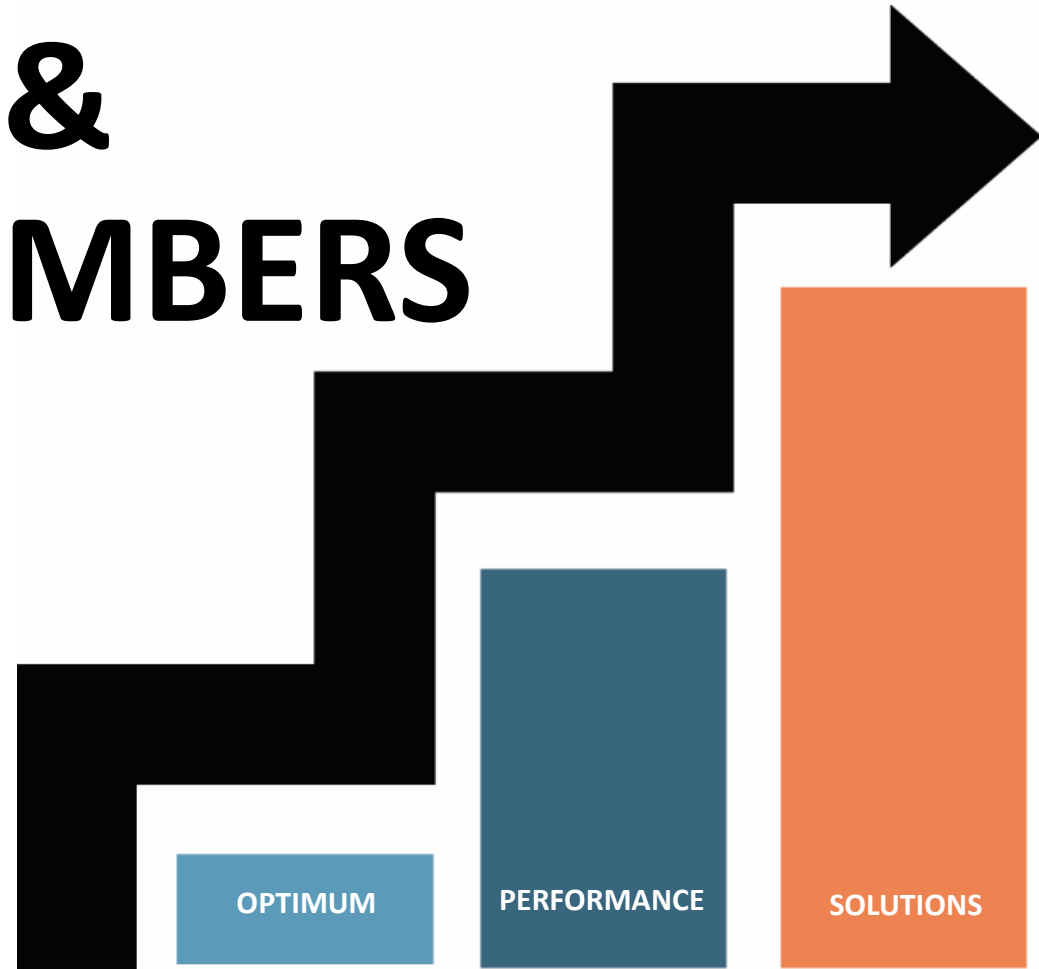


ACQUISITIONS and PERPETUATION for NETWORKS & AGENCY MEMBERS

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Goals of a Network



- 1. Retain and grow existing members**
- 2. Have members write profitable business via network carrier appointments**
- 3. Add members**
- 4. Provide members value services beyond market access**

Successful Networks



Help members remain independent

Educate members regarding acquisitions and perpetuation:

Identify & evaluate good buyers

Provide tools & knowledge

Financing sources

Enable acquisition opportunities to grow an agency's book


Facilitate perpetuation within network membership

Identify members who need to perpetuate

Provide resources and education

Expand value to its members

By the Numbers

- 
- 50%+** Amount of 2016 announced deals that were private equity deals.
 - 78%** Percent of largest acquirers that are private equity backed (five of which did not exist ten years ago)
 - 21%** Amount of 2016 announced deals that were by privately held brokers
 - 53.3** Weighted Average Age of Agency Owners (in years)
 - 25%** Percent of agency owners over 60
 - 4,000** Approximate number of new agencies established over the last five years

Networks should support their members doing acquisitions as well as perpetuating internally or risk a shrinking membership.

