Which questions to ask,
pitfalls to avoid, and how to
successfully close the deal.

SCOTT D. TIETZ, CLU

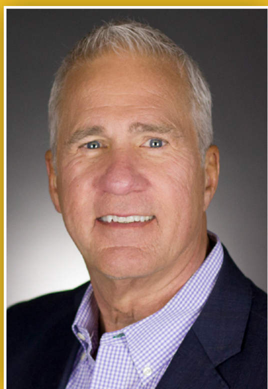
©Copyright 2019 Partners Advantage - A Gallagher Company. All rights reserved.

The Ultimate Guide to Buying and Selling Insurance Agencies

Which questions to ask, pitfalls to avoid, and how to successfully close the deal.

SCOTT D. TIETZ, CLU

This communication is for educational purposes only and does not represent the opinions of the company that currently employs the author. You should not treat any opinion expressed by the author as a specific inducement to make a particular investment or follow a specific strategy, but only as an individual expression of his opinions and experiences. Business owners should consult their individual tax and legal counsel prior to entering into a business transaction.



About the Author

Scott D. Tietz, CLU, is the Area Chairman of Partners Advantage Insurance Services – A Gallagher Company, an industry leader in the life and fixed-indexed annuity marketplace.

Scott joined the insurance industry in 1982 and opened Partners Advantage in 1993. He has more than 30 years of industry experience, specifically in buying, selling, and merging insurance agencies for profit. He has led 11 mergers and acquisitions for Partners Advantage.

Prior to the formation of Partners Advantage, Scott worked as an agent, sales manager, home office regional executive, and general manager for a career agency distribution company.

Dedication

I've learned that life doesn't stop while you strive to grow your business and there have been many things happening over the years in my personal life as I ran my business, like my marriage to Susan — 33 years strong. This is by far the best deal I've ever closed! My son Zach is a cancer survivor married to his better half, Chelsea. My daughter Madison is soon to be married to her perfect complement, Jon. I turned 60 years old (blows my mind even writing a number that high) and still have unwavering enthusiasm for guiding agency owners in building their dream agencies. This book is dedicated to each one of you who give my work greater meaning.

Table of Contents

Intro 9

Chapter 1: Learn from My Experience: Growing, Merging, and Selling Agencies for Profit 11

Chapter 2: Evolve Your Business to Stay Relevant 15

Chapter 3: The Secrets to Mergers & Acquisitions 22

Chapter 4: Are You Prepared to Buy, Sell, or Merge? 29

Chapter 5: How to Buy the "Right" Agency 40

Chapter 6: Prepping for a Successful Sale 48

Chapter 7: Merging Your Agency for the Win 56

Chapter 8: Demystifying Insurance Agency Valuation 61

Chapter 9: The Keys to Financing an Acquisition 67

Chapter 10: What to Include in a Purchase Agreement 70

Chapter 11: How to Position Your New Organization for Success 73

Chapter 12: The Power in Strategic Alliances 79

Chapter 13: What Not to Do in Mergers & Acquisitions 82

A Final Word 87

Introduction

When I wrote my first book, “Mergers & Acquisitions 101” in 2011, there were many changes taking place in our industry. Many good companies had been sold, merged, or just up and left the life insurance and annuity space. Because of that, there was a void for agents who were committed to just one career company. The trend was a move away from career companies and agencies and into the wide-open brokerage market. At that time, the internet was transforming the way agents and agencies worked. For one, everyone was going paperless and an even bigger change was the public comparison of products, features and commissions.

I thought change was happening rapidly back then, but that was just the tip of the iceberg and nothing compared to what we’re experiencing today.

Unfortunately, some of the same problems are plaguing us now as they have over the last two decades.

We’re facing an aging agent population with the average age currently over 58 years old. This has meant agents in their seventies and eighties are working part-time, keeping their licenses for the occasional sale. And the total number of agents is getting fewer and fewer.

Not only do we have agents leaving the business, we’ve had carriers leaving too or at least a product segment, to focus exclusively on different products. For example, long term care was once sold by many insurance companies as a stand-alone product, but today is almost extinct.

Despite some of these issues, it hasn’t been all negative. In recent years, we’ve seen the mergers and acquisitions market heat up with many agencies having been already sold and many more likely to be sold in the near future. We’ve seen private equity firms, broker dealers, and large insurance companies leading the way in acquisition.

In the last five years, I’ve received calls from 12 firms asking if I was interested in selling. Although selling wasn’t my intention — it was buying and growing — I learned a lot from these firms and did listen to see if the “perfect deal” might exist that would change my mind.

With so many owners of IMOs, FMOs, BGAs, agencies, and brokerage firms considering selling, I’m writing this book to provide insight I’ve gained from meeting with over 100 agencies face-to-face and discussing in depth, the possibility of a merger or acquisition. So many groups I met with had the same questions, fears, and concerns and I felt it was important to share my experiences as a way to help others, like you, who might be facing a similar situation.

CHAPTER 1:

Learn from My Experience: Growing, Merging, and Selling Agencies for Profit

I entered the insurance industry, like many people, completely by accident. I got out of the Army in October of 1980 after three years – some of the best years of my life. Then I went to college for one semester before I realized that two Cs and two Ds weren't a great start to my education, so I left and got into real estate when interest rates were at 17 percent!

I knew I was meant to be in sales when watching a show on PBS (one of only four channels at the time!) called Action Auction — a live auction to raise money to keep public television stations on the air, I bid $300 ($2 more than I made in my first month in the Army) on a $4,000 item that was supposed to help you find the perfect career using tests, live interviews, resume building and face-to-face meetings with career counselors and everything pointed me to a continued career in sales.

After mailing out 50 resumes, I got five interviews and four offers of employment. I accepted a financial planner position with Mony Financial Services where I went through their training and financing programs available to new agents. I spent four years at Mony before moving on to Minnesota Mutual for three years as a Regional Wholesaler, after which I married my wife Susan and moved to California where I was General Manager at Mutual of Omaha for four years.

My story is one of learning from my mistakes

In 1992, my wife and I welcomed our son, Zach, into the world and then

bought a house that took considerable time and money to keep up. A year later, what do I decide to do? Yes, start my own business. They say that some of the top stresses in life are having children, buying a home, and starting a business. But as I said, this is a story of learning from your mistakes.

My goal was to build an agency that catered to my surrounding community in the Inland Empire in southern California. At that time, June of 1993, there was no internet, guidebooks or mentors to help me and I made mistake after mistake. I leased a large office, moved agents into it, and was surprised at how little planning I'd done to get to this point. What I didn't realize right away was that I would need to get access to a phone system, sign copy machine leases, and pay for advertising. I also hadn't thought at all about margins, as the independent brokerage world was newer back then.

Next, I got stuck on one of the first big tasks as a business owner — coming up with a company name. I eventually settled on Apex Insurance and had some business cards printed with a cheesy logo, only to find out both the Department of Corporations and Department of Insurance had to approve the name.

I spent my first three years struggling to find my identity, recruiting by day and selling by night to pay the bills. I was working longer hours than I should have, but hey — I was the president of my own company! However, what I needed was a partner and had talked to several people about joining me, but no one was as committed as I was to make it work. Nor, were they willing to sacrifice time and money.

So, I kept at it — they say a solid foundation for a business is built in five years and I completely agree. It took me that long to match the income I'd been making at Mutual of Omaha. I wish there would've been an organization like Partners Advantage around back then for an agency to get mentoring to help them avoid landmines and hit the gas on high-potential opportunities.

Entering the world of mergers and acquisitions

Before 2007, I hadn't even thought of buying or merging other agencies into Partners Advantage. By that time, I was making a good living and wasn't working very hard to be able to travel a lot with my family. Life was good. So why would I mess with this? Because I like to do everything the wrong way… until I do something right!

My first move in the M&A world was to buy a company with a couple of very talented owners (one of the reasons to buy is to acquire great talent) called Loyalty Performance. But the owners, Brian Schneier and James Wong, were like a lot of less-mature agencies in that they were overworked, underpaid and

undercapitalized. Brian and James joined our team and renewed my interest in growing a large organization — beginning with 6 a.m. coffee meetings where we mapped out the course for the day. As soon as we started coming in early — our salespeople did too.

I felt like I finally had true partners in the business — something I never thought would happen. Now, when problems come up, I have a small team to handle and when there's success, we share in it.

James and Brian worked as hard as I did to make Partners Advantage a national brand. As a small business owner, this was a great weight lifted off my shoulders — one I didn't even realize I was carrying.

After the merger I had a new outlook on how we wanted to grow as a company and what we wanted it to look like at the end. We discussed the idea of buying or merging other agencies and marketing organizations into ours. Our goal became creating the best IMO/FMO/NMO in the country.

Improving our M&A process

The only thing I knew at the time about mergers and acquisitions was what I'd learned from our attorney during the purchase process. I did very little due diligence and focused more on valuation and what we were going to pay for an agency. What I learned is that we also needed talented management, distribution, and revenues. We ended up buying or merging a total of six very small to mid-sized companies in four years. They all brought different skills to our company. I knew if we continued along this path — adding distribution and developing an enhanced value proposition, we could easily increase our sales and cross-selling capabilities.

Through the trial and error, I learned a few key lessons along the way.

What to avoid:

- Overspending on things that don't drive revenues
- Get rich quick schemes
- Placing all the focus on high compensation — sometimes it's better to take lower comp and get help to grow your business
- Working with too many companies — it makes it difficult for your marketers, contracting team and case managers to handle

What to do:

- Reinvest your profits to grow your company — more money will come over time
- Stay honest and keep integrity high
- Build-out or rent sales programs to recruit and help your agents succeed
- Treat your employees well and develop a strong sales culture with the team
- Work with carriers and agents you want to work with and stay loyal

Because we didn't really know what we were doing during those first years of doing mergers and acquisitions, we ran into some issues. We took on companies that were involved in minor lawsuits (thankfully, the companies we bought were doing things correctly) and paid a lot in legal fees. We also tried letting others handle our operations, paid too much for some companies, gave up too much of our stock, and brought in talent that didn't fit our organization.

But we eventually figured it out and now know what to look for.

What to look for when buying or merging an agency:

- **Talent** - Who on the other company's team could make your team better?
- **Distribution** - What does their agent base look like and do you have pro grams that will help them — or vice versa?
- **Revenues** - What can be done with additional revenues that will help the company grow?
- **Synergies** - Can you reduce rent or lease? Or save money on your staff by increasing the number of salespeople and creating contract and sales program cooperation?
- **Culture** - One of the most important things to look for when buying or merging. If the culture isn't a match — stop negotiating and get out!

In the past, most of our mistakes in acquiring agencies revolved around who to give responsibilities to under new senior management. We struggled with questions like, if you have two people in senior management and grow to eight, how do you divide the job duties? It took a while for me to figure out the answer to this and many other questions but can now say with confidence that we know how to bring in talent — one of the cornerstones of successfully buying or merging — as well as help others do the same in their business.

CHAPTER 2:

Evolve Your Business to Stay Relevant

Twenty years ago, this industry looked a lot different than it does now. Back then, millennium agents were brought into career and captive agency opportunities with a defined training program and a built-in middle management program for support. Oftentimes, there was also a financing program to help a new agent get started in their career with some income baked in. But things changed with the advent of the independent brokerage contracts, which paid more than 99 percent commission in most states. And because of the information available on the internet, agents were able to see that one company didn't have the most competitive products for all ages.

The IMO (Independent Marketing Organization) was different then than it is now too. The role of an IMO has expanded dramatically. In the early days, IMOs would contract as many agents as possible and lock up the contracts for 6-12 months. You might recall that contracting was much simpler back then with some contracts being only three-fourths of a page on one side! Faxed contracts were flying fast and furious in the wild, wild west of contracting. Marketers were being evaluated and paid by the number of contracts being brought in each day.

As a result, carriers developed different contract levels depending on whether you were an agency, an agent who was recruiting, or a solo agent – sometimes these contract levels would go 17 levels deep! It seemed like everyone became a recruiter and wanted to make a few points off other producing agents. So IMOs (like Partners Advantage), would recruit not only agents, but other established

agencies as well as agents who were looking to build their own agencies. It was easier back then because the value proposition for a majority of agencies was product, compensation and service. Everyone talked of the "Big 3" and soon the market was flooded with agents trying to start agencies — with some having great success.

In the last 11 years, the industry has gone through both the financial crisis and SEC Rule 151A and has come through leaner and more conscious of what products look and perform like and what the public perception is of the insurance industry. Products today are amazing considering the low interest rate environment and Compliance and Suitability are better than ever. We're also seeing changes in the agent base with fewer agents coming into the industry and when they do, they're becoming Series 6, 65 or even Series 7-licensed.

The emergence of the "Super IMO"

A new IMO is emerging in 2019 — one we've never seen. This "super IMO" will change our industry forever. Super IMOs are being formed by private equity firms, broker dealers, large insurance companies or agencies and will become the new norm for agencies, agents and carriers alike.

They'll offer what agents have been looking for, which is to work with an IMO that creates opportunities for them, such as how to get in front of more prospects, make more money, or build the type of company they want. Agents know there are consumers that want and need our products, but they're looking for different options on how to reach those consumers to make a sale. Because not all agents want to do business the same way, the new IMO will need to accommodate agents' differing needs:

- Some agents only want to work online with prospects — where they're not required to physically talk to the consumer.
- Others want to sell via seminars, which can be expensive but very effective.
- Some agents want to work only leads, whether that's through direct mail, a call center or leads they attract online.
- Still others are using certain types of products to interest the consumer like P&C, Medicare Supplement Plans, Medicare Advantage Plans, final expense insurance, and even pet insurance that could potentially lead to the sale of life insurance and annuity products.

Another change is that IMOs have costs they've never had before. The new IMO employs a Legal team as well as Compliance and Suitability. They spend substantially on technology, which affects many areas of the business. For

instance, technology helps the commission team do their job with greater accuracy and gives the sales and marketing team access to all the tools available on the market today. With commissions being decreased by some carriers and the demands and costs of the new IMO being so high, it will force them to create size and scale to cover their expenses and still make a profit. This may not be a bad thing for our industry as it will force smaller agencies to align with the larger IMOs. This will give their agents the tools needed to compete while not forcing those smaller agencies out of business.

