



Bank Strategy Briefing

Ideas and analysis for community bank executives

Non-Bank Acquisition Strategies

With so much attention on organic growth and whole-bank M&A activity, one often overlooked strategy for community banks is the pursuit of new or “niche” business lines through non-bank acquisitions. Examples include trust and investment services, independent mortgage operations, insurance agencies, consulting services and equipment leasing. We have long been advocates of this non-bank acquisition strategy for several reasons.

For starters, these transactions tend to be less complex and risky than whole-bank acquisitions, with fewer regulatory and operational hurdles. In addition, they can create significant shareholder value by (i) providing a platform to drive additional top-line revenue (often in the form of non-interest income) and (ii) reducing risk by diversifying the bank’s revenue streams. Anecdotally, we have observed for many years that community banks producing truly superior returns for their shareholders tend to have invested in and developed one or more niche business lines at some point in their history, often via acquisition.



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So what are some key considerations for boards and executive management teams to consider with respect to non-bank acquisitions?

- **Permissible Activity / Regulatory Application.** Prior to pursuing any new business line or acquisition, confirm with your legal counsel and regulators that the activity is permissible. Regulatory applications may be necessary.
- **Structure.** These acquisitions are most often structured as asset purchases rather than true “mergers,” allowing the acquiring bank to leave certain undesirable assets or liabilities behind. Sometimes acquiring banks prefer to use an operating subsidiary to acquire the target. This can have certain advantages (such as isolating any liability inherent in the target’s business) but is not always practical or necessary.
- **Sourcing Opportunities.** Often targets are identified organically based on local ties or existing relationships. For example, we have seen multiple situations where the principal of a local independent investment advisor, title company, etc., with an existing relationship with the bank becomes interested in formally joining forces. Often the profile of such a candidate is someone who is ~10 years from retirement and interested in switching from a commission-heavy compensation structure to a more predictable one. Be on the lookout in your market for these opportunities.
- **Pricing is Difficult.** Targets are commonly “balance sheet light,” meaning that their value is primarily derived through their existing pipeline of new or recurring revenue. Determining a fair purchase price can therefore be challenging, but there are several ways to arrive at a mutually agreeable pricing mechanism (e.g. earn-outs).
- **Employment Agreements are Paramount.** As with many acquisitions, the value of the target is largely tied to its people. Therefore, employment agreements, including non-compete and non-solicitation commitments, are often critical aspects of the negotiation. Be prepared to come to terms on these matters early in discussions to avoid unnecessary roadblocks later on.

We strongly believe that non-bank acquisitions should be “on the table” as a possible option for many community banks wishing to maintain their independence for the foreseeable future, and we encourage boards and executive management teams to consider whether such a strategy may provide value for shareholders.

Bank Strategy Briefing is prepared by the Banking & Financial Institutions Practice Group at Godfrey & Kahn, S.C., Milwaukee, Wisconsin, as a service to the community banking industry. It features commentary focusing on strategic business and legal issues relevant to community banks. Each written edition contains 500 words or less and no more than 2 editions are published per month. Information found in Bank Strategy Briefing is for educational and informational purposes only and is not to be construed or relied upon as legal advice.