes. Any other use of such proprietary information by, or its disclosure to, any person or organization other than the receiving party and its employees would be highly detrimental and damaging to the originating party.
- The material shall be kept secret, and shall not be made available to any third party. The recipients may make the material available to their employees, consultants, accountants, and attorneys for evaluation purposes only, provided that they tell the recipient that the material is a trade secret and to be kept confidential, and provided that each recipient signs a copy of this agreement.
- Upon conclusion of negotiations, all copies of the material shall be returned to the other party upon request.

All persons subject to this Confidentiality Agreement shall follow all reasonable procedures to maintain the confidentiality of the materials subject to this Confidentiality Agreement.

Signed _____

Signed _____

Signed _____

Signed _____

Agency 1

Agency 2

Date _____

Date _____



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Consulting ♦ Valuations ♦ Seminars

Meeting the Needs

Exceeding the Expectations

Firms today are faced with a continually and rapidly changing business environment. Because of the effort to just keep up, owners and managers often find it difficult to be proactive and have an organized approach to managing the day-to-day activities, determining the strategic direction and planning the growth and perpetuation of the firm.

Also, when a unique opportunity presents itself, such as a merger or acquisition, owners and managers are often not aware of how to analyze or approach the situation to maximize benefits and avoid the common pitfalls.

Business and management consultants can assist owners and managers in focusing on what is most important and bring order to chaos. An outside opinion can open a new perspective on old problems. Also, an experienced consultant can save time and money when looking at a business combination, sale or merger. A third party can ask the tough questions and get to the heart of the issues with a dispassionate approach.

Why We Are Unique

Oak & Associates' consultants offer a wide range of consulting services to firms across the country at competitive prices. Our philosophy is to customize our consulting or valuation work to meet the unique needs, desires and operations of our clients. Every business interest and every valuation assignment is unique, presenting its own set of challenges and demands.

No one method or set of methods is right for all situations. It takes a qualified, experienced expert to interpret the information correctly and arrive at correct and defensible results.

Mission Statement

Oak & Associates is a highly responsive, hands on, personalized consulting firm. We are in business to assist our clients in improving their value over time and in consummating effective business combinations, when desired.

Oak & Associates

P.O. Box 2047 ♦ Glen Ellen, CA 95442 ♦ Phone (707) 935-6565 ♦ Fax (707) 940-4240
www.oakandassociates.com ♦ email info@oakandassociates.com



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Services Offered

Oak & Associates provides a variety of consulting and valuations services, as well as training programs & seminars.

Consulting and Company Strategic Work

We provide custom designed consulting services to help streamline business operations and improve productivity and profitability through these services:

- Mergers & Acquisitions
- Compatibility Analysis
- Management & Organization Studies
- Product Analysis
- Owner & Sales Compensation Plans
- Financial Analysis
- Management and Executive Coaching
- Evaluation of Distribution Systems
- Annual Business Planning Meetings/Retreat
- Systems & Procedures Review
- Sales and Marketing Planning
- Productivity Studies
- Strategic Alliances
- Determination of Target Markets
- Streamlining Annual Game Plans
- Team Building

Seminars and Workshops

We have a variety of seminars or workshops available or can custom design a program to fit any length meeting on a variety of management, sales or financial subjects.

Business Valuations

We will establish a fair market value of a firm and provide consulting work for a variety of needs:

- Merger, Acquisition or Sale
- Changes to Business Form
- Credit Establishment
- Internal Sale or Other Usage
- ESOP
- Divorce
- Perpetuation Planning

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