Ongoing challenges facing our industry

However, there are a few challenges we must be aware of, including:

Fewer carriers: The number of carriers in our space using IMOs is decreasing and in some instances, carriers are getting out of product sales altogether or being merged into others. Some carriers have announced they don't want to work with IMOs and would rather contract the smaller agencies direct.

Fewer agents: This has been a problem for decades — fewer agents coming into the life insurance and annuity industry and current agents getting older and older.

Carriers building out a direct model: This has been a trend for a while now with carriers building products and going direct to the consumer — completely bypassing agents, agencies and IMOs.

Government regulations: We've made it through SEC Rule 151A and other government regulations set forth by the Department of Labor (DOL), and more are coming! There is continued talk of creating more oversight of annuity sales and life insurance sales and renewed conversations around full commission disclosure to clients.

Commission-play IMOs: There are more and more IMOs and agencies popping up that only have commissions as their value proposition. They find the best compensation plans they can and offer them to agencies and agents while only keeping a few points themselves. This will eventually kill the pricing plans for carriers and not be good for the industry with no oversight, training, compliance and guidance being given.

A Super IMO's role in today's environment

A "Super IMO" in 2019 and beyond, will offer many services. They will be a one-stop shop for agents by providing expertise or resources in the following areas:

Compliance and Suitability: There must be a team reviewing every application to make sure a suitable sale was made and that agents understand the new rules of selling to seniors. Full training should take place constantly so there are no bad sales being made, no confusion for the consumer, and that the best product is being offered (not necessarily the one with the highest commission). In general, the products we have available for sale to the consumer are good and we should be happy to share all the benefits available to the prospects.

Large Case Support in Life Underwriting: Having people on your team that specialize in working with health and financial underwriting, is critical to making sure the products being written have the best chance of success for the consumer. These carriers change — sometimes on a weekly basis —what they will and won't take in terms of risks so having a knowledgeable team can solve a lot of problems.

Advanced Markets: This was an area that, in the past, was only accessible to a few. Today, with all the information available, more financial professionals can find success with larger, more complex cases. The Super IMO will be the perfect resource for point-of-sale help. Some IMOs have focused on specific areas and been successful with Premium Financing, Retirement Planning, Executive Bonus Planning, and others. And there are still plenty of opportunities that have yet to be uncovered. Constant training in Advanced Markets will open up these markets to all financial professionals whether they end up taking advantage of them or not.

When I came into the business in 1982, I started selling to friends and family and also worked a lot of orphaned policies. I ran into one on a Clark Griffith and went to see him. As it turned out, he was the son of Calvin Griffith, the owner of the Minnesota Twins at the time. I was only four months into the business and totally ill-equipped to do any planning with him. But I gave it a shot and was given the "Our attorneys handle all that" line. However, I did score a couple of tickets to that night's game from him!

Hard working professionals come across large cases on a daily basis — they just need to know what to do once they find them.

Strategic Alliances: Creating partnerships where both parties win will be the

job of the Super IMO. And it's something that Partners Advantage has developed strength in. Agencies will often come to us with great ideas (and others not so great) that they need our help to make happen. Sometimes they need help developing an idea and making sure it's viable, other times they are looking for us to invest in their idea and still others, are looking for guidance and mentoring as well as our distribution. This is something we enjoy doing and will often have partner carriers that can get involved to help finance some of these ideas or get involved with designing a product. More partnerships are needed in our industry and that can come from financial professionals, agencies, or carriers.

M&A (Mergers & Acquisitions): I've said this many times over the last decade, but EVERYONE should be open at any time to buying, selling, or merging (bringing on an agency, or merging your agency with another). Considering it or looking into it doesn't mean you have to do it — but it's worth exploring your options. These kinds of opportunities are everywhere if you're looking. They can create problems if you aren't careful, but they can also solve a lot of problems, such as:

- Lack of production
- Low revenue
- Lagging profits
- Talent shortage
- A need to size and scale
- Underdeveloped synergies

If you truly want to establish yourself as a significant agency that can be sold for a profit in the future — mergers and acquisitions is an avenue you may want to consider. If you don't know how to get started, not sure how to value, don't want to make rookie mistakes, or don't know how to pay for an agency — we have a lot of experience in each of these areas. We do understand how to help make each party feel like they got a good deal in the transaction as well as set clear guidelines for diligence and integration, creating the blueprint for the new company moving forward.

Sales Programs: Have programs readily available to your agents who want to work directly with consumers. These can be programs for lead generation, seminars, premium finance, etc. Your agents want to be able to work programs they feel an affinity towards and is best to keep an arsenal of tools in-house.

RIAs/Broker Dealers: Agents today are getting licensed to increase AUM

and build a long career by working in the insurance and securities industry. Most IMOs are affiliating with, creating, or buying into these types of companies.

Training and Partnerships: With so many moving parts — from products to compensation to sales programs, and more, it's more important than ever for agents to work with a marketer that understands them and can help them grow their business. I like to look at a marketer as an inside partner to the agent in the field. An agent today doesn't have the time or energy to keep up with all the new programs and developments that are happening and should be able to rely on the marketer to keep them up to date as well as give them sales ideas.

Annual Planning: It's unfortunate, but many agents and agencies do little to no annual planning for their own businesses. They determine whether they're successful by looking at their balance in the bank or awards they win. That needs to change. Agents need to do planning to learn how to execute their financial plans and attain their goals. A progressive marketer can help build out these plans for the agents but usually with the contingency that agents place all their business with that IMO.

Embracing Technology: Bigger, better and faster is key! IMOs are building platforms that make it easier for agents and agencies to run their own businesses. E-contracting and e-applications ensure paperwork is complete before it's ever submitted and make it easier to update information from producers while saving time in contracting with new carriers. Technology and automation mean greater accuracy in commission payouts as well as reporting on status of pending applications, upcoming term renewals, and production. This allows the modern agent and agencies to make educated business decisions quicker.

Technology will also have a hand in recruiting and sales, saving time and effort. Direct to consumer models are popping up daily and last I heard, there are over 200 of these up and running but by the time you read this, there are sure to be more. We are already seeing financial professionals meet with consumers, they buy products, and contracts and policies are issued and in an agent's inbox before they even get back to their car!

Although not as common, we'll see more of the video chat model of doing business — where agents no longer need to meet a client in person.

Social Media: From Facebook to Twitter, LinkedIn or YouTube, there are plenty of social media sites available today. By the time you read this, there will most likely be new ones. Through these channels you can get content out to

clients and potential clients, letting them know who you are and what you do. When using social media, it's just as important if not more, to be cognizant of the information your IMO is putting out in the world. Once it's out there, you can't take it back! You never want to turn off the exact people you are trying to attract. As an IMO, you have an incredible opportunity to recruit new agents and agencies via social media, if done correctly.

Recruiting: A lot of the old ways of doing things, don't work today. And that's the case with recruiting. An IMO in 2019 and beyond, will recognize that their value proposition has to be different than the big players in this space. Agents and advisors know total compensation for IMOs, they know what others are receiving and are naturally, using it to their advantage. As an industry, we need to work on bringing in new agents and advisors, training them properly and helping them get through their first year or two financially. Whoever solves this problem the best and the fastest, will spend less time competing for agents and advisors and more time finding exactly the right people to bring into the business and spend their time on.

The changes are coming and can't be stopped, so alignment between agencies and IMOs will be key to running healthy and strong organizations. The days of agencies working with many different IMOs will likely decrease in the future as the time spent and mentorship provided by the top IMOs, will far outweigh potentially making an extra point or two.

CHAPTER 3:

The Secrets to Mergers & Acquisitions

Many owners hear the term "mergers and acquisitions" (M&A) and assume they go together when in fact, there are significant differences.

A merger is combining two or more companies to create one larger company or entity. The goal is usually to create something better than the sum of the two parts (2+2= 5). An acquisition, on the other hand, is the purchase of one company or entity by another. It may be the whole company or just a division or product line, but it is a full purchase and the acquirer (buyer) can do anything they want with their purchase. A partial acquisition is the purchase of only part of one company (usually controlling interest) to keep it going as a standalone company but with capital, structure, and guidance from the acquiring company.

If you are looking to sell or merge your agency, let's take a look at the different reasons why an agency owner would sell the whole company, part of it, or consider merging.

Reasons to Consider Selling the Whole Company:

- Undercapitalized
- Health issues
- Want more family time
- Want to enjoy hobbies
- Go into personal production
- Retirement
- Not having fun
- Don't have the size to get top contracts and don't

have the energy or money to build
- Become a consultant

Reasons to Consider Selling a Portion of the Company:
- Undercapitalized
- Still a lot left in the tank and want to work
- Want someone to help grow the business
- Still want to maintain the company's identity and typically, remain as president

Reasons to Consider a Merger:
- Want a fixed salary and bonus
- Don't want to wear all the hats you have to wear as an owner
- Believe you could be an asset to another organization and make more money being more focused
- Still have love for the industry and don't mind letting someone else be in charge
- Want to give employees and producers a better opportunity than they currently have

How to handle inevitable changes

M&A activity can immediately change the make-up of the two companies. The process integrates people, systems, processes, and locations — just to name a few of the changes you might encounter. There may be a steep learning curve for the acquired company's employees regarding new day-to-day business activities. This can be stressful for everyone. In order to make this a smooth transition, the buyer must have a plan in place, a timeline, and good communication between employees of both companies.

The selling company's employees' worlds will be turned upside down because most of the time, there's very little that stays the same. And in most acquisitions, everything changes for the acquired company as well. The value proposition is different, the processes are different, and the people are different. It can be a breeding ground for fear and confusion where, *that's not how we've done things in the past*, can become a catchphrase unless there's good communication and training between the buyer's and seller's staffs on how things will be done going forward.

Owners that want to sell often only think initially of the sales price and not

the long-term effects to many other people at the time of sale. In reality, there are many other factors to consider. I've come across quite a few in my involvement with mergers and acquisitions, such as:

- Whether or not you understand that even if staying on for a period of time, you no longer own the business and it may not be "business as usual." I've seen some ex-owners who were forced to stay on for one to three years during the earnout and were miserable.
- For owners who say they want to retire — are you truly ready? What will you do for an extra 8 to 10 hours a day? Will you or your spouse stay sane if you're spending all that time together?
- When employees come to the ex-owner to solve problems, there may be a new chain of command and the answers may not be what you'd give.
- Your life will change when you sell the business and you'll want to consider the impact on a spouse or significant other, and everyone close to you.
- For an owner whose self-worth is tied to the business, this may be a difficult time and a hobby or other interest would be nice to have to fill the void.
- It can be extremely difficult to get through the earnout period of 3 to 5 years before getting back in and starting another agency. I've seen many people try and fail. The industry and its leaders, as well as agents can change dramatically in that amount of time.

Risks for Buyers and Sellers

It's been said that most deals don't meet the expectations of buyers. The synergies they expected didn't happen, production flow wasn't what they were expecting, the post-merger period was fraught with problems, etc. Both sides must go in with an open mind and remember that everyone should benefit from the process. Deals fall apart if one side tries to take advantage of the other. Open and honest dialogue is a must during this time, which can take anywhere between 30 to 180 days to complete. Both parties need to feel comfortable throughout in order to move to the next step.

Each side has a lot on the line during an M&A, one with their company and the other with cash. Therefore, it's critical for each agency to perform due diligence. Many conversations will take place to set up a blueprint and timeline for how everything is supposed to happen. Without full cooperation from both sides, everyone could be wasting time (and money) and the deal could fall apart.

A seller does risk some exposure if the buyer doesn't close. If a buyer walks away because he found red flags during the due diligence process, the next potential buyer may be wary knowing someone else walked away. Future buyers

may think the seller is asking too much, the seller's attorneys are too difficult, or the seller is unreasonable or ambivalent.

Deal Killers in the M&A Process

As I mentioned before, most deals never make it through to the end. Probably 75 percent of potential deals fall through for numerous reasons:

- Culture fit
- Can't agree on a price
- Red flags found during the due diligence process
- Egos
- Selfishness
- Terms of sale
- Seller or buyer got cold feet
- Employee retention
- Shareholder approval
- Books not in order or irregularities
- Too much or too little communication between presidents
- Impatience
- Incompatibility of systems, processes, or compensation and benefit plans
- Trying to force the purchase/sale when it just isn't right
- Timing
- Loss of key customers or key employees/management during negotiations
- Changes in buyer's or seller's strategies
- Inexperienced players
- Internal and external politics
- Overdependence on the president/key employees
- Family dissension
- Indecision on purchase vs. merger
- Changes in the selling agency during the transaction
- Not agreeing or post-closing roles and obligation

Why Now is a Good Time to Buy or Sell an Agency

Despite all the doom and gloom reasons a deal may fall through, in my nearly 37 years in the insurance industry, this is the first time I'd say there are good opportunities to both buy and sell an agency. I believe this is true for many reasons.

Buying an agency

- If you're planning to position yourself as a Super IMO, buying agencies can accelerate your growth very quickly. But a word of warning — make sure to continue growing organically too. It can be easy to get wrapped up in the integration process and trying to figure out how to grow only through acquisition. However, organic growth is what got you to where you are today and should not be neglected — 50 percent of your growth should continue to happen through this channel. It's the combination of growth through acquisition and organic growth that can result in real profits one to three years down the road.
- It's evident to me that our industry is lagging behind the rest of the world in the use of technology as well as certain business skills. I've met with hundreds of agencies face-to-face and 85 to 90 percent weren't running efficiently. I don't blame the owner though because there hasn't been much guidance on how to maneuver in this space. Knowing this, there are many value-buys out there that could be purchased at a good price.
- With fewer agents in the industry than there were 10 years ago, we're seeing fewer sales leaders too. You can buy an agency for the talent alone and have the purchase pay for itself.
- If your company is a true sales organization with sales programs and a solid company culture, you can buy agencies that lack these traits at a real steal.
- If you're a smaller agency, the potential of getting larger and creating financial synergies is a smart reason to buy. And if you're a medium-sized agency, buying smaller agencies and doubling each year for a few years, can create wealth for all owners.

