



THE

Board Chair Forum

Opening the door to new ideas

NEWSLETTER

Gerrish Smith Tuck, Consultants and Attorneys

July 2020

In this month's edition of the Board Chair Forum Newsletter, we look at some recurring challenges Boards often have dealing with executive sessions and how to manage them. Likewise, we consider how the M&A market is being impacted by COVID-19 and national events, and how the form of consideration has shifted in light of these developments.

We also take a look at risk for your organization from two interesting angles. First, from the standpoint of enterprise risk management, we consider the type of lending in which you might want to engage. For this analysis, we look at the example of a bank that is somewhat on the cutting edge with what many of you would perceive as a highly risky venture, yet they view it as more safe than what your loan portfolio probably looks like.

Finally, we conclude by looking at risk from the standpoint of strategic risk going forward, and we take an interesting look at how banking may need to look to other industries, such as the fast food industry. Perhaps we should begin modeling what a "new normal" might look like once the crisis mentality subsides. We hope you find these items informative and interesting.

Happy Reading!

Jeffrey C. Gerrish

Philip K. Smith

Greyson E. Tuck

*Gerrish Smith Tuck
700 Colonial Road, Suite 200
Memphis, TN 38117*

Phone: (901) 767-0900; Website: www.gerrish.com

Copyright © 2020 – Philip K Smith

Any accounting, business or tax advice contained in this communication, including attachments and enclosures, is not intended as a thorough, in-depth analysis of specific issues, nor a substitute for a formal opinion, nor is it sufficient to avoid tax-related penalties. If desired, Gerrish Smith Tuck would be pleased to perform the requisite research and provide you with a detailed written analysis. Such an engagement may be the subject of a separate engagement letter that would define the scope and limits of the desired consultation services.

Gerrish Smith Tuck, Consultants and Attorneys
July 2020

Board Chair's Summary

- ◆ What Is Your Risk Tolerance?
- ◆ M&A Moves Toward Cash
- ◆ Use Executive Sessions Properly
- ◆ Fast Food Restaurants and Branch Banks
- ◆ Meeting Adjourned

What Is Your Risk Tolerance?

You should know by now that the Board of Directors is ultimately responsible for establishing and managing the organization's overall risk profile. We often hear the buzz words such as "enterprise risk management," "fiduciary duties," and "sensitivity to risk" thrown around, and we inherently know that the Board has a responsibility in those areas. However, as the Board Chair or as a member of the Board of Directors, how often do you strategically think about how much risk you want to undertake? We suggest those types of board risk evaluations should occur at a minimum once a year, and more likely, once a quarter.

So, if you set about trying to determine the organization's overall risk profile, what is a risky activity and what is not? A recent article in one of the trade journals points out just how differently people can view elements of risk. For example, there are plenty of banks around the country that in one form or another have the word "Farmers" in their title. Is it risky to lend in the agricultural sector?

Is extending an operating line of credit for a local farmer risky? Many of us would probably not think so – that’s the way community banks do business. However, what would you think about a bank that is specifically focused on lending to professional poker players! Lexicon Bank in Las Vegas does just that. It is a new bank founded a year ago by a professional gambler (insert your own joke here) and it caters to professional poker players. Many of us would not think of doing that in our wildest dreams because of what we would perceive as the risk inherent in doing so, if not the overriding compliance burdens. But this bank likely views lending to farmers riskier than lending to gamblers.

The banker running the show seems to think the risk is manageable. As he points out, professional gambling winnings are publicly posted, you can track the players’ participation in tournaments more easily, match it to their deposit entries, and the like. According to the bank, if you know poker, it is actually easier to scrutinize than your typical retail business. So, the next time you are around the boardroom, ask your board members if they want to get into the low risk game of lending to professional poker players! Discuss and know what your Board’s risk tolerance is.

M&A Moves Toward Cash

Some of you may be surprised to hear that the M&A market is still functioning. There are still banks looking to make acquisitions and target entities that are still planning their exit strategies. At least on that front the world has not (yet) stopped. However, in many of the transactions with which we are currently involved, there has certainly been a move toward creating more certainty in transactions. By its very nature, that means a movement toward more all cash deals.

It is not to say that if you are a buyer with a strong stock performance that no one will want your stock. And it’s not to say if you are a seller that under the

right circumstances accepting at least some stock in a transaction isn't favorable. But, the big question in today's market is, what is anyone's stock really worth?

For example, what is your Board's underlying feeling about the overall stock market in general? Will it be higher than it is now at the end of the year? Will it be positively or negatively impacted by the Presidential election? If someone made you an offer initially and their stock was trading at \$20.00 a share but now it has fallen to \$15.00 a share, should you still take the same number of shares even though the value has fallen? You can see how so many variables come into play and with all of the uncertainty going on in the markets and in our country, the M&A market typically moves toward greater certainty. As a result, we are seeing more sellers opting for all cash deals rather than rolling the dice on the value of some purchaser's stock. Keep those ideas in mind if you are a buyer or a seller, or even if you are simply trying to remain independent and enhance your own stock's value.

