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Caitlin B. Houlton Kuntz

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Vendor Contracts 101: M&A Considerations

Legal Update

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Whether we are representing buyers or sellers, when we begin advising on a potential transaction, one of the first questions we ask is, “Have you taken a look at your biggest vendor contracts?” This next installment in our Vendor Contracts 101 series takes a closer look at how to plan for mergers and acquisitions when negotiating vendors contracts.

With the banking industry returning to its pre-pandemic trend of steady consolidation, M&A activity should not be ruled out for any bank – one just never knows when the right opportunity might come along. Negotiating major contracts with an eye toward provisions that impact deals can save headaches and money when the right opportunity comes.

Early Termination Fees

Early termination fees are already on the radar for every banker when negotiating vendor contracts, as most significant contracts these days come with some form of default early termination penalty provision. Facing a continuing trend of losing customers to consolidation, vendors have been firm on imposing harsh early termination fees to cushion the blow. There is another side to that coin, however – you may be able to negotiate a break in early termination fees in the event your bank is converted to an acquirer’s contract with the same vendor. Early termination fees have become one of the largest line-item expenses in M&A transactions, so this can be a great benefit to both buyers and sellers as deal terms are hammered out and costs allocated.

Notice Requirements

How far in advance must the vendor receive notice of an M&A contract event? Termination, change in control, deconversion, and conversion could all have different notice requirements attached to them. Examine each of these and consider how they fit together. Further, how do any notice timeframes fit in with the typical timeframes associated with public announcement of a planned transaction?

Deconversion/Conversion

One of the biggest operational challenges of any M&A event is converting and consolidating the services of the combined institutions. When negotiating significant contracts, think ahead to these situations and what you might need from your vendors. In addition to the timing requirements mentioned above, banks can sometimes negotiate deconversion and conversion pricing and logistics up front, resulting in significant savings. This becomes even more beneficial with longer-term contracts – as we have seen in recent years, the market price for deconversion services on a contract signed today is likely to increase considerably by the time a five- or seven-year term expires. While it is generally easier to negotiate *deconversion* pricing up front, if your bank plans to acquire another institution during the term of the contract, it is worth a conversation with your vendor to see what deal might be struck regarding converting a target onto your platform down the road.

Exclusivity

But what if your institution plans to keep two contracts in place following an acquisition (even if just temporarily)? Most contracts for major services contain exclusivity provisions that prohibit the bank (or enterprise) from obtaining similar services from other vendors. Both sets of contracts should be reviewed to make sure no exclusivity provisions will throw a wrench into the banks' plans, and the parties should start discussions with vendors early if there are.

Records, Records, *Records*…

Anyone who has longstanding relationships with their biggest vendors knows that contracts change over time. Vendors merge, master agreements change, product schedules are added and terminated – all of which can result in a cobbled together mess of contracts (which are then stuffed into a scary drawer where you will not need to think about them very often). While most banks have become more adept at vendor management in recent years, figuring out what exhibits, schedules, and addenda are actually part of your current contract can be challenging. If an M&A event might be in your bank's future, do yourself a favor now and be meticulous in your record keeping. I assure you, this is preferable to spending a couple of days digging through that scary drawer (or paying your attorney to do it!).

Conclusion

M&A can seem like a strange thing to plan for when there is not an actual transaction on the horizon. But given the impact of vendor contracts and services in M&A transactions, shifting shareholder priorities, and a reawakened market for bank transactions, it has become something prudent for all bank management to consider. When you start negotiating a transaction and the subject of communicating with vendors and consolidating services comes up, watch the other party breathe a sigh of relief when you say, "Don't worry, we've got this."