Selling an Agency

- There are a lot of buyers today looking for agencies that want to sell. And with low interest rates, financing hasn't been this attractive in decades.
- It's easy to sell an agency but difficult to get the value you think you deserve. There are ways you can get what you want, if you think outside the box.
- Prices being paid today are 25 to 35 percent higher than they were just five years ago. We may not be at the top of the market yet, but we have seen a substantial increase in values.
- M&A activities were prevalent in our industry in the early 2000s, but then the financial crisis hit and sales came to a standstill.

Many agencies were ready to sell during that time, but there were no buyers. So, timing really is everything. If you're ready, now is the time to strike!

- There are marketing companies and private equity groups that buy con-

trolling interest (51 percent) in agencies. They may infuse cash, structure, and other support to help grow the agency. This is a good way to build up the agency with silent partners, keep the company name, and stay on as president (usually). It can be a good alternative to selling the whole agency, if you only need cash support to keep growing and have a strong desire to work hard and keep building the agency.

You should always have clear goals in mind when you decide to buy, sell, or merge your company. It helps to ask yourself a few important questions:

- What am I trying to accomplish?
- What are the absolute deal-killers?
- What is the timeframe?
- What will the company look like after the deal goes through?

Consider the hot button and negotiable items that each party wants and needs. **Some of these may be:**

- How much cash or stock they want up front?
- Length of the earnout
- Who retains the renewals?
- Distribution of property
- A desire for a higher earnout based on growth

There are many ways for everyone to get what they want and need but it may require you to adjust expectations and terms to get the deal sealed.

If you don't know how to buy or sell an agency but want to learn more details about the ins and outs, you can get mentoring and coaching throughout the process and have someone negotiate deals for you — to date, Partners Advantage has helped eleven agencies with this over the years.

Success Story

A Smart Business Move

At age 48, Mike McIntire was having a ball running his own company in Massachusetts and wasn't looking to sell. However, he was looking for ways to make his business more successful and for ways to give the agents he already had more opportunities. A strategic alliance seemed to be the best opportunity.

Enter Mike's long-time friend Scott Tietz. Both being in the business for years, they had known each other a long time. Over time they thought it might be good

to work together, and they both started Maxx Financial in 2003, which was eventually bought by Partners Advantage. Mike still runs McIntire Associates out of Massachusetts.

For Mike, a strategic alliance was a smart business move.

"It's been great for us," he said. "We try to do everything we can here in Massachusetts, but we always have that back-office support and expertise from Partners Advantage."

At first Scott and Mike joked that it was an east coast/west coast thing that could be fun. And in the end, it was the best of both worlds as it opened up markets for agents, gave Mike access to carriers, and afforded him strength in numbers especially in a changing industry.

"I could have gone to a lot of other organizations, but Partners Advantage is a real entity," Mike said. "I didn't want to just get more contacts and compensation. I wanted to build something of value."

And as the industry is going through a lot of changes, Mike sees one big problem – the increasing age of agents. The biggest fall-out from this is that younger agents aren't taught to sell, they have learned to take orders.

"The day that selling isn't important in this business, is the day that 100 percent of product will be sold over the Internet," he said. "And we know how that works – it doesn't motivate people."

CHAPTER 4:

Are You Prepared to Buy, Sell, or Merge?

Before considering a merger or acquisition, you want to set a solid foundation, meaning have a clear understanding of who you are as an agency. If we don't know where we came from, we can't know where we're going, right? As an owner you need to be able to answer some important questions to gain clarity about your own company:

What is your agency's mission statement? You need to know who you are or who you want to be and believe in it before you can sell others on your goals. I've seen so many agencies with no mission statement to share with employees and customers and I feel it's a huge missed opportunity.

What, as an owner, are you really good at? As an owner, you need to play to your strengths! You may be good at something, but don't enjoy doing it — so just do it until you can find your replacement. Hopefully what you're good at you also enjoy so that you can fill a personal need as well as a business need.

What are your weaknesses? As owners, we sometimes think we can do it all well (probably not true). I had to learn quickly that I wasn't organized and so surrounded myself with organized people. I do what I do well and what I can't do well, I delegate to other people.

What sets your company apart from your competitor's? The answer may be nothing! But understand that you want to create your personal WHY for

your company's existence. You may not have it today and that's ok. Agency owners sometimes don't find their niche until decades after opening their doors. Your differentiator may be a need you see in the industry or you may find it through acquisition. You can still run an agency and make a living without finding something that sets you apart — but if you want to be a Super IMO, you're going to need to know what makes you different.

Is the company organically growing as quickly as you want it to? This question is like going to your doctor for an annual check-up. How does your company look based on your years of experience (are you where you "should" be)? Use the last few years as a baseline — are profits, revenues, and production growing? If yes, can you pour gasoline on the fire and really expand the business? If not, why not? Are you lacking sales programs, or do you have the wrong employees or just the wrong fit? Have you been investing in the future? Have the programs you've tried failed? Diagnose what's going on in your business and change direction as necessary.

What would you like to do but aren't able to because of capital constraints, no time to do it yourself, or no one in your company being able to do it? This question opens up so many ideas of what could be. If you have any "can't miss opportunities" in mind but can't afford to do them, understand that maybe you can't afford NOT to do them. Get a business loan, sell a part of your agency, merge with someone, bring your idea along and create a bonus plan to implement it. You need to hire the right people for the job you want done — not people who haven't done the job before that you think can do it. Yes, there will always be time constraints for things you want to do — so what are you willing to give up or hand off to another employee so you can grow your company?

What's your succession plan? Know what you want to do today and understand you can change your mind at any time. If the plan is to sell sometime in the future, begin setting up your plan today to be prepared. Most of your decisions should be driven by what you want your organization to look like in the future, break even timelines for new projects, and have both long and short-term goals. It's important to always be ready because although you may have the plan to sell in five to seven years, there may be an opportunity you want to take advantage of in three years. And also remember that so many things can happen, from illness to death, regulation or industry changes that will affect your business.

Are the company's business activities transferable to a large producer base? What are you doing today that could be applicable and add value at sale or merger?

Most agency owners unknowingly build their business like a house of cards by basing their profit centers on one specific product line or program, or even worse, by trying to excel in too many areas. The industry is constantly changing, so focusing on a single program puts the agency at risk. On the other hand, agencies that have no focus, never seem to accomplish anything well. And if the business tries to do everything, management can't adequately train employees, and therefore, lose control unless the staff is substantially increased. Answering the questions above are a way to start establishing a well-balanced business.

Whether you buy, sell, or merge: Culture is everything

The term "corporate culture" has become a buzzword these days, but what defines it? Culture is a pattern of norms, values, beliefs, and attitudes that influence individual and group behavior within an organization. The combination of each of these factors contribute to the overall image of the brand and can help attract and retain talent. The corporate values and beliefs are often established by the leaders within your company but will filter down to the employees who need to adopt them as their own for the culture to show up in all aspects of the business. Essentially, culture is "the way we do things around here," and often includes:

- Decision-making style and speed
- Organizational values
- Management leadership styles
- Communication style with customers and employees

The effects of negative agency culture

If your agency culture is lacking or not where you'd like it to be, rest assured, corporate culture can be changed over time. However, it's critical that executives lead the charge and support the process. They must believe in and defend the culture shift for other employees to do the same. It's important for them to communicate to the employees and follow that up by reinforcing the new culture. This is just as, or even more important, when training new employees after a purchase or merger.

The industry has changed dramatically, and many agencies will need to reinvent themselves (or shift their corporate culture) to accomplish profitable growth. Many agencies continue to do business as they did five years ago only to find it doesn't work. Agencies that don't embrace change often find their revenues falling, profits disappearing, and new sales slipping. These are signals it's time to make some changes!

Creating an agency culture

Culture is something that evolves over time and hopefully, if it's a positive culture, it takes on a life of its own. But it starts by being intentional. Many businesses treat it like an afterthought, which can be a detrimental approach.

If you haven't taken time to think about what defines your culture, you'll want to address that as soon as possible. You can establish or renew your agency culture by first considering what type of people do well in your agency and what common values, beliefs, and habits characterize them. By sharing this outside of your organization, you're more likely to attract more of that into your business.

And it's not just your internal employees and a strong management team that you're trying to acquire by developing a unique culture, it's a strong sales force as well. The producers that contract with you, have a huge impact on the success of your agency. So, you want to attract those who align with and support your agency culture.

Culture fit also comes into play when you merge with another agency or purchase one. I've seen many M&A deals falter, and ultimately fail, due to company cultures being misaligned.

The benefits of a strong culture

In fact, the emphasis placed on culture is one of the main reasons why Partners Advantage recently joined the Gallagher family. And it's most likely why Gallagher has been recognized as one of the 2019 World's Most Ethical Companies® by Ethisphere for the 8th consecutive time. Named "The Gallagher Way,"® the company culture is characterized by shared values like:

- We support one another. We believe in one another. We acknowledge and respect the ability of one another.
- We push for professional excellence.
- We can all improve and learn from one another.

The Gallagher Way permeates everything they and we, by extension, do in our business. It guides day-to-day decisions. When you have a culture that runs deep — where everything is viewed through that lens first within your agency, you give the people you employ, the people you partner with, and the clients you serve a consistent and memorable experience every time.

If your agency has good middle and senior managers with the same or similar values as you do, they're able to control the desired corporate culture and reproduce it themselves. In fact, every CEO or president should aim to make him

or herself expendable. The management team should learn from the top but be allowed to make mistakes. You can't expect someone to ever take over your role if you're making every decision. You'll need to think about how you can train your staff to do your job better than you do. This allows you the freedom to focus on other activities or work less and enjoy life.

Improving agency culture starts with employee feedback. To ensure your employees are engaged, motivated and on board with your strategy, you need their honest feedback. Download the employee satisfaction survey and use it to gauge your current culture and uncover ways to improve it.

Why the past years are so important

The last three years of a company's history will tell potential buyers a lot about an agency. There are several basic questions owners must ask themselves as they look back:

- Have revenues gone up or down?
- What is currently being done to change or enhance the trend?
- Is distribution growing or shrinking?
- Has anything new been introduced, or anyone new hired, in the last three years that will dramatically improve results?
- Is the management team intact and will they stay on after a merger or acquisition — and do you want them to stay on?

In a three-year period, every agency will see changes in revenue and profits — either an increase, decrease, or no change.

If growth is flat, management should ask what's keeping the company from growing and why. If the agency is growing, management should continue doing what works but constantly evaluate areas for improvement. If the agency isn't growing as quickly as desired, management needs to investigate. Could it be capital constraints, lack of talented managers, or time away from the business spent improving your golf game or your tan while profits decrease? All of these can be fixed IF you take initiative to address them.

If production is flat, the issue is likely stemming from lack of effort in trying to grow, complacency, or losing production out the back door as quickly as it's coming in. M&A is a way to change this situation and spark growth.

I've seen declining production become a trend in M&A cases. When production goes down, so goes revenue. And when revenue is down agency owners go into cost-saving mode — often cutting staff, services, and anything else that might turn things around. Owners often don't take home a salary because the

future of the company is uncertain. These are prime prospects for mergers and acquisitions.

Once you've evaluated a company and understand strengths and weaknesses along with production trends and needs, it's time to put a plan in action. A talent-poor company needs to hire, grow organically, or acquire or merge talent in. Now is not the time to sit on the sidelines and let time pass — that's how agencies with three to five straight years of declining production got to this point in the first place.

Believe it or not, probably 40 to 50 percent of agencies today would consider a merger opportunity if it were good for the owner and the company. Putting up to three agencies together and building a strong talent base can be an incredible opportunity. In roughly 90 days, you could have notable size and scale, a talented management team, synergies for cost savings, higher production for overrides, and a larger distribution system. If each owner has strong attributes, why not share those with more people?

There are also agencies today that don't just want to sell — they have to sell! They may have built their agency over several years without making the necessary changes, which inevitably led to declining production and zero ability to cut expenses further. These agencies are often more than willing to talk about merging. Many of them are solid agencies with good management, but they haven't been able to and/or haven't been willing to do what's necessary to keep the agency healthy.

Buying or merging agencies doesn't need to cost much. You can use shares of your own company in cases where the previous owner is going to continue working with you. And if they're not going to continue working, you can create earnouts, consulting contracts, balloon payments, or they can carry the note for a certain number of years.

Every agency's growth plan should include possible purchases and mergers. Agencies can create synergies, acquire talent, and create an instant distribution channel far more quickly through a purchase or merger than by doing it organically. Succession plans can be created by merging companies and having partners.

So, what is the end game of *your* agency?

It might seem like we're doing this backwards but think with the end in mind. Agency owners need to consider where the company is headed (what's the end goal). Why are you building growth? What was in your head at the time you created the agency, either recently or decades ago? What was your WHY?

As an agency owner, you've put in the years of work — sometimes 60-80

per hour weeks. Maybe you even had to spend time away from family to get the thing off the ground just so you could have the lifestyle you want now. I know I did when I started Partners Advantage 26 years ago.

When you hung out your shingle and opened your doors to a career in recruiting, training and supervising agents – you had an end goal that would make all your hard work worth it. In my experience, most agency owners build their business with one of three exit strategies in mind.

What was yours? And what are you doing today to prepare for the future?

Did you build to sell?

If you built to sell, whether that timeline was 3, 5, or 10 years down the road, you must continually build value so that when you find the person to buy your agency, you'll be able to sell it at profit. Have you taken the time to consider how long it will take to find the right buyer? Will you find a buyer … at the price you want to sell? Have you done all the groundwork and established all the procedures so you can quickly and accurately get through a due-diligence process? With the build to sell approach, you will always put a significant amount of energy in building an agency in order to sell it down the road. Here are a few practical ways to increase the value of your agency:

- Identify and continue to develop your niche — whether that's a territory, product line, or market that you can dominate
- Invest in marketing and technology
- Explore new market segments and increase cross-sells
- Cut costs and increase efficiency
- Get rid of debt
- Have a good middle management team to help run the company to be less dependent on you
- Team up with an IMO that you want to sell — get mentorship!

I've been approached by many agencies to buy them, and in some cases, it was the right fit and we both benefited from the sale. In other cases, we either missed on the timing or on the opportunity. At Partners Advantage, we've built a robust team to help guide you in order to position your agency for a potential successful sale. If you're even thinking about selling your insurance agency, whether that's two, five or ten years down the road, we'd be a good sounding board to help walk you through the process we've used over the years.

