

Creative Deal Structuring when Stock is Currency

Co-Authored by Phil Trem (VP)
and Dan Skowronski (SVP)

As the soft market continues within the insurance industry, organic growth has been difficult to achieve. Many agencies, including independently owned, private equity backed and public brokers rely on acquisitions to help achieve their growth expectations, both quarterly and annually. Buyers have often used their stock as one form of currency in transactions, but public brokers have an advantage in doing so since their stock is readily tradable. While many sellers prefer not to take buyer stock, the near-liquid form of publicly traded stock is more palatable than stock which is not readily tradable or has restrictions.

The utilization of a contractual agreement known as a collar can be a useful tool when dealing with a buyer who is using publicly traded equities as consideration within a transaction. A collar can customize a transaction to limit buyer and seller risk due to fluctuations in the buyer's per-share price as determined by the public exchange on which it trades.

There are two main types of collars: the fixed exchange ratio collar (not addressed in this article as it is relevant to transactions where both the buyer and seller are publicly-traded companies) and the fixed-price collar (also known as a fixed payment or value collar). In a fixed-price collar, the sale price is fixed within the boundaries established for the collar. In this way, the number of shares of the buyer's stock provided in the deal is known in advance of a deal closing. The collar helps alleviate purchase price uncertainty for both sides from short-term fluctuations in the buyer's stock price.

For purposes of an example, let's assume that a buyer and seller have agreed to use buyer stock to satisfy \$5,000,000 of deal value. Furthermore, while the buyer's stock is currently trading at \$10.00 a share, it has traded in a range of \$9.00 to \$11.00 per share over the past twelve months, but over the past month has been trading in a much tighter range of around \$10 per share. In this example, a collar of between \$9.75 and \$10.25 per share might be established, indicating that as long as the per-share value of the stock on the date of close is between these amounts, the buyer agrees to deliver 500,000 shares of stock. However, should the per-share price of the buyer's stock decrease or increase outside of this pre-determined range, the number of shares of buyer stock is renegotiated.

Value Per Share at Close	Intended Deal Value	Fixed Value Per Share	# of Buyer Shares Delivered at Close	Market Value of Shares at Close	Protection
9.50					
9.75	5,000,000	10.00	500,000	4,875,000	Buyer
10.00	5,000,000	10.00	500,000	5,000,000	Even
10.25	5,000,000	10.00	500,000	5,125,000	Seller
10.50					

Had the collars not been used and if the price of buyer stock at closing was \$9.75 a share, the buyer would have had to increase the number of shares in the deal to 512,821, in order to maintain a deal value of \$5 million to the seller. To the buyer, increasing the number of shares due to a short-term decline in stock price equates to overpayment in their eyes. If the price of buyer stock at closing was \$10.25 per share, the buyer would have decreased the number of shares in the deal to 487,805, which would not be viewed positively by the sellers as they are now receiving less shares due to what may be a short-term increase in the per-share price.

Collars can be a valuable tool to allow equities to be utilized as currency while avoiding huge swings in purchase price (up or down). The use of a collar can protect the buyer from overpaying in the event of a short-term decline in their own stock price and protect the seller from receiving less value due to a short-term increase in the price of the buyer's stock.

MarshBerry M&A Advisory Services

Deal Strategy

1. Acquisition Planning
2. Deal Return Modeling
3. Strategic Options Analysis
4. Alternative Buyer Comparison

Deal Preparation

1. Sale Preparation Management
2. Offering Memorandum Development
3. Strategic Pitch Book Design
4. Candidate Profile Creation

Deal Representation

1. Buy Side Representation
2. Sell Side Representation
3. Letter of Intent Development / Negotiation
4. Creative Deal Structure Alternatives

Deal Analysis

1. Agency Fair Market Valuation
2. Market Comparables / Deal Benchmarking
3. After-Tax Return Optimization
4. IRR, ROI and EPS Analysis

Deal Execution

1. Diagnostic and Confirmatory Due Diligence
2. Intangible Asset Allocation - GAAP Reporting
3. Fairness Opinion
4. Definitive Agreement Best Terms / Conditions

Post-Deal Management

1. Post-Closing Integration
2. Goodwill Impairment Testing
3. Peer-to-Peer CEO Exchange
4. Earn-Out Maximum Consultation

SNL Financial M&A Advisor Rankings

Insurance Broker Merger & Acquisition Deals
1997-2009

Rank	Firm	1997 - 2009 # of Deals	2009 # of Deals
1	Marsh Berry & Co. Inc.*	275	23
2	Hales & Co. Inc.	123	14
3	Reagan Consulting Inc.	113	7
4	Mystic Capital Advisors Group, LLC	95	11
5	Macquarie Capital Advisors Group, LLC	44	8
6	Bank of America Merrill Lynch	22	2
7	B.H. Burke & Co., Inc.	16	0
7	Harbor Capital Advisors, Inc.	16	0
9	Keefe Bruyette & Woods, Inc.	15	0
9	Sica Consultants, Inc.	15	3
11	North Bridge Advisors, Inc.	13	0
11	Sandler O'Neill & Partners, L.P.	13	1
13	Philo Smith & Co.	10	0
14	Credit Suisse (USA) Inc.	9	0
15	Business Management Group, Inc.	8	0
15	Curtis Financial Group, LLC	8	0
15	J.P. Morgan Securities, Inc.	8	0
18	Boenning & Scattergood, Inc.	7	0
18	Gill and Roeser Holdings, Inc.	7	0
18	Nexus Group, Inc.	7	0
21	2nd Generation Capital Corporation	6	0
21	Garland McPherson & Associates, Inc.	6	0
21	Goldman, Sachs & Co.	6	0
24	Lazard Freres & Co. LLC	5	0
24	Wells Fargo Securities, LLC	5	0
26	Austin Associates, LLC	4	0
26	Nomura Securities International, Inc.	4	0
26	Piper Jaffray & Co.	4	1
26	Russell Miller Corporate Finance, Inc.	4	0
26	UBS Investment Bank	4	0

All States // Completed Transactions
Whole deals as reported by SNL Financial, January 15, 2010

* MarshBerry has closed 28% of total deal flow since 1997

MarshBerry's clients are committed to realizing their fullest potential with respect to growth, profit, survival and shareholder value. Our agent, broker, bank and carrier clientele engage us to achieve their goals within the retail and wholesale channels of the insurance distribution system. Our unparalleled industry-specific services include consulting, performance benchmarking, peer-to-peer exchange networks, merger and acquisition intermediation and producer recruiting.