

The



*Opening the door to new ideas*

# Chairman's Forum

Newsletter

**Gerrish McCreary Smith, Consultants and Attorneys**

*November - December 2016*

As we come to the close of another year, we reflect back on the numerous meetings, seminars, and consultations we have had with Chairmen and other board members over the year. In particular, the recent Annual ICBA Community Bank Chairman's Forum we hosted in Napa Valley was a huge success and we appreciate everyone attending and for the highly insightful and informative discussion. In this month's edition of *The Chairman's Forum Newsletter*, we will be highlighting some of those thoughts and comments.

As you look to guide your institution in the new year, there is much to be thankful for in this past year. From a banking standpoint, the economic, political and regulatory forces have all calmed a bit and we have generally seen banks producing greater income for their shareholders. However, in the midst of those improvements, the roles of board members and the Chairman of the Board, in particular, continue to evolve with even greater expectations being put upon the individuals serving in those capacities. Accordingly, we hope that our Forums, and this Newsletter, are serving as a source of ready information for you for your important tasks. We look forward to continuing to provide more information in the new year and hope that this month's *Chairman's Forum Newsletter* provides additional insights as you wrap up your year.

Happy Reading, Merry Christmas and Happy Holidays!

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## **Chairman's Summary**

- ◆ Distinguish between Executive Sessions and Executive Committees.
- ◆ Who is the ideal director?
- ◆ Can you remove a director?
- ◆ Have an appropriate Capital Plan.

## **Executive Session or Executive Committee?**

Recently, we have run into a couple of situations in different parts of the country where Boards of Directors were struggling with appropriately defining what their board does and how it should be accomplished. In particular, the question has come up from a few Chairmen as to the appropriate distinction between using an Executive Committee versus holding an Executive Session. They are really two entirely different animals.

The Executive Committee is in fact a committee of the Board of Directors and is often one of the standing committees established. Its primary purpose is to be able to act typically in an emergency situation in lieu of the full Board of Directors acting and to handle special matters of consideration at the highest level. Typically, the Chairman of the Board

would serve as Chairman of the Executive Committee, it would contain at least some outside directors, and typically also includes the President or Chief Executive Officer if that individual is not also the Chairman. It would typically meet on a special needs basis, keep regular minutes and handle other functions like a typical committee. Subject matters that it might handle may include acquisition matters (if there is not an M&A Committee); board or management succession issues; confidential matters, perhaps dealing with fraud in the bank or similar items; strategic planning concerns; and other matters.

On the other hand, the Executive Session is primarily intended to be a somewhat informal meeting of only outside directors, typically held before or following a regular Board of Directors meeting. Normally, some limited agenda may be utilized and cursory or topical minutes are maintained, but not detailed or formal information as with regular board committees or the board meeting itself. Formal decisions are typically not made during Executive Session. The purpose of the Executive Session is to allow the independent outside directors the opportunity to discuss any and all matters they choose outside of the purview of the management team, to allow them to appropriately exercise their fiduciary duties of independence from, and oversight of, the management team. Following the Executive Session, the lead outside director, who typically runs the meeting, should report any discussions to the President and CEO. It is not a secret meeting, but rather merely a separate meeting of outside directors to improve overall corporate governance.

## **Job Requirements for Directors**

At the Chairman's Forum, one of the topics that was discussed was the retention of directors and the recruitment of new directors. In particular, we looked at the core issues of what a director really does, what are their job functions, what are the requirements of the position, and similar topics. Among the prevailing thoughts about what constitutes the ideal director were the following items:

- Directors should own stock in the organization he or she supervises;
- Directors should not be afraid of yearly performance evaluations;
- Directors should have written job descriptions;
- Directors should be required to have a minimum number of educational hours each year;
- Directors should maintain the strictest of confidentiality;
- Directors of community banks should be part of and active in the communities they serve;
- Directors should seek to refer business to the bank;
- Directors should be compensated for their board service.

Considering that list, which is certainly not exhaustive, ask yourself, as Chairmen, "Do I have ideal directors?; Do we need to impose director qualifications and have them in a written job description?; Do I lead by example in these areas?; Do we need to implement additional job

requirements?; What do I do with directors who do not meet these standards?''.

Keep in mind that if you are not holding your directors accountable to the same standards that your shareholders and your regulatory agencies would demand, then you are exposing the director to potential future liability when things do not go well.

### **Handling Director Misconduct**

As Chairmen, how would you handle areas of director misconduct? The simple answer is we would remove them from the Board. But, the question becomes, "Is it that easy?" Some Chairmen find that their corporate documents (Articles of Incorporation and Bylaws) have historically been written in such a way that it becomes much more difficult to remove a problem director or one subject to misconduct than you might think.

Consider, for example, does the Board of Directors, by a majority vote, have the authority to remove a director who has been elected by the stockholders? If your Articles and Bylaws are silent on the removal of directors, what does state law say? Do you know if your Articles and Bylaws are consistent with what your state law provides or, for national banks, what the National Bank Act provides? What if a director is engaged in "misconduct" but it is not technically illegal? For example, in states that

have legalized marijuana, would there be a problem with directors being seen in establishments that sell the product? While not illegal, you might find it causes reputational damage to the institution.

Similarly, consider whether a director is caught engaging in an affair with an 18 year old member of the opposite sex that leads to the director's divorce. Is that "scandalous" enough to result in the director's removal? Or, more importantly, do your Articles and Bylaws even address those types of circumstances? If there is no provision to remove a director for reputational damage to the institution, your only recourse may be to wait until the next shareholders meeting and not re-nominate the director or hope shareholders vote against the director. The key here is to ensure that your corporate documents are up-to-date and that you have them reviewed periodically for these types of crisis circumstances before they actually arise.

### **Make Capital Planning a Priority**

In the past several years, when we have thought about the Chairman's role in capital planning, we generally thought about being responsive to the regulators to ensure that we have a sufficient amount of capital to meet the minimum requirements or to ensure that we have developed a written Capital Contingency Plan if things go wrong because the regulators have demanded it in an enforcement action. However, as we look to the new year, it is appropriate for organizations of all sizes to have a strong Capital Plan that is forward-looking in terms of growth and development of the bank for capital needs rather than as a minimum benchmark.

Accordingly, the Chairman should be asking the management team if the organization perhaps needs to consider conducting an offering of new shares (either to existing stockholders or to new stockholders) as a way of having more capital resources that the bank can grow into rather than being limited in your asset growth plans by what may seem like an artificial boundary of maintaining minimum capital levels. With a recent presidential election behind us, there generally seems to be an environment in the financial institutions world that we will have some improvement in interest rates, we may have less regulatory burden, there may be new opportunities for growth and expansion and, accordingly, as Chairman you may want to be prepared to take advantage of potential growth opportunities in the new year by having sufficient levels of capital. This may also give your stockholders the opportunity to buy more shares to increase their ownership stake for what they hope will be a positive future. So, make capital planning part of your overall strategic plan, not just for regulatory purposes, but for future growth prospects as well.

## Meeting Adjourned

We appreciate those of you who are our clients for allowing us to represent you this past year and we look forward to renewing our acquaintance with you in the coming year. For the rest of you, we hope to have the opportunity to work with you in the future, but, regardless, we hope you continue to receive good advice and feedback on your very important job as Chairman of the Board. Wishing you all a very Merry Christmas and Happy Holidays, we will be in touch again in the New Year!

Until next time,



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and



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