Personally, this was never my intent when I started Partners Advantage, but

this is the motivation for many who start their own agency. If you know what you're doing and find a niche in the market, you can start and sell agencies every five years or so. There are always buyers for successful companies that show they can grow organically. The way you build a company for a relatively quick sale is different than building to own for decades before selling. If you do want to sell quickly, you'll need to grow quickly and back off expenses as much as possible in the third year as long as growth continues.

Did you build to retire and leave a legacy?

This was my end goal when I started Partners Advantage. I knew that I wanted my son or daughter to take over the business so built it with a strong foundation of trust and integrity. I thought I would retire at 55 (didn't happen) and they would take over (didn't happen).

Building out a company that stays relevant for decades or generations is possible, but your exact plan should evolve along the way and is often different than when you started.

Maybe you've already set a tentative retirement date when you'll move to Mexico, golf your days away, and live off the dividends while leaving the business in the capable hands of your family or an internal successor you trust.

If this is your goal, you need to figure out who wants to take over the business and make sure that's in line with who you'd like to take over when you're no longer involved in the day-to-day. Even though you may have selected a right internal candidate to run the show, for some people, it's hard making the transition from employee to manager, and there are a lot of mistakes that can happen along that path. Ultimately this person, or persons you identify, may want more than just a paycheck and day-to-day management responsibilities, which is why you need to put a process in place to transition ownership, at least a portion at the beginning.

Take these steps to put that into place:

- Hire a leadership team that shares your vision, mentor them and in some cases — offer part ownership now
- Create a timeline for transferring full ownership
- But keep your timeline fluid — many things can change the date you set, such as health, financial responsibilities, or you just "being ready"

With the build to leave a legacy plan, you're still going to want to think through and build out internal processes so that the business continues to run

smoothly as you gracefully ride off into the sunset. You put a lot of blood, sweat and sometimes tears into building your business, and having a robust business process makes that transition go smoother. You want to ensure the people you served over the years, continue to enjoy that same level of support, especially once you're not around to make sure things go right. If you need any help in building out those internal processes to run your business, we can help put you on the right track so that your transition goes more smoothly.

Did you build to work until you die?

If you want to stay in the business for as long as you live because you love what you do, that's great, I applaud you. But it's important to take into consideration that working into your later years can take a mental and more likely physical toll on you. When you are physically and mentally drained in the later years, this typically leads to a lag in your business because you're not as actively involved in growing the business, and let's be honest, this is a very tough job.

What are you doing to prevent the business from going downhill as you and your agents age?

Take these steps to help prevent that from happening:

- Seek out new lead sources and add new producers
- Have a solid support staff in place who know how to run the day-to-day operations of the business
- Create an emergency or continuity plan

I know we're all in the life insurance business, so maybe this goes without saying, but I hope you have some sort of life insurance or estate plan in place so that you don't leave your loved ones with a mess trying to unravel your ownership. If you have employees that have been with you throughout the years, if you die in the business, will their jobs die too? I know that's never the intent, but unfortunately sometimes that's the reality. If you're planning to work until you die, you need to have a plan to ultimately transition the business so that it can survive.

Understanding the real reasons behind why you built your agency, will help you figure out the best means to grow, change, adapt, and navigate change in the future. It will also help you understand how or if you want to approach a merger or acquisition.

Success Story

New Opportunities to Grow and Specialize

Business was flat for Independent Brokerage Network (IBN), in 2008. They had just lost two of their major carriers, and they were looking for new opportunities to grow their business and increase revenue.

Kevin Gotto, who was a senior vice president and CFO at the time, was part of the talks for a merger with Partners Advantage. In the beginning, IBN was only looking for ways to gain better contracts. As Kevin recalled though, they soon found they had services and tools that would be beneficial to Partners Advantage; they could offer a better commission system and expertise, along with a securities line that Partners Advantage didn't currently offer. It made perfect sense to merge.

"We were able to fill Partners Advantage's holes, and it made sense to move the organization over," Kevin said.

Three years later, Kevin realizes that one of the greatest benefits of their merger was the opportunity for specialization. Becoming part of a larger organization brought many different types of projects to the table, allowing their staff to focus on one area of the industry.

Making the transition from a small company to a large one may have taken some time, but Kevin says the advantages were worth it. He recalls that before the merger the owner and senior management were always called upon to take care of the specific, small issues that arose every day. He finds that he is busier than he ever was, but the scope of his work is much different. Now, he has the added benefit of a larger team who are available to help with specific problems, freeing him to focus on what can be done to make the whole organization bigger and better.

"Scott honestly has your best interests in mind, and he's smart enough to see that if you're doing well, it's only going to benefit the company," Kevin said.

As the insurance industry goes through changes in the future, smaller agencies will face a different landscape then IBN did when it started out. Kevin realizes that today it is much more difficult to be in a smaller shop.

“Carriers want to work with larger groups and focus their energy there,” he said. “It will be very difficult to even get started in the industry if you aren’t connected to a larger group.”

CHAPTER 5:

How to Buy the “Right” Agency

It’s easy to buy an agency, what’s hard is buying the *right* agency. During the due diligence phase, you must turn over every stone and make sure the agency you’re buying is a fit. Studies have shown that more than half of all acquisitions have brought down shareholder value over time. Revenues can be quickly enhanced while shareholder values, destroyed.

You want to avoid buying the wrong agency, where you open yourself up to:

- Decreased shareholder value because the deal was wrong
- Internal conflict about the new direction of the company
- Ruined morale for employees of both companies
- Stunted growth due to integration problems
- Too much time spent with attorneys rather than growing the new company

If you’re looking to acquire or buy an agency, I urge you to watch out for the pitfalls I’ve seen others encounter. In part, these failures were due to poor executive leadership which led to a misunderstanding and breakdown in teamwork. Cultural mismatch is a major reason for acquisition failure as is overpaying based on stated values. And our list of things that could go wrong wouldn’t be complete without mentioning just plain old bad integration and execution.

Now, if after all that you aren’t scared off from buying an agency, there are plenty of reasons that you might want to continue with this decision:

- You’ll be acquiring new clients
- Expanding geographically

- Potentially gaining access to a new technology platform
- Benefiting from new employees
- Increasing your ability to cross-sell to your current client base
- Growing your agency without having to do it completely organically
- Making more money
- Creating new partnerships
- Accessing new markets
- Joining forces rather than competing against a rival agency

Once you decide to enter the world of agency acquisition, there are a few main areas you need to focus on:

New Business: Ask yourself questions like, Will this acquisition help expand the business and get additional production? What are the real growth opportunities?

Profitability: You'll want answers to other questions such as, Will business stay on the books? And it is profitable to stay in all product lines?

Carriers: Questions for consideration might be, Will there be access to new markets? Or will higher volumes of production help win better contracts?

Retention: You need to know whether you will be able to retain key producers, agencies and accounts.

People: Think about teams — How will they fit into your culture? What do you expect in terms of employee turnover?

Integration: Identify the operating differences up front.

Which type of buyer are you?

Are you a Strategic Buyer? This means you buy companies that will add a missing element to yours. That could be critical mass, a new product line, or management talent. As a strategic buyer, your goal is to take the sum of the two companies and create something more valuable than the two companies alone. Are you a Financial Buyer? If you're a financial buyer, you'll look for companies you can build into a larger organization by infusing capital and then selling for

a profit. You can often use investor's capital to buy the companies and everyone shares in the profits.

Are you a Management Buyer? You'll likely partner with a private equity firm to buy a company. In a management buyout, the management team usually get a significant chunk of the company's equity in the acquisition.

Regardless of which type of buyer you are, you must have a plan for buying your agency. You can't just wake up one day and go out and buy one. There are 10 steps in the process I'll lay out for you, which might seem like a lot. But I know from experience, you can't just wing it. If you work the plan, the plan will work so here you go:

> **Step 1.** Create a list of target agencies you want to buy. This list may be based on geographical location, product line, or talent in the agency.
>
> **Step 2.** Initiate communication with the companies on your list. Start with a letter to one agency or group of agencies and state the reason for writing the letter, the description of your company, and your intentions for putting a mutually beneficial deal together. You can wait for a call back or be proactive and follow back up with the agency after sending your letter.
>
> **Step 3.** Create an information package on your company including the history, business activities, and the direction you want to take the company. This should be appealing to potential sellers and share as much as you can without getting into personal or sensitive information.
>
> **Step 4.** Sign a Non-Disclosure Agreement (NDA) if the potential sellers like what they hear. Once signed, you can share the personal and financial information, along with anything else that would help the both of you to move forward in the process.

Step 5. Once both companies have shared a fair amount of information, it's time to set up an in-depth meeting. This allows both parties to get to know more about the other, their time management, and their corporate structure. This is where you gather all the information that doesn't translate well on paper.

Info you should have access to as the potential buyer:

General Business Information

- Articles of Incorporation
- Minutes from board meetings
- Any Doing Business As (DBA) names for the company outside of the registered corporate name
- List of all licenses and permits
- List of all professionals they work with, including their attorney, accountant, and consultants, etc.

Operations Information

- List of all products and services offered
- Any current promotions
- Any contracts with producers
- All equipment, software, and vendors being used

Sales and Marketing Information

- Customer list with production amounts
- Names of any large producers lost
- All current advertising programs
- Any sales programs the selling company is currently running

Financial Information

- Income statement, balance sheet, and cash flow statement
- Accounts receivable and payable
- General ledger
- Copy of the business plan
- Prior three years' tax returns
- Copies of all real estate leases, equipment leases, debts, and notes

Fixed Assets

- Copy of all physical assets (equipment, furniture, vehicles, etc.), including purchase date, price paid, and depreciation already taken

Intellectual Property

- List of internet domains owned
- Any patents, copyrights, and trade names
- Summary of any legal issues concerning intellectual property

Human Resources

- Organization flow chart
- List of employees with hire date, title, salary, and bonus structure
- Key employee resumes
- Job descriptions
- All agreements signed by employees
- Copies of any executive bonus plans
- Employee handbook
- Copy of employee benefit programs
- List of any past, present, or possible future legal issues
- Workers compensation claim history

Debt

- Any promissory notes, loans, or unpaid taxes
- Any leases for equipment, office, automobiles, etc.
- Any defaults or other impending debt

Contracts

- Any contracts pertaining to the business — oral or written
- Vendor contracts, including price and compensation
- Stock options or bonuses promised to shareholder, vendors, or producers
- Contracts with promises to pay — advertising, software, lists, etc.
- All management contracts
- Any maintenance contracts

This is a lot of information to gather but is absolutely necessary to ensure you're making the right decision. Don't be afraid to walk away at any time. Moving forward with a company that doesn't feel right, could be a very costly mistake. Remember, 75 percent of acquisition attempts never make it to signing day.

Ok, onward and upward…

Step 6. Once you find a company you're highly interested

in, sign a Letter of Intent. This letter states that you intend to buy the company, at what price, under what terms and on what date. This letter also asks for exclusive negotiating rights for a period of time. This is a non-binding agreement by both parties, but it is a starting point based on the information you have so far.

Step 7. After you sign the Letter of Intent, perform due diligence and look at every agreement, lease, and contract associated with your agency. Pore over the other company's business and personal financials, learn about their staff, and look for synergies that make buying the agency a good idea. This is your opportunity to turn over every stone for any opportunities as well as potential deal killers.

Step 8. Create a purchase agreement. See Chapter 10.

Step 9. It's signing day! All the details have been ironed out and today's the day everyone meets to transfer ownership to the new owners as well as cash, stock, and agreements to the sellers.

Step 10. Integration. Now the fun begins! See Chapter 11.

But wait, there's more! One of the major decisions you'll need to make when buying an agency is whether you'll employ the past president. Let's weigh the pros and cons of this decision carefully:

Pros:

- ✓ Past presidents can be instrumental in getting the message out to their distribution channels, if they're supportive of the new company's value proposition.
- ✓ Past presidents can be a wealth of information and a big help in integrating the two agencies. Many agencies may have done things that weren't written down anywhere, such as oral agreements with customers or systems (this can be good and bad) that only one or two people know about.
- ✓ They can fill you in on intellectual property or programs that are only partially complete or used very little that you may be able to bring to life.

- ✓ Past presidents have connections. And their contact with carriers or other marketing companies and agencies could prove useful.
- ✓ Keeping the past president on could mean senior management stays intact, making engagement with existing partners that much easier.
- ✓ Having the past president on board in the event of a legal issue stemming from the way he or she did business, can be a huge help.
- ✓ You can leverage the strengths of the past president by off-loading non-revenue generating activities and allowing them to work in their zone of genius for the good of the new company.

Cons

- ✓ Past presidents may have built their company from the ground up and are used to doing things that are contrary to the way you want to run the business.
- ✓ For many, it can be a big transition to stop using company money to pay for personal items, which can lead to issues for you.

If you ultimately decide to the keep the past president on, you'll want to lay out the parameters of their job description or employment agreement so there's no room for misinterpretation. This should include what's expected, the bonus schedules (if applicable), their title, and their work hours.

The employment agreement, if you choose to create one, should be one or two years in length and have an "out" in the event they are terminated for cause or quit on their own so that your company isn't required to keep paying them.

You also have the option of hiring the past president as a consultant and if the integration goes well, you may choose to hire them as an employee down the road. It might work well to put them on a small base salary with great bonus potential considering they're an entrepreneur who started their company with unlimited income potential in mind. Using this model, past presidents can use their skills to build out a division of the blended company, do what they like, and still have the potential to achieve their own financial goals.

A lot of the issues that can arise, like who gets a car allowance, the country club membership, or other perks. These should all be discussed in the discovery phase or they could be what kills the deal in the end.

If issues do arise with a past president, it can be like a cancer in your organization so it's best to sever ties and move the person out as quickly as possible. It's not your role to help the past president adapt to the new company, it's theirs. The integration phase will be challenging enough without this added distraction.

At this point, you should be completely prepared to buy an agency, but what

if you're the one being acquired? Next up, we'll discuss how you can become the "right" agency for someone else to buy.