Use Executive Sessions Properly

An issue that we have discussed in the past but where we still encounter some practical application problems for Boards of Directors is in the appropriate use of an executive session. It is our belief that the Board Chair should insist upon executive sessions at least quarterly. But, ensure you are using them properly.

An executive session is a fancy way of saying that the outside members (non-management members) of the Board of Directors will meet in a formal session without management present. That includes not having the President or CEO present, even if he or she is also a member of the Board of Directors (which is often the case). The purpose of these special meetings is to simply allow outside non-management directors to discuss things going on with management, discuss their understanding of how meetings are being conducted, or generally to merely discuss things that help them exercise their fiduciary duties to stockholders.

Typically, we do suggest that minutes of executive sessions should be kept, although they should not be near as detailed as your typical board minutes. Often, we simply recommend that minutes of executive sessions outline topics that were discussed, or simply include an agenda of items discussed. Typical items might include review of CEO performance, strategic planning discussions, future growth and initiatives, etc. But, the most important thing to keep in mind is that executive sessions are really “discussion only” meetings. No formal decisions should be made at the executive session because your inside management who are members of the Board do have a right to be present and vote on substantive items. So, the executive session is not a secret meeting to get together and make decisions without the President or CEO. Rather, it is merely an opportunity for outside directors to have a formal discussion outside the purview of management.

Because these are not secret meetings, we wholeheartedly endorse the idea that immediately following the executive sessions or shortly thereafter, a designated individual (normally the Board Chair if he or she is not also the President and CEO) should report to the management the topics that were discussed at the executive session and any reporting to the CEO that would be appropriate. If the President/CEO is also Chairman of the Board, then a best practice is to appoint one of the outside board members as the “lead outside director” and he or she leads the executive session. Keep these ideas in mind for best corporate governance practices.

Fast Food Restaurants and Branch Banks

As we all continue dealing with the effects of COVID-19, we are once again seeing many banks closing lobbies, using drive-thru services only, developing greater implementation of technology for the benefit of their customers, and similar factors. Likewise, we continue to see many fast food restaurants that have not yet reopened their lobbies, have fully automated drive-thru facilities to handle curbside orders, typical drive-thru, or mobile-based apps

that allow you to order your food on your phone and simply pick it up at the drive-thru. From a Board of Directors and Board Chair standpoint, consider the similarities in these two businesses in many ways and think about the outlook for the future and whether it is time to rethink our models. Does anyone really go to a fast food restaurant because of the joy they have from sitting down inside the facility, mingling with the other elite clientele, and marveling at how spacious and clean the facility is?! Probably not. Likewise, are customers coming into your bank branch lobbies because of the wonderful carpeting, the development of pens on chains in the 1960's, the wonderful row of teller windows that were added with the expansion in the early 1980's, even though you have fewer tellers now, or similar factors? Also, probably not.

So, while we intend this to be a bit “tongue in cheek,” give serious consideration to whether post-COVID customers will have grown accustomed to the automation provided through drive-thru services, closed branch bank lobby hours, and similar modifications. Are you really any worse off because your lobby was closed at some of your branch locations? If you were to build a new branch, could you get by with only a third of the space you have in your typical location? Will some of these fast food places be so advanced in their technology and automation that they now can begin to open up drive-thru only facilities without any playground, or on-facility dining?

Many of us have taken drastic measures with our organizations by necessity and, as they say, necessity is the mother of invention. Is it time to take a hard strategic look at what we are doing with our branch banks going forward, and perhaps be ready for an entirely new dynamic once the storm passes?

Meeting Adjourned

Well, it normally would be that time of year again when we mention that schools are about to be restarting. But are they? It seems in every part of the country no one knows for certain. Some colleges are starting back, others are not.

Some are going to online classes, others are not. High school students are a bit in limbo and none of us can really predict what tomorrow brings. In the midst of all this uncertainty, the Board of Directors and the Board Chair can continue to add stability to the organization through level-headed decisions, avoiding a panic mentality, and continuing to focus on shareholder needs. We hope this newsletter helps you in that regard.

Until next time,



Jeffrey C. Gerrish



Philip K. Smith



Greyson E. Tuck

*Gerrish Smith Tuck
700 Colonial Road, Suite 200
Memphis, TN 38117
Phone (901) 767-0900
Website: www.gerrish.com*

HOW TO CONTACT US:

If you have questions or comments about the newsletter or would like to ask a follow-up question, please email Philip Smith at psmith@gerrish.com.