Acquisition Process Missteps



1. **Valuation: Buyer talks price before fully understanding the agency & cash flow**
2. **Poor Letter of Intent and ambiguous deal terms**
3. **Lack of Due Diligence expertise**
4. **Not understanding Tax Considerations**

Networks can and should facilitate education of Buyers & Sellers

Acquisition Process



- 1. Identify potential sellers**
- 2. Sign non-disclosure agreement**
- 3. Gather Information to evaluate**
- 4. Prepare Letter of Intent**
 - Terms?**
 - Earnest money?**
 - Carrier approval?**
 - “No shop?”**

Sourcing an Acquisition Candidate



- Other network members
- Friends
- Associations
- Vendors / Companies
- Advertise
- Consultants / Brokers

Friend	26.2%
Carrier referral	25.4%
Seller called Buyer or advertised to sell	23.0%
Buyer called Seller or advertised to buy	12.7%
Industry consultant / broker	5.6%
Other	16.7%

Network Members Competitiveness



1. **Difference in commission rates between the network commission rate may be greater than the seller's commission rate.**
2. **Additional carrier premium – How will it impact any potential contingency bonus?**
3. **Loss Ratio of Seller – Will this help / hurt the contingency bonus received by the network and members?**

Someone should help the buyer / seller set realistic expectations. Is this a role the network can / should play? Is there potential liability for the network by getting too involved in a transaction?

Buyer vs. Seller



Someone needs to help the buyer / seller set realistic expectations.
Is this a role the network can / should plan?

BUYER WANTS...	SELLER WANTS...
Lower price	Higher price
More dollars to ordinary expense (Faster Depreciation)	More dollars to capital gains (Lower tax bracket)
Retention Clause	No Retention Clause
Payments over time	Cash up front
No Collateral	Collateral
To buy just the assets	To sell the corporation (if C corp)

Agency Value Factors



- 1. Retention ratio**
- 2. Profitability**
- 3. Company markets**
- 4. Quality of personnel**
- 5. Public image**
- 6. Accounts receivable**
- 7. Producer compensation agreement structure**
- 8. Average commissions**
- 9. Errors and omission experience**
- 10. Productivity of employees**

Buyer's Cash Flow




Most agency owners want to buy an agency / book of business. But can the Buyer afford to pay for the agency?

Not willing to pay a fair price means the buyer will be unsuccessful. Overpaying for an agency can result in cash flow problems.

Buyer's typically do a cash flow but fail to take into consideration the tax aspects.

Just because there is an after tax profit doesn't mean there is a positive cash flow.

Funding Options

- 
1. Seller holds note
 2. Conventional Loans
 3. SBA Guaranteed Loans

Issues to Consider



1. **Payment schedule - Price vs. Time**
2. **Calculation for retention of business**
3. **Non-compete agreement & non-piracy agreements – This is critically important to both the buyer as well as the network.**
4. **Benefits of a negotiator – Shouldn't be someone associated with the network as it could result in potential liability to the network.**
5. **Remove personalities from the negotiations**
6. **Develop a checklist of issues**
7. **Develop best case and worst `case scenarios and stick by them.**
8. **Keep notes**

Stock vs. Asset



1. If a Stock Deal, what does the network/member agreement say about the new shareholder being a member.
2. If an Asset Deal, is the network/membership agreement assignable?
3. What are the steps involved in retaining the member?
4. Should the network make payments directly to the seller by deducting it from commissions that should be paid to the new owner?

Stock	11.5%
Asset	88.5%

Shareholders' Agreement



Need an agreement addressing the relevant issues.

If no agreement, potential for lawsuits increases and a network could be dragged into court.

Networks should encourage multiple shareholder agencies to have a strong agreement.

Shareholders' Agreement



Do you have a Shareholder's Agreement?

Yes	73.4%
No	26.2%

If yes, with whom?

Existing partner(s)	75.0%
Existing employee(s)	9.1%
Owners of another agency	4.5%
Family member	6.8%
Other	4.5%

What does the Shareholders' Agreement address?