CHAPTER 6:

Prepping for a Successful Sale

Selling your agency is a huge decision that requires you to be brutally honest with yourself. If not, you may find that you're in a weak negotiating position or doing something you shouldn't be. If there are several owners, the president must take the lead in putting shareholders' interests ahead of their own.

In this chapter we'll address what may compel you to sell as well as how you can make your business more attractive to qualified buyers.

First reason you might be looking to sell — **retirement**. In most cases, buyers will want the sellers to remain working for at least a short time after the sale. If an earnout is part or all the sales price, the seller would probably want the same thing to protect their own interests. Usually, the new owners want the past president to remain for as little as six months to as much as five years. But if you are selling to retire, you may want to look at the shortest period the new owner is comfortable with. If you really want to retire once the business is sold, you should begin planning a year or more in advance. Hire or build a strong management team, including a president. The president can stay on with the new company for as long as both parties want, and the owner can usually sign the deal and be done within 30 days.

You might also be looking at selling due to a **change in strategic position.** If your agency is doing 70 percent or more of your business within a particular market, and you feel the market is saturated or may go away — that could be a catalyst for selling. Many agencies, both successful and not so successful, have a product line that most of their business comes from. With that, there can be concentration risk.

For example, when 151A was taking up so much of our time and energy, agencies with a strong brokerage annuity background but few registered reps, were in danger of losing the majority of their business. Or for agencies generat-

ing mortgage leads almost exclusively, they were successful… until the financial crisis hit our country and that well ran dry for a few years. I personally know of agencies who business dropped by 80 percent during this time. This was due to concentration risk. If you look at agencies that primarily sold Long Term Care insurance, they were rolling in money just six years ago. But when carrier after carrier dropped out of selling these types of products, hybrid products and LTC riders were added to many products, which caused sales of conventional LTC products to take a hit.

These are a few examples but would be applicable to any market that could be impacted by the economy or government. Working one product line can be extremely successful — until it isn't. Diversifying is the new norm and spreading risk is important. Because otherwise, agencies making millions of dollars in profits could be gone or severely crippled in the event of industry or economic changes.

At some point you may face personal factors outside your control that would prompt you to sell your agency, such as **your health.** If health concerns are unexpected, that or death could lead to a fire sale if not handled properly. It might be necessary for another president or CEO to step in to run the company during the transition period if an owner's health takes a turn for the worse, or they pass away. This provides continuity to both employees and customers during the sales process. However, if the new management team in place for the transition does well and the shareholders aren't happy with the price they'd be getting, they may take the business off the market. Too many times an owner doesn't or can't work, and the key employees or customers leave, decreasing the value of the business. Without active management, a quick, forced sale may decrease the value of the business by 50 percent or more.

An unfortunate factor contributing to the decision to sell could be **disputes among owners.** Maybe you've encountered this — someone perceives they are doing the majority of the work, or one owner wants to grow the business and another wants to keep things the same and enjoy the distribution rather than reinvesting. Perhaps, the owner's spouses don't get along or there are trust or ethics disputes. The odd thing about owners is that many times they don't want to sell their shares to each other. Neither wants the other to get a better deal by staying or leaving. They would rather sell to an outside party so each would get equal treatment. In some cases where there are two owners, they sell, and one gets cash to get out and the other gets cash and an earnout for several years. In that situation, they could both veto the deal if they think one is coming out ahead of the other. This could be the easiest or most difficult sale depending on the mood of the sellers. But for the sale to achieve maximum value for the business, they'll want to find a way to work it out.

One of the most common reasons many smaller agencies want to sell their business are **capital concerns.** What would be ideal is for agencies to get premium from products at one carrier with the highest contract they can get. But no carrier has an end-to-end product portfolio needed, so the business gets spread among several carriers and an agency can't maximize its override potential. Plus, many owners don't have the capital to expand their distribution base and technology or create additional opportunities for their producers.

You may be in a situation where you have the formula figured out on how to build but can't grow as quickly as you'd like because you don't have the money to do so. These are the types of agencies buyers love to buy or merge with their own company. If you're a motivated seller with good ideas and work ethic, you can develop a partnership where both parties win and make a lot of money in the process.

Make your business attractive to buyers

Once you've decided to sell, it's time for some housekeeping. By cleaning and updating the books prior to sale, you'll find everything goes much smoother.

Before the sale

1) Prepare a current balance sheet and cash flow statement.
2) Cut any personal expenses.
3) Get family off the payroll if they don't have any significant responsibilities.
4) Pay off short-term debts.
5) Clear up any lawsuits before putting the agency up for sale. If that's not possible, make sure all legal documentation is made available to the buyer for review. A savvy buyer will look at the lawsuit as a nuisance, want a discount on the price they would've paid without a lawsuit, or simply walk away. That's why it can be better to settle the lawsuit rather than taking a discount or losing a qualified buyer.

Timing is everything

There are certain times that selling an agency is best for the seller. If you sell at the end of a fiscal year, buyers typically look at historical results over the last three years. If you're able to show the company trending higher the last 12 months and can explain why the trend will continue — buyers can look at the forecast results. This is important because a seller (you, in this case) would be better selling off the forecast, whereas the buyer would normally rather buy off the historical results.

Other factors affecting the timing of the sale would be whether you brought on a large group of producers or internal cuts you're making (e.g., a large lease coming to an end). As a seller, it doesn't make much sense for you to go to market too early after these types of changes and miss out on some of the growth that could lead to a higher sale price.

The sale and your employees

You'll want to be prepared for the possibility of selling to your management team. If you are president or CEO, consider whether there's a senior manager ready to become president. If so, it's a good idea to make that happen before the agency is up for sale. The new president can then take over your responsibilities and give you time to clean up the agency. When the agency is sold, the new president may be retained, which allows you to get out quicker and easier. However, if promotion is not an option, consider if another member of the management team might be a fitting candidate.

When preparing to sell, it's best if you tell as few people in the office as possible. The more people know… the more people can create problems or participate in "water cooler talk," which could eventually reach the ears of your customers and result in key accounts being lost. The only people who need to know are key senior managers and the controller or CFO. If these people are not owners, it's a good idea to create a package that's beneficial for them at the close of the sale, such as a one-year employment contract (usually three to six months' salary), or a retention bonus for staying with the merged company for a period of time. These contracts and bonuses should be tied to a confidentiality clause as well. This will generally encourage employees to stay quiet about the sale when it's tied to a personal bonus.

A must-have

One of the core documents in preparing for a sale, is to create an Offering Memorandum, which is basically a requirement to be taken seriously by buyers. It's a detailed report describing almost every aspect of the agency so that interested parties don't end up wasting their time. The most important part of the Offering Memorandum is the executive summary. This is one of the first parts the buyer will look at to see if they want to continue reading the full memorandum. Everything in this section must be 100 percent accurate because if the buyer decides to move into the due diligence phase and discovers inaccuracies in the Offering Memorandum, they could walk away. If the buyer finds that you've lied or embellished even one point, they may believe you've distorted the truth in many areas.

Your Offering Memorandum should include:

- Teaser
- Executive summary
- The agency
- Financials
- Exhibits

Teaser: A one-page summary of what the agency does and what makes it different and special.

Executive Summary: An expanded version of the teaser that could be three to 3 to 10 pages long.

Section 1: Overview of the agency describing the market it sells to, products sold, and business operations.

Section 2: Would be about growth opportunities and what the future might look like. The point of this section is to sell the buyer on how good the agency could or will be.

Section 3: A one-page description of financial facts about the agency.

Section 4: Describes the benefits a buyer would gain by owning the agency.

Section 5: Includes shareholder objectives, such as who is willing to stay on during the transition and beyond, the reason for selling, and under what terms the owner would be willing to sell.

The Agency: This is the longest portion of the memorandum and gives potential buyers a clear understanding of the agency. It would include:

- **Agency history:** When it was formed, by whom, how it has grown, an how it's changed.
- **Products and services:** Describe what products and services are provided to earn income. What's the product mix between term, universal life, indexed universal life, and whole life? Include any company brochures, training programs, and website information. If involved in securities, talk about the broker dealer the company is affiliated with and what product it sells through the broker dealer. Also include information about products the company has developed or is currently developing.

- **Markets:** Provide an explanation for the agency's target markets, such as small business, wholesale brokerage, lead market, or any others where agency recruits, trains, or assists.
- **Customers:** Give as much info as you can about the agencies and agents the company works with. How many agents does the company have under contract, how many actually produce, what is the average case size, and how many paid applications per month?
- **Vendors:** Describe the insurance companies the agency works with and which products they use. Also include the compensation schedule for the agency, what additional comp is available, and how long the owner has worked with these companies. The answers to these questions can help buyers realize synergies or new markets that could be started.
- **Offices:** Are offices owned or leased? What are the terms of the lease? If the buyers are looking to buy more than one agency in the area, the leases could be key to finding early synergies.
- **Management:** Include a Bio on key persons in management. Discuss what they do for the agency, how long they've been there, and their insurance industry background. Having a strong management team on board can be a real asset to both the buying and selling company since they're often key to running an agency, and the owner should have employment agreements and non-competes signed by each. *Do not include the names of management staff without having a 'no-solicitation – no hiring' clause for all staff included in the confidentiality agreement with potential buyers. Without this clause, the buyers could poach key employees if they end up not buying or you decide not to sell.
- **Employees:** Give facts without names of employees, including pay schedules, tenure, special skills, benefits, etc., so the potential buyers can get a feel for the employee base.
- **Legal exposure:** Any lawsuits in which you are either the plaintiff or the defendant need to be shared in full. Many times, a buyer will still complete the purchase as long as they feel the lawsuit can be settled or isn't too dam aging to the agency.

Financials: Buyers like to see financials of the agency for a five-year period. This includes income statements, balance sheets, and profit and loss statements. They should be broken down in great detail so the potential buyers can see trending and financial changes your agency has experienced.

Most agencies give a detailed description of any excess owner compensation and excess owner expenses they want added back into the EBITDA (earnings before interest, tax, depreciation, or amortization). By adding these back into

the EBITDA, the goal is to get a higher sales price for your agency. If you earn $500,000 in salary, you could hire a replacement president for $200,000 and add another $300,000 to the EBITDA. Oftentimes, agencies sell for four or five times multiple. You could realistically get $1.2 to $1.5 million more by getting these add backs. There are other terms that can add or detract from your EBITDA number:

- Non-recurring events, such as an office move costing $50,000
- One-time settlement received or paid due to a lawsuit

Exhibits: Any other information or long exhibits like audited financials, litigation, leases, or any pictures of the agency could be included here. This will support some of the information already provided.

Whatever your personal reasons for selling, preparing as soon as possible and as thoroughly as possible can make your agency even more attractive to buyers and increase perceived value.

Who do you sell to?

Selling an agency can be a bittersweet time for an owner. They sometimes have decades building the company just to have it gone — sometimes as soon as three to six months. You want to at least make sure you're selling to the right person.

Some questions to consider:

1) Do you sell it to the highest bidder only?
2) Do you want all cash or stock ownership in the acquiring company?
3) Are you willing to take a longer earnout for a potentially higher payout?
4) Are there employees you want protected — such as an employment contract for a period of time?
5) Can the world know your agency is for sale? Realize that competitors may attack and try to take your agents and employees if they get wind of you selling. Can you take that risk, or should you keep it under wraps?

Potential Buyers

Competitors: Another agency may want to buy your agency to increase its footprint in the industry, add a different product line or gain your talented staff.

This can be a great option IF the culture is the right fit.

Friends and Family: You can sell your agency to friends and family, but again — only if it's the right fit.

Staff: Some of the best to sell to, in my experience, is the staff. Especially if they've been integral in helping build your agency. If they are known and liked by customers, it makes the transition easier. If your agency is valuable, try to get substantial down payment, if you're going to allow them to make payments to purchase.

Bank and Credit Unions: Buying a strong local agency makes good sense for a bank or credit union. However, we don't see a lot of deals happening right now.

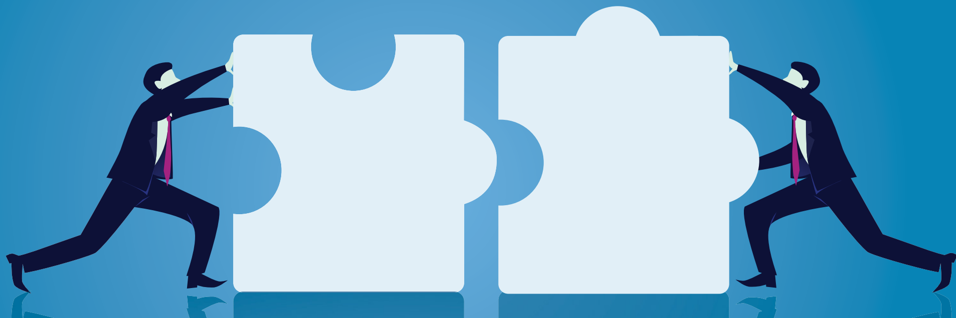
They are attempting to hire their own insurance agents and build small brokerage shops rather than buying. Hopefully this changes in the near future and they become active buyers again.

P&C Shops: Selling to a large P&C shop makes sense for both parties. The life and annuity agencies have warm referrals to the P&C shop customers and vice versa. Of course, culture fit is a top priority, and both need an understanding that they're entering a completely different space in the market.

Carriers: I've seen this happen many times in the past and it's worked out well in some cases, but pretty badly in others. Understand that if a carrier owns you, other carriers may not be interested in doing business with you. And some agents and agencies are biased against carrier-owned agencies.

Private Equity Firms: They have the capital and they understand the spend on technology as well as what's required to grow an agency. Some PE firms know they want to sell off in 5-10 years, so ensure their timeline and yours coincide. Business Broker/ Highest Bidder: If you know you want to sell and don't mind everyone else knowing, this could be the way to go. They charge you in the range of six to eight percent to help you put your package together and market it to the world.

You have quite a few options about who to sell your agency to and the decision comes down to which buyer fits your agency's needs and culture.



CHAPTER 7:

Merging Your Agency for the Win

Merging agencies can be the easiest and quickest way to build a healthy, profitable agency. If done correctly and with the right partner, marginally successful entities can be made into one very successful business.

Merging is not quitting. In fact, merging is quite the opposite. Many times, merging a company into another marketing organization is done because it's the best move for the customers, employees, and agents. By helping create a larger entity, everyone can be a winner — it can be done with no losers!

Looking back to June of 1993 when I started my company, I wish I could have merged with someone because I was overworked, underpaid, stressed out, and broke. I had to handle every problem that came up. Every bill that came in was mine. And if it wasn't for a supportive spouse with a good income, I wouldn't have survived my first three years.

Merging might be a way to save your agency and in some situations, your sanity.

Reasons for Merging

- Want to be part of something larger
- Want a salary and bonus program
- Want to do what you're good at
- Don't want to do all the things necessary to run your own company
- Not having fun
- Want to be part of a team
- Can make more money
- Have a lot less stress
- Decreasing revenue and distribution

Although mergers can look enticing on paper, they need to be well-thought-out and communicated between owners.

What you need to know before merging

Before a merger, there are a few points you need to be clear about:

1) **The role each principal will play after the merger.** What scope of authority does each person have, what daily duties are they responsible for, and what management roles will be shared by committee?
2) **During the merger process, the time and capital of the executives from both companies are diverted from growing their respective businesses.** You may want to delegate that to someone else in the interim.
3) **The human cost.** Staff can be stressed and overworked, friends or family may be terminated, and amount of change in the organization can put a strain on everyone. It will be important to communicate to the staff the benefits of the merger to help them see it as a win-win situation.
4) **The management team will work through a myriad of trials and tribulations.** These help to achieve a combined organization that is more competitive, efficient, and effective than either of the prior organizations.
5) **Buying is fun.** But merging can be hell.
6) **Sometimes a merger can take an ineffective and unmotivated owner and turn them into a productive one.** Having new teammates, value prop, or company culture can be motivating. It can be difficult at times as a solo owner so change can be a catalyst for getting the creative juices flowing again.

Keep in mind the reasons for the merger. Creating financial synergies, efficiencies, and better management, employee teams, and work environment are the goals. And there may be several other motivations for a merger. What about the customers (your agents and agencies)? The merger must be a win for your agents as well, or it will be a struggle to keep them.

Merging more agencies into one company often comes down to your people more than anything else. Getting talented people into the right roles, having another entrepreneur on the team, and having individuals who understand the rigors of operating a successful agency will be critical to a successful merger. It's important to remember:

- Both parties must be able to trust each other — lack of trust can be a deal

killer. Even though each individual is different, principals should have shared values and goals and similar competitive drives. They should be on the same page about where the company is currently and where they'd like it to go.

- Mergers actually work best when the principals' skill sets are different. They must be able to figure out how to complement each other yet know their own roles. And if one is working 80-hour weeks and the other 20, it can be difficult to keep harmony. Flesh this out during the due diligence process.

The benefits of merging

Merging means that you could take the best of both agencies and create a new agency that is even better. There are many benefits to merging, — I'll name a few:

Talent: Choosing someone to merge with that has the same ideals and goals is wise and if the merging entities have varying skill sets that can contribute to overall success — that's exciting. It becomes a team effort with each member having his or her own responsibilities based on individual expertise but working together to create something special.

Financial: If done correctly, the shares of the new company can increase due to cost savings, redundancies, and changes to the size and scale of contracts.

Focus: Merging allows you to focus more on certain projects, which can lead to you becoming a better businessperson.

Revenues: Combining revenues of two or more agencies allows the company to hire more talented people.

Time: When partners start taking on more responsibility, you'll have more time for family, hobbies, or rainmaking.

Problems/Issues: Meaning, you have less of them to deal with because one person can usually handle, and you don't need to be involved with every one that comes up.

Built-in Successor: If something were to tragically happen to one partner, having a properly drawn buy-sell agreement frees the agency from being forced to take on the surviving spouse as a partner. If one of the partners wants to sell,

the other owners may want to buy.

As an owner, you wear many hats including recruiter, problem solver, agent to insurance company liaison, case manager, underwriter, trainer, human resources officer, accountant, therapist, and paralegal. It's hard to wear so many hats and remain effective. Sometimes the weight of the hats becomes unbearable. And you may only wish to focus on recruiting, training and selling without having to worry about what happens after the sale. You need someone who can manage things like employees showing up late, vacations, incomplete applications or website issues. You want to drive more business but having to pull your attention away from that to the operations side of the business, can be inefficient.

Merging allows you to focus on one or two duties you enjoy, while hiring someone else for the other tasks, which could be a dream career for them with a substantial salary, bonus package, and benefits. However, hiring more staff to help fill some of these roles adds expenses, training time, and supervision duties. Many owners not only believe that no one can do it quite as well as they do but fool themselves into thinking they can make a lot more money or have family time if they run things alone. In reality, that's not likely to happen. If I knew I could have merged with someone and focused solely on marketing my company, I would have been able to grow it faster and more effectively than trying to do it on my own.

Wisely choose the company to merge with, and a merger can be a smart move for both your agents and employees. Choose a company with strong benefits and work environment for the employees and one that offers training, support, and programs for the agents to succeed. Make the right choice and you create a four-way win — employees, agents, the acquiring company, and the selling company. Plus, as the owner, you may earn as much or more than before.

CHAPTER 8:

Demystifying Insurance Agency Valuation

There are many different ways to value a company, but it's important to remember valuation is just a guideline of what a company is worth on paper. Sellers can ask whatever they want for the company but will have to find a buyer willing to pay that price.

Methods for determining an insurance agency's value

In general, the most common valuation method for companies is a discounted cash-flows methodology. However, because an insurance agency does not have tangible assets, a multiple on earnings method was used in the deals Partners Advantage Insurance Services was a part of over the past few years.

Multiples of earnings before interest, tax, depreciation, and amortization (EBITDA): This has been considered a common valuation process for buying and selling insurance agencies. Once the agency's EBITDA is known, the value can be found with a multiple. For example, if the EBITDA is $1,000,000 and the multiple is 4, the agency is worth $4,000,000. (See the list below for how to determine the multiple and value of your agency).

Multiples of revenue: This is a good way for a seller to value an agency when it's losing money. There would be a multiple attached to the revenue, which would be the purchase price. And yes, under certain circumstances, a buyer may be interested in an agency that's losing money. Ideal conditions for turning a profit may include start-up companies, those that are poorly run, those that have

bad contracts, or companies that are poorly managed.

Multiples of gross profit: Gross profit is the difference between revenue and the cost of goods sold. If the business is breaking even or losing money, this is a good valuation method to use. Thus, valuation also works well for the buyer if they are buying through an earnout.

The intangibles that increase the value of an agency

If you've been in business for a few years, you may already have the intangibles that could increase the value of your agency. But if you don't, knowing what could increase value down the line can be extremely helpful as you plan for the future.

Does your agency have…

Market penetration: Does your agency dominate a product line, territory, or specific market niche? Maybe you're the largest brokerage office in Nebraska or write more target life premium in the college planning market than anyone else. What segment of the market does your agency "own"?

Diversified revenue stream: Spreading income over several markets, product lines, or carriers can decrease the risk of a catastrophic financial hit.

Distribution relationships: Do you have both a personal and business relationship with key producers? Will producers stay with your agency if there is a sale or acquisition? Maybe you have a long-term relationship with key people in a carrier home office that you write a majority of your business with.

Organic growth: Has your agency grown year over year for the last three to five years? It's good to show that your agency has weathered bad economic times and was still able to add production and profits.

Operating model: An agency that is results-driven rather than process-driven is viewed as more valuable. Although having a process is beneficial, buyers are ultimately looking for results.

Age of shareholders and employees: Buyers are generally like to see a mix of managers between ages 30 and 60 with some younger professionals in decision-making roles.

Non-compete agreements: It's a good idea for agencies to have every employee sign a non-compete even if they are difficult to uphold in a court of law. For many, it's the threat of legal action that may stop them from giving, selling, or stealing proprietary information. It also protects owners from employees trying to take your agency information and open a competing agency.

The actual number of producers in an organization: As a marketing organization, you should have a broad distribution base of producers who write business each year. The 80/20 rule almost always works — 20 percent of your producers account for 80 percent of annual production. Knowing the actual number of producers and spending the majority of your time with them can improve your overall production, which could translate to a higher valuation for your agency.

Size and scale: The size and scale of your existing operations may have a direct impact on your ability to withstand the loss of key individuals or accounts. A buyer would not want the agency to be crippled by certain individuals or accounts leaving. By having a larger staff, greater production, and more producers, your agency's valuation can be higher because it can absorb those losses easier than a smaller agency.

Technology and systems: Does the technology your agency uses allow employees and producers to work as a team? The more an agency can use technology instead of spending hours manually managing policy updates, agent communication, training, and development programs, the more it will increase its bottom line and sale price.

Seek to increase the value of your business strategically

It's astonishing that even though agencies are an owner's largest personal asset, they aren't being run as a sustainable, long-term business. From what I've seen, they spend little or no time on planning, building shareholder value or thinking about their end game. In most cases, agencies are being managed on a day-to-day basis, and strategic planning and goal setting are non-existent.

You could be putting your agency at risk every day if you don't have proper supervision of all departments and proactively manage your business. Additionally, if you aren't actively creating intangible value and realizing competitive advantages, this can lead to lower agency valuations.

Some of the most favorable ways to solve differences in valuation

During the negotiation period over an agency's value, everyone is out to get the best deal possible. Sometimes the numbers just don't add up, leading one party to walk away. The multiples given to a agency several years ago, could be different than the multiples now. Since we can't go back in time, and assuming everyone wants to close the deal, there are some alternatives to an all-cash deal:

Earnout based on revenue: The seller can get cash up front and an additional sum of money (usually after two years) based on revenues the current agency brings in. This is a good way to ensure both buyer and seller remain on the same page and have the same goals during the first few years after the sale. If you, as the seller, believe in what you're selling — this is a good way to get your asking price.

Partial buyout: If the buyer and seller cannot come to terms, the buyer can purchase a portion of the agency. Typically, the buyer would purchase a majority interest (51 percent) and would use his or her skill set to increase the value of the agency. Generally, the seller would stay on as an owner and try to build the value of the remaining 49 percent to get more money in the sale.

Consulting contract: In this situation, the seller would stay on as a consultant for two to five years after the sale and receive additional monies for the work.

Payments over time: This is a common approach to solving differences in valuation. By spreading payments over time, a buyer can use current cash flow to make the payments and the seller can get the price they want.

Overcoming the challenges of valuing a smaller agency

It's more difficult valuing a smaller agency because the owner of the agency is usually closely tied to the business. If this is you, you may be the one who has the relationships with the agents, staff, and carriers. When buying or selling a smaller agency, it is usually best for you to stick around for at least a year or two as an employee or consultant.

Many times, the smaller agency also runs many personal items or services through the agency checkbook. These need to be taken out to find the real EBIDTA for the agency. If you haven't kept your books current or kept good reporting records, these items will need to be brought up to date in order to create

a correct valuation.

If you're staying on for a period of time, the best way to fund these buyouts is to create an earnout of some sort. That way the buyer gets a true valuation and neither side is taking advantage of the other. There isn't a large market for small agencies either so most of the time the owners just run off the agency until it has no value.

The real benefit of buying in the small agency market is that there are usually easy synergies that can be capitalized on. A small agency typically has lower contracts and sometimes redundant staff for the buying organization and the potential for rent and software savings.

Success Story

Get Big or Get Done

It's said that in the insurance industry that you either get big or get gone.

And it was this thought, along with changes to the industry, which brought Steve Freking and the other three owners of Independent Brokerage Network (IBN) to look for opportunities to grow their business.

"We couldn't get the top contracts because we weren't big enough," Steve said.

In April of 2008, they finished a merger with Partners Advantage that offered them greater opportunities to grow the business in a larger agency. Steve was able to gain part ownership of Partners Advantage and IBN got to keep its staff members, who are now better off in a larger organization. It was a positive move for everyone.

Steve advises that the key to a successful merger is aligning with people you can work with on a relationship basis. "Details are messy and there will be hiccups along the road, but if you are working with people you like, you can work through that stuff together," he said. "It's all about forming the right relationship."

For Steve, he recalls two tricky parts to their deal with Partners Advantage. One was during the valuation period and the other during integration.

After the merger, Steve had to adjust to his new position. As co-owner of IBN, he had to wear a lot of different hats to keep all the wheels moving. But at Part-

ners Advantage, he found it hard at times to not have his hands in everything. In the end, he found that being part of a more stratified agency where he could focus on one or two more specific roles did have its advantages.

"From the marketing standpoint, it's really exciting because I can really drive some programs and focus on that and not get pulled into a million different other things all the time," he said. During valuation, IBN shared that it paid all agent commissions, all the time, including renewals – something that Partners Advantage wasn't looking to add to their agency. Eventually, they were able to strike a deal in which IBN still functions solely to pay out renewal commissions. "It made the valuation process less complicated this way, because we didn't have to value a book of business, we could focus on valuing the future of the business," Steve said.

They had spent six months hammering out this deal, only to have the Partner Advantage president leave shortly post-merger, which threw off the IBN staff a bit, especially considering the challenges during the integration process. So, having built those key relationships between the two companies ended up being really important. Having one person leave didn't matter because they had enough in common with the rest of the staff at Partners Advantage that the deal didn't hinge on just one person.

"We were able to move forward, and it was a great move for everyone involved," said Steve.

CHAPTER 9:

The Keys to Financing an Acquisition

Depending on the size of an acquisition, financing can play a key role in making it possible. If the seller wants or needs to be paid in cash, it's usually done on a discounted sales price because of the financing. It obviously works to everyone's advantage when interest rates are low.

Options for financing an acquisition

Agency Ownership: The buyer's agency ownership can finance the purchase. Although this dilutes the shareholder's shares, the goal is to make each share more valuable through the purchase of the agency. This is more commonly accepted if the seller is remaining on as an employee and has vested interest in making the share values increase. The shares can be vested immediately or given as warrants (option to buy ownership) at some time in the future at a fixed price. Ownership can also be given as a short-term form of equity transfer with the option to buy the ownership back at a certain time for a certain price.

Earnouts: Sometimes when the buyers and sellers can't come to terms on the price of an agency, the buyer's price can be used with earnouts. An earnout gives the seller additional money or ownership only if the acquired agency performs above a specified level in the future. Sellers usually believe they have new production, new producers, or new ideas that will grow their business dramatically in the next one or two years. An earnout allows the buyer to purchase at a price they are comfortable with and the seller can get their price if specified conditions and production goals are met.