Death	98.9%
Disability	77.0%
Retirement	75.9%
Involuntary termination	54.0%
Involuntary conversion	37.9%

Life Insurance




Failure to have adequate life insurance and/or payment terms written into the agreement could result in a forced sale of the agency and the potential loss of a network member.

Shareholder's Agreement Checklist

- 
1. Do you have a buy-sell agreement?
 2. When was it reviewed?
 3. Does it address all possible changes of ownership?
 4. Is disability clearly defined?
 5. Is valuation of the business clearly defined?
 6. Are terms and methods of payment defined?
 7. Are interest provisions within IRS guidelines?
 8. Are security provisions included? (personal indemnity)
 9. Restrictive covenants - non piracy?
 10. Injunctive relief for violations?
 11. Is normal retirement defined?
 12. Is sale mandatory on employment termination?
 13. Will change in the agreement require a 51% vote of shares or something greater?
 14. Are all new partners / shareholders required to be a party to the agreement?
 10. Injunctive relief for violations?
 11. Is normal retirement defined?
 12. Is sale mandatory on employment termination?
 13. Will change in the agreement require a 51% vote of shares or something greater?
 14. Are all new partners / shareholders required to be a party to the agreement?

Agency Perpetuation Considerations



Do they have a written perpetuation plan?

Size of Business (Income)	Yes (%)
All Businesses	33%
Less than \$500,000	33%
\$500,001 - \$1,000,000	20%
\$1,000,001 - \$2,000,000	34%
\$2,000,000 - \$5,000,000	53%
Greater than \$5 million	56%

At what age do they plan to retire?

Age	%
55 or less	2.7%
56 - 60	7.0%
61 - 65	21.7%
66 - 70	43.6%
Over 70	17.3%
At death - Never retire	7.6%

Agent's Personal Objectives



1. Current & future financial needs
2. Ability to assume risk
3. Long & short range goals & desires.
4. Physical health & family health.
5. Spouse's goals & desires.

Networks need to be proactive in helping members address these issues.

By understanding members objectives, a network can better forecast its own membership numbers and income.

Healthy Agency = Good Price



1. What is the current cash position of the business? – If the buyer fails to pay the seller, the network could lose a member.
2. How stable & predictable is the income stream?
3. How strong and predictable carriers? – Shouldn't be an issue for network members and something networks should emphasize when recruiting / retaining members.
4. How stable and proficient is your operational staff?
5. Is there truly have a future "owner" on staff? – Internal perpetuation is better than external perpetuation for networks. Are networks providing support for training future owners ?
6. What is the probable retention rate of your client base?

Five Methods of Perpetuation



- A. External Sale – To another network member? If not, what are the chances of the network adding the buyer as a member?**
- B. Internal Sale – Does the network / member agreement automatically allow the buyer to participate in the network?**
- C. Merger - What if the merger partner isn't a member of the network?**
- D. Cluster – Should the network (or its member(s) be a buyer of last resort in the event of an unexpected death?**
- E. Run it into the ground – Not a good option from the networks perspective.**

Selling an Agency



Many agency owners feel they can sell their agency themselves, yet they hire a realtor to sell their house.

Networks should encourage their members to utilize industry professionals that understand all the facets of buying / selling an agency.

Networks can be a resource to help sellers find buyers (preferably within the network).

A Program for Your Members



Create a proactive program to:

1. help educate your members
2. identify ready buyers and sellers
3. provide the tools needed for members & networks to reach mutual goals.

Survey Your membership - Identify buyers and potential sellers and organize by

1. Geography
2. Size
3. Timeline to retire
4. Book profile
5. Perpetuation plan (Y/N)

Build an education platform with content on:

1. Buying
2. Selling
3. Perpetuation Planning

Provide strategic partnerships:

1. Financing
2. M&A/Perpetuation Consulting
3. Legal
4. Accounting

Conclusion



The success of a network is directly linked to the success of its members.

Networks are in a unique position to assist / advise its members in the area of agency perpetuation, but should be careful how involved the network becomes.

If you don't focus on maximizing the value of your agency or network, you will end up working harder and earning less.

Definition of Insanity – Doing the same thing over and over again and expecting different results.