When putting together an earnout package, you'll want to discuss:

- What formula will be used
- Whether the earnout is based on profits, revenue or production, or a particular project
- How long the earnout will last
- The minimum and maximum amount of the earnout

Seller carrying the note: This is a common practice in the small to midsize agency purchases where the buying agency is financially stable. Typically, the buyer makes a down payment to the seller, and the seller carries the note for the rest of the purchase price. The terms of this note (interest rate, principal payment, length, etc.) can vary depending on the negotiations. Sellers usually want a shorter-term note with higher interest rates and the buyer wants a longer-term note with shorter interest rates.

The seller will carry or hold a note because banks usually aren't excited about funding small to midsize agencies. They are looking for strong cash flow, little or no debt, and significant assets. Also, the buyer will usually have less rigorous standards about what they will buy and for what price. Usually, the sale will be completed much quicker and with fewer steps when the seller holds the note. To help the seller who's willing to carry the note, the buyer can put in one or more balloon payments into the note to get cash in the seller's hands quicker.

Debt assumption: Some agencies carry debt for expansion, furniture and equipment or lines of credit. It's best if those can be paid off before the sale but if not, they can usually be assumed. The buyer would assume the debt and continue to make the payments as part of the purchase price.

Employment agreements/ Consulting agreements: When a seller wants to remain a part of the new organization, one of the discussion or negotiation points can be getting a guaranteed contract. The amount and terms to be negotiated but would be part of the buyout package.

Bank financing: Banks will look at both the buyer's agency and the combined agency in deciding how much money they'll loan. Banks can also offer a favorable interest rate, meaning the loans can be paid off in a relatively short period of time.

> <u>Commercial bank loans:</u> These include short-term loans, lines of credit, and intermediate-term loans.

Short-term loans: These loans can be used when the buyer doesn't need a large sum of money and will pay the loan back in 6 to 12 months. Most of the time, short-term loans are easier to get and are usually unsecured. With a good long-standing relationship with the bank, these loans can be completed within a couple of weeks.

Lines of credit: Marketing companies should set up lines of credit with a bank well before they ever need it for M&A activities. The bank will give a preset amount to spend and interest will be paid only as money is drawn against the line. Make sure to get favorable terms on all moving parts — term line of credit (usually one to three years), renewable or non-renewable, fixed or variable interest rate, ceilings on interest rates, upfront fees, etc. These accounts typically come with a checkbook to draw against the line of credit at any time.

Intermediate-term loans: These loans are usually given for a three to five-year period, and the loan and interest are divided into equal installments. These loans are almost always secured by the buying agency ownership and sometimes with personal guaranties. These are usually for a larger amount of money than the short-term loans, and the banks want to make sure they're fully guaranteed of getting their money back.

Subordinated mezzanine financing: Subordinated debt is a way to get additional financing using both debt (loans) and agency ownership. It's a good way to get additional cash, but it usually comes with a higher interest rate and the possibility of giving up some cash. Usually buyers will get all the bank financing they can and if additional capital is needed, use subordinated mezzanine debt.

Equity deals: venture capital, insurance companies, private equity groups: There are many equity groups willing to invest in sound business ventures. They usually have plenty of cash they're willing to use for M&A activities that will give them ownership in the company and in some cases controlling interest (51 percent). If buyers can't get financing on their own but have a model they believe will work, giving up equity may not be a problem. It goes back to the old saying that having a smaller piece of a bigger pie can work to your advantage.

CHAPTER 10:

What to Include in a Purchase Agreement

The purchase agreement is signed by both the buyer and the seller at the time of closing. Understanding the importance of the purchase agreement is critical — because it can determine the success of your merger or acquisition. Carefully crafting this detailed document with your attorney can help both parties start their new relationship on the right foot and avoid painful or costly problems in the future.

There are many items and agreements included in a purchase agreement. Here are a few:

A General Checklist of Exhibits and Schedules

- Representations and warranties — Sellers
- Representations and warranties — Buyers
- Insurance agreements
- Litigation history
- List of the exhibits and schedules
- Escrow agreement
- Flow of funds at closing
- Adjusted EBITDA
- Real estate leases and deeds
- Confidentiality agreements
- Non-competition agreements

- Non-solicitation agreements
- Employee agreements
- Shareholder list
- Liens
- Financial statements
- Closing date balance sheet
- All contracts
- Bank accounts
- Employee benefit plan
- Intellectual property list
- Insurance policies
- Inventory list
- Pending list of policies or contracts
- Brokers agreements
- Accounts receivable
- Change of control obligations
- Reimbursable expenses
- Customer list

Representation and Warranties – Seller

Representations and warranties disclose information between the two parties of a contract and help ensure the risk is split between the two for the safety and security of each. The seller will have a lot of representations to give the buyer. These representations need to be either fact or true to the best of the seller's knowledge. The warranties are promises of indemnity if the representation is false or inaccurate.

Below is a list of representations and warranties the buyer will most likely want the seller to agree to (there may be others in addition to those listed here). They want to ensure that the seller:

- Is the owner of the shares or assets.
- Can legally sell the shares or assets.
- Confirms sale of the shares or assets will not trigger a material change in the company.
- Verifies that no options, warrants, or claims to the company are outstanding.
- Has provided a complete list of arrangements, contracts, and agreements between the company and other parties.
- Has filed all tax returns.

- Has paid all corporate taxes.
- Represents all current financial reports are accurate.
- Has provided buyer with a listing of all company bank accounts and credit cards.
- Doesn't know of any current or pending litigation involving the company.
- Company owns all the intellectual property it's selling to the buyer.
- Confirms computer software and databases are owned and paid for.
- Has given a listing of all insurance policies to the buyer.
- Verifies all inventory is usable and saleable.
- Has provided the buyer with a complete list of all accounts receivable.
- Doesn't know of any key customers that would stop working with the new buyer or will substantially reduce their production.
- Has provided the buyer with a complete list of customers.

The buyer has significantly less to prove to the seller, but does need to provide or confirm:

- His or her company is in good standing.
- They have the authority and legal right to execute the purchase agreement.
- Buyer pays all of his or her own costs for any advisors used during the sale.
- Copies of insurance benefits, buy/sell agreements, key man policies.
- Copies of general liability and workers compensation, including past or pending claims.
- Copy of errors and omissions including past claims.
- List of any past or pending litigation — either as defendant or plaintiff.
- Description of any settlements made or offered.
- Any bankruptcy proceedings.
- Any judgment, orders, or injunctions applicable to the company.

There may be more information requested and oftentimes, getting one answer prompts more questions. It's important to be an open book during the due diligence process to avoid future issues.

As an agency owner, whether a buyer or seller, you may walk away from a purchase or sale at any time if you don't feel comfortable. Any re-negotiations should take place as soon as possible to save legal accounting fees. But if either party is uneasy about anything, you should openly discuss so that little issues don't develop into bigger ones. And of course, the purchase documents shouldn't be signed until each party is 100 percent on board with the purchase price, terms and conditions, timeframes, and all else related to the purchase/sale of the agency. Agency owners should always consult their attorney and tax advisor to understand how a business transaction can impact their individual liabilities.

CHAPTER 11:

Position Your New Organization for Success

After months of planning, meetings, and expenses, communication can fall apart without a good integration plan. Nothing can destroy the hoped-for value created by an acquisition faster than ineffective integration. In order to successfully complete the acquisition process, the integration plan must be well-thought-out, well-communicated, and thoroughly executed.

Bringing two companies together with two different management teams, two different cultures, and often two different operational practices can be a daunting job. Everyone must be on board with the plan, how it will be done, and have a timeline showing when changes will take place. This should include all executives and employees.

Issues you might see in a poorly executed integration include:

- Leadership can't come up with a style that suits upper management
- Loss of customers or key employees
- Cultures don't mesh well
- Misunderstandings and false promises
- Not able to create synergies as anticipated
- Integration not completed quickly or efficiently

To have a successful integration, there are a few important steps that need to take place before the deal closes.

1) Share a common vision.

2) Provide leadership.
3) Avoid office politics.
4) Make the tough decisions.
5) Act with speed.
6) Set reasonable expectations.
7) Accept change.
8) Communicate, communicate, communicate!
9) Let employees and top customers know they are important and valued.

One way to accomplish a successful integration is to create a 100-day plan, which is a detailed project plan laying out everything that needs to be done, who's responsible, and a timeframe for completion. Plus, a project manager to coordinate it all.

It's imperative to build the plan during the due diligence period so that it can be communicated between management and their teams. If integration lasts too long, it can kill employee morale, cause customer frustration, and distract from growing the company. Without a solid plan in place, customer service can suffer because employees will be focusing on the integration rather than the needs of your customers.

The acquiring company should be completely transparent during integration. To do that, they must:

- Be honest with employees and let them know what to expect
- Handle layoffs quickly, if they must happen
- Communicate the culture, value-adds, and company direction with the acquired company retained employees as they are likely nervous about what's happening
- Bring the team in to the acquired company to immediately begin training on your way of doing things

Making a successful transition

The seller should gather all available employees and tell them about the acquisition as soon as possible and buyers should speak to employees and tell them about their new company. The employees want to know what will happen to them and how the sale benefits them. These meetings need to be as upbeat and informative as possible. This will often be the first time employees have seen the new owner or heard about the new company. Remember, first impressions can

never be re-made.

To protect the company, the buying agency should have all employees sign the following:

Employment Agreement: Provides basic information such as salary, bonuses, benefits, and termination provisions. It usually stipulates a length of time the agreement last but also adds that the agreement is at-will. This means the employee can be terminated at any time, for any reason or no reason with two exceptions — discrimination and contract.

Confidentiality Agreement: Stipulates the employee cannot share any proprietary information or producer lists with anyone during and after the employment period.

Non-compete Agreement: Prohibits employees from competing against the company for a period of time and sometimes in certain parts of the country. These are non-enforceable in many places, unless it's on a shareholder of the company. Agreements are generally for 1 to 2 years for employees and 5 years for an agency that the company is buying.

Non-solicitation Agreement: Prevents employees from soliciting clients or other employees to leave the firm.

Announcing the Acquisition

This is it — time to get the news out about the purchase. Draft well-written press releases, advertisements and social media posts. Then get ready to blast them out to everyone!

Even before the contract is signed, prepare for the event. The operations plan needs to be in place 30 days before closing so the phone lines as well as other day-to-day activities automatically switch over on closing day.

You'll also want to arrive at closing day with the following information already prepared:

- Interoffice communication
- Letters or brochures to the customers of the acquired company
- Meeting scheduled with the acquired company's retained employees on the day of the announcement
- The new organizational chart
- Email addresses for each employee

- Face-to-face or phone visits scheduled with key agents or customers

All the fun begins on closing day! Set up a meeting with your employees explaining the acquisition. Talk to them about your benefits package, new compensation structure or bonus plans (if applicable). In addition, you'll want to share the new org chart and walk through the updated website. You'll want to supply new employee handbooks and provide all necessary information regarding how their job may change — making sure to state everything in a positive way.

It's important to allow for an extended Q&A so that everyone feels their questions are answered and any concerns addressed. You may also want to hold one-on-one meetings with any remote managers or employees and have them visit the home office as soon as possible.

The first 90 days

The last thing you want is for employees to leave after integration. What you do in the first 90 days can help make the transition a success.

- Make any physical moves of locations, employees, or equipment
- Train new employees on company practices and software
- Combine any operations, administration, or accounting procedures
- If the acquiring company is taking over all accounts, shift all addresses of the office, change any electronic deposits from carriers to the corporate account, and notify all vendors of the change
- Analyze technology and software
- Make any necessary changes to the management team
- Address any differences in agency culture with employees and customers
- Focus on the customer! As soon as possible, contact the top 20 percent of customers, preferably in-person or by phone, to let them know how things will improve for them
- Host webinars for as many customers as possible so that you can walk them through the changes
- For anyone not attending the webinars, contact by phone, email, or letter to explain the changes in detail

Lay out your communication plan

Very shortly after the sale, you want to reach out to your agents with a message

focused on the benefits to them.

24 hours after closing:

- Top executives place calls to acquired agency's top agents to personally notify them of the changes before they hear it elsewhere
- Mail letters first-class from the acquired agency's principal to the agent base, including an invitation to the webinar or conference call where they'll learn more

3 to 5 day after closing:

- Email agents the information that was included in the letter and invite to the webinar or conference call
- Email a review of benefits, instructions on how to access the website and other tools, and a reminder about the webinar or conference call
- Hold the webinar or conference call with acquired company's principal introducing the new agency owners and benefits
- Send press release to industry and newswires
- Email follow-up information after the webinar or conference call restating the benefits to the agents, employee and servicing department contact info, and a copy of the press release

If you execute the strategy and implementation plan, you're more likely to find success in the integration phase.

Although mergers and acquisitions can be challenging, if integration is done well, they can be a competitive growth strategy for your agency.

Success Story

Synergies

Jim Lehmann had already been working with Partners Advantage long before he and Scott Tietz entertained an official merger. As the owner of Innovative Marketing Strategies, Jim was nearing retirement age and started thinking about a succession plan to ensure a real future for his agents.

"I wanted my employees to be in a place where they could keep growing," he said.

In talking with Scott, they started looking at the timing and technology that Partners Advantage could offer and realized a merger could be something special.

Jim felt it was the perfect fit to merge the two companies due to their similar business ethics and operating procedures. They also realized there were a lot of synergies to be gained by a merger. Due to Partners Advantage size, it could offer Jim and his company more technology, training, and access to carriers and product lines.

"There was no way for me to take Innovative and move it to the level that Partners Advantage was at without a huge expenditure of capital," Jim said.

The two companies had complete transparency from day one – in fact, on the day the deal was made, Scott came in to talk with Jim's employees. While the road to a merger came fairly easy, they did run into some hiccups post-merger. There were some integration issues when introducing the merger and bringing the two groups of people together.

"Everyone in senior management knew what was happening, but we didn't necessarily push it down to mid-management and the employees."

Since then, Jim and his team have worked to develop on-boarding materials that give them a step-by-step process for bringing on agencies, starting new projects, and merging agencies. Jim explained the overall purpose of these materials is to explain to everyone why the merger happened, how it will help grow the company and then to get them to a place where they can help in making it successful. The employees of Innovative Marketing Strategies weren't the only ones who had to deal with a major transition during the merger. Jim himself faced going from the owner of a company to being an employee of a large organization and being part of the team.

"I hadn't been an employee since 1985!" Jim said.

Sitting down with Scott, Jim said he was very upfront in acknowledging his new role, and the two of them worked together to make the transition successful and smooth. Jim said the key to this process was that it was done intentionally. Flexibility was also of key importance for everyone involved during the integration process. It is that flexibility that has made their merger so successful. Now, Jim has handed over the parts of his job he didn't care for and focuses on the things he likes doing.

"Do I own my own company anymore? No. But I am enjoying life a little more."

CHAPTER 12:

The Power in Strategic Alliances

Sometimes owners will find an agency or other marketing organization and neither party is interested in merging, buying, or selling. Both may have different ideas on how to grow their business and think the other company isn't necessary. Regardless of the reason, a merger isn't happening in the near future.

However, in these situations, creating a strategic alliance can help both organizations and is less permanent. If done correctly, it may eventually lead to forming one company.

A strategic alliance could reap some of the same benefits as a merger, such as:

- Reducing costs through shared office space and leased equipment
- Combining contracts for higher carrier bonuses
- A sounding board for ideas
- Cooperating rather than competing
- Improving your influence and position

It's also possible to look outside the industry to create these alliances. Consider industries that may provide a new client base, are in a service type industry, and one where their clients may also have a need for your company's products.

Some examples include:

- Property/Casualty agencies

- CPA firms
- Tax preparers
- Group health agencies/employee benefit agencies
- Payroll service companies

Pros and Cons of aligning with a property/casualty agency

This industry can be tough to break into, and it's important to find a mature agency that will allow you to work directly with their clients. A mature property/casualty agency typically looks like this:

- Have 2,500+ clients
- Owners make approximately $250K per year
- Owners generally work from 9 a.m. to 2 p.m. each day
- They enjoy lunch meetings (if you pay!)

Most P/C agencies have plenty of space for an agent or two, are receptive to working with other companies, and are also looking for a new revenue source. They may not be the best at giving referrals, which is why it can be helpful to put an agent right in their office. Additionally, it can be good to work with P/C agencies whose primary focus is the workers compensation and liability space. Because otherwise, agents tend to sell only term insurance.

Pros and Cons of aligning with a CPA firm

Some CPA firms have built or bought insurance divisions, but most have chosen to create strategic alliances to work on more complex, advanced cases. These can be the best alliances because they allow for the opportunity to work with a trusted advisor who can pass along referrals.

Agencies can work with one firm, many firms, or one large network of CPA firms. This industry isn't the easiest to approach and requires a seasoned professional, but it can be one of the most profitable alliances an agency can build.

Some insurance companies offer CPA continuing education courses, which puts them in the same rooms with financial professionals, opening the door for them to share information about their businesses.

Pros and Cons of aligning with tax preparers

There seems to be an over-abundance of tax prep companies that offer basic services for around $59. However, they are essentially out of business from May 1st to December 31st each year. Some tax preparers do have an insurance license but may not know how to sell. Their goal is usually to grow their business to around 1,500 clients and retain 80 percent of past customers year after year.

Many of the tax prep companies, like H&R Block, Liberty Tax, etc., have franchise owners that own more multiple franchises. These businesses can be a great source of clients who you already have financial information on. The off-season months are the perfect time to do annual planning, and most times the tax preparer may become an agent for the insurance company as well.

Pros and Cons of aligning with group health/employee benefit agencies

These agencies often work with both large and small companies. A great way to do a lot of insurance and annuity business is collaborate with these agencies on payroll deduct cases, or group sales presentations, for example. By working together, you could get access to potential clients much easier.

This type of agency is a prime candidate for acquisition by a life or annuity agency or IMO because it opens up opportunities for financial planning and larger cases from executives of the companies they serve.

Pros and Cons of aligning with payroll services companies

Payroll companies are now getting involved in all aspects of small-to-midsize companies. They are doing the health, benefits, compensation, and liability; and most utilize employee training on many different topics. Creating an alliance with one or more payroll companies could potentially give your agency access to many employees and owners of companies.

It's possible to create a strategic alliance with each of these types of companies and maybe several of each. Alliances allow both companies to share customers, ideas, and databases.

CHAPTER 13:

What Not to Do in Mergers & Acquisitions

In this book I've shared my personal experience in building, merging, and growing businesses in this industry, which have been both exciting and humbling. The main sections of the book were designed as a guide for you to follow when buying and selling agencies. But sometimes knowing what NOT to do is just as important as knowing what to do. If I can help you avoid some of the mistakes I made, then I've accomplished my goal.

However, if you've made mistakes when buying, selling, or merging — you're not alone. I'll share a few of mine with you:

1) Creating a new division that consisted of one person

I tried for years to get into the annuity business using life producers as my sales team. Twice, I hired annuity specialists to build our own annuity division and both times — failed miserably. I realized that one person does not make a division and one person can only know what they know. After we bought First Choice Financial (FCF) out of Long Beach, California, we had a team of people who not only knew the annuity market but also had thrived in it for more than a decade.

Once our life producers understood that we had a talented annuity team, they began to send us their annuity business and we grew that to more than $600 million in three years.

If you want to open a new division within your agency, don't add just one person — add a team or buy an agency that works in that space. Then use your

distribution to grow that division.

2) Adding a senior management team too quickly

We closed four acquisitions in a little over a year and added five people to our senior management team. This was one of the reasons we entered the M&A marketplace, but we weren't prepared for what we wanted each of these new team members to do. So now, we make sure and discuss that during the due diligence process and include a job description and detailed plan on how to get started.

During the integration phase, we get everyone moving quickly on their new responsibility. Every officer of the acquired company who will work with you, likely wants to know the same things: how they can make more money than they did in the past, how they can use our current distribution base to launch their program, and what their responsibilities will be.

3) Integrating without a plan

In the beginning we sort of just let integration happen — we didn't have a plan other than notifying the field about the changes that had taken place. It was always a disaster for three to six months before things settled down and everyone knew their roles. Now we have a detailed plan that walks us through communication (both internal and external) as well as sets timelines for tasks to be completed.

4) Overpaying for an agency

We have merged or bought agencies that didn't give us the synergies we had hoped for and actually decreased my profitability rather than increasing it. It really takes a full year to know what you bought and compare what you paid for the agency to what you got. I haven't bought one yet that I was unhappy with, but I certainly would have changed the price we paid for some of them. My philosophy has been that it may take longer to recoup the purchase price, but we can make lemonade out of lemons.

5) Keeping all the employees

For our first four acquisitions, we met with the employees of the selling company and told them we wouldn't be eliminating jobs and would integrate everyone onto our team. Although this strategy was done with the right intentions, I would not do it in the future. We believe in upgrading each position in our company and we plan to keep that mentality going forward.

The goal is to keep key, talented employees. Each selling president thinks their employees are the best in the industry (I've actually heard this on several occasions), so it's important to meet with the employees and form your own opinion.

6) Using systems from both companies

Our initial thought was to use hybrid systems to make our staff and the staff of the acquired company comfortable. However, after a year of changes, errors, and frustration, we decided to adopt one software, agency management system, and protocol to use.

Now when we acquire an agency, the remaining staff is required to learn our systems. Don't get me wrong, we always take into consideration the systems of the acquired company, but only upgrade if they are superior to our current system.

7) Not having an alpha owner

Although it may sound arrogant or conceited to some, it's important to know who's leading your company. Since I'd never had partners before, I tried to run by majority vote or committee — it failed miserably. Each partner wanted to leave their own footprint in running the day-to-day operations, which resulted in chaos.

I still believe each partner should have a voice and I encourage him or her to use it. But in the end, decisions are best made by one person. If that person isn't driving profits, replace them (even if that person is you).

8) Giving up control of operations

At one point, I came to the conclusion that the worst part of running a marketing organization was operations and so we outsourced it to another state. Not only did we move it, but we also bought a 2,000-square foot building and relocated our key employees to Fargo, North Dakota. It was a disaster from day one with low unemployment, there was only a small pool of potential employees. Plus, there was bad weather and flooding. It took us two years to unwind that mess and get the operations moved back so we could run our business more cost-effectively.

9) Using shares instead of cash

When we began buying and merging agencies into ours, we primarily used our ownership as a means of payment. This is a good strategy to use if you don't have available cash, lines of credit, or access to loans (or if you're too cheap to spend the cash). It can also be effective if you're buying an agency that will be critical to your success or if the owner will not close the deal without ownership.

But it's not a good strategy to use long-term unless it's used only as a last resort. As your organization grows, the agencies you bought previously will eat up a lot of the ownership interest in the agency and using these shares can dilute the shareholders' value dramatically. You end up with many partners but aren't

able to take care of key employees using stock.

10) Keeping all offices open

We started by keeping all agencies we bought open and active with some sort of team in place. As we've evolved though, we now keep an office open primarily to handle marketing only and have the majority of the back-office functions handled in the home office. Communication and training can become a problem when you don't handle everything under one roof and don't provide constant training and supervision. However, I am a big believer in having branch offices around the country to provide support and training to local agents.

11) Being process-driven instead of results-driven

When we began our mergers and acquisitions path, we found ourselves growing but not making any additional profits. We were so focused on our process that we completely lost sight of the results. It took quite a long time for us to get staff to focus on results rather than just being busy and we did revamp our employee bonus schedule to drive change.

12) Trying to do too many acquisitions at the same time

After discovering the M&A space, we attempted too many deals at once. It's true that there are many opportunities out there, but it's better to be selective and spread them out. When you try to buy too many agencies at the same time as we did, it compounds communication and integration issues. It's difficult enough to have a smooth transition doing one every six months or so until you have a transition team built and ready to go.

During my last decade of meeting agencies interested in selling or working with Partners Advantage, I've come across a few situations that would make my list of what NOT to do. Because they could affect your ability to be successful as an insurance agency owner as well as during a merger or acquisition.

- ✓ Misspell your own title — I've come across 100s of websites that misspelled advisor as adviser. This could be an indicator of bigger oversights. Minor details tell a much bigger story than we sometimes realize.
- ✓ Don't let the decision on when to sell hinge on one salesperson — unfortunately, they may leave you to start their own agency, causing your production to plummet and your business to not be as appealing in a sale.
  When you work with agencies with principal partners –

make sure you put business first and align yourself with the business driver, not the one that's your friend. Or pay the price down the road.

- ✓ If you're in business and don't have current P&Ls, a business plan, or any direction for your company — you're like a boat adrift just floating along. No one will want to hop on that captain-less boat with you.
- ✓ Whether they always hold up in court or not, as a business owner you can at least make an effort to protect yourself through non-compete and non-solicit agreements.
- ✓ Don't abandon your agency in favor of possibly improving your golf game — you're leaving your business as fair game to anyone who wants to take control in your absence.
- ✓ Don't let your agent base become stagnant — one of the worst things you can do is stop growing, rest on your laurels, and let aging agents be the sole source of your business's production.
- ✓ What's in a name? A lot actually. It's the first impression a prospect has of you — choose wisely.
- ✓ There's value in being an optimist — but that's different than ignoring obvious issues in hopes that the situation will correct itself.
- ✓ Have enough faith and confidence in your business value that you don't let agents or anyone else take advantage of you.
- ✓ Sometimes the old adage is true — blood and business don't mix. If you employ family members that aren't skilled, polite, or hard workers it can be a morale killer.
- ✓ And almost impossible to get them out. You don't want to rely on a merger and acquisition to do the dirty work for you.

A Final Word

Mergers and acquisitions can be a lucrative endeavor IF you know what you're doing. Partners Advantage has been fortunate enough to be a part of many that were hugely successful and I, for one, feel that many more agency owners could benefit (more than they realize) from mergers and acquisitions.

My hope is that you found value in this book; it's one I wish I would have had on my bookshelf many years ago. Instead, I learned everything I know know about buying and selling agencies the hard way. I had to track down information wherever I could, try strategies and fail. But it's allowed me to put together this guide with all the info you need in one convenient place, saving you a lot of time and headaches.

Now, I invite you to take a couple of actions:

1) If you have questions I didn't cover or want to work directly with someone who's done it all before, reach out to me at (888)251-5525 Ext. 103.
2) Tell a colleague or fellow insurance agency owner about this book. If you think they could benefit from even one page, please share the book with them. I'd greatly appreciate it.

Thanks for reading. I wish you much success on your next merger or acquisition!

Scott D. Tietz, CLU
Area Chairman, Partners Advantage Insurance Services – A Gallagher Company

RESOURCES

To access the resources and additional reading mentioned in the book, visit:

Sample Employee Satisfaction Survey
https://offer.partnersadvantage.com/hubfs/documents/producer/2019/sample-employee-survey.pdf

Does Your Agency-IMO Relationship Include These 5 Quality Indicators?
https://blog.partnersadvantage.com/does-your-agency-imo-relationship-include-these-5-quality-indicators?hs_preview=UBmDlDUK-10468156193

5 Tips for Attracting Top Senior Level Talent to Your Insurance Agency
https://blog.partnersadvantage.com/could-you-be-attracting-more-top-talent-to-your-insurance-agency

*Links active as of October 2019. Subject to change.

PARTNERS ADVANTAGE®

A Gallagher Company

About Partners Advantage- A Gallagher Company

Partners Advantage Insurance Services, LLC, was founded in 1993 by Scott Tietz, CLU. The company has been built into an industry leader in the life and fixed-indexed annuity marketplace. This well-respected independent marketing organization represents more than 50 of the top-rated insurance carriers in the nation. The company is a one-stop brokerage shop for licensed agents and agencies throughout the United States. Partners Advantage offers specific expertise in advanced markets, Registered Investment Advisor (RIA) and broker-dealer services for registered representatives, top-tier technology, comprehensive training programs, and innovative lead and agency-building programs. Also a leader in mergers & acquisitions with 11 successful mergers to date, Partners Advantage can assist agencies looking to sell in the next five years, in creating a higher value at sale.