THE

Board Chair Forum

NEWSLETTER

Opening the door to new ideas

Gerrish Smith Tuck, Consultants and Attorneys

October 2020

As we are in the midst of the fall strategic planning season, this issue of the Newsletter takes a number of circumstances that we have seen at recent planning retreats and describes to you how those are being impacted by the current state of affairs. We also look at best practices for your Board in terms of executive sessions, strategic planning, and the like.

You will also see some commentary regarding change, the use of technology, and even revisiting some of the most basic structures of your organization that may be subject to change now. For example, when was the last time you looked at the hours of operations within your organization?

In these unusual times, the role of the Chair and other board members is certainly not getting easier, but because of the uniqueness of circumstances and the everchanging dynamics in our markets, it is also safe to say there is no right answer since we are all somewhat feeling our way through this. But leadership never goes out of style. Keep working hard, keep focusing on creating the best boards you can, run your bank in a safe and sound manner, and all other things will fall into place. We hope you find some useful takeaways in this month's edition, and if we can help you, please let us know.

Happy Reading!

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Board Chair's Summary

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- Can You Keep Your Branches But Modify Them?
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A Continuing Focus on Reducing Branches

Since our last newsletter, there have seemingly been a daily list of articles about more and more banks across the country closing branches. In one Friday edition of the *American Banker*, there were three different articles about organizations in Pennsylvania, Oregon and Washington State each closing branches. The bank in Washington was closing 20 branches, the Oregon bank up to 50 branches. Why do you think that is? How in the world can an organization make such drastic office location closings and still find itself relevant? Does the branch closing efforts leave its customers, its communities, and its stockholders with a feeling that these organizations are underperforming, on the brink of massive losses, are bailing water in an effort to keep the regulators at bay or to keep from failing? No! None of that appears to be the case, nor is there any kind of negative reaction to the massive branch closings we are seeing by larger organizations across the country.

Interestingly, those organizations that are publicly reporting institutions with a publicly traded security, often find that that the news of massive branch closings is met by an uptick in their stock price. Why is that? The reality (which sometimes is difficult for smaller banks to face or to realize) is that in the publicly traded market these types of actions are viewed as difficult but necessary strategic decisions which result in huge cost savings and a reallocation of investment out of fixed assets for locations perhaps into a separate category of fixed assets for technology investments and other "upgrades." So, what can smaller banks learn from those actions? We think there are a couple of ways to think about this.

First, a smaller bank might very well find some opportunities to acquire one or more branches of a larger organization that is pulling out of a particular market. Often, the depositors will stick around even if someone else acquires the branch because of the difficulty of converting and low cost deposits are certainly a great resource for funding your own growth in other markets. Secondly, if you happen to be in one of the markets where the branch of a larger organization is closing, take the opportunity to emphasize the uniqueness of community banks in remaining in communities, continuing to serve local customers, and not pull out of markets. Do not miss the opportunity to seize on a great marketing tool for your organization that you are still dedicated to your community when others are leaving.

Finally, we think it should also cause you to reevaluate your own branch network and branch structure. Even as a small bank, you may, for example, only have a few branch locations, but maybe you can really still operate with even fewer. We certainly do not want to act and behave merely according to whatever the largest banks are doing, but we can no longer, in today's environment, continue operating with excessively high efficiency ratios where we remain overstaffed and have excessive investments in premises and other fixed assets. So don't hesitate to critique your own branch structure to determine if it is optimized.

Can You Keep Your Branches But Modify Them?

Perhaps it is not going to work for your organization to close or eliminate branches. In fact, we hope you do not see the necessity to do that. But maybe it is time to also reevaluate how the branches are functioning. Over the last couple of months as we have moved into the fall strategic planning time, it has become apparent to us that as we evaluate how banks have coped with the COVID-19 fallout, most organizations limited lobby hours or closed lobbies or locations for some period of time. The interesting result of that, though, is that most of those organizations did not experience a dramatic dropoff in the number of transactions per branch. Rather, the customers either began to utilize an online banking platform, use the drive-thru facility more, or took similar actions. The result is that many community banks, in particular, are finding that they can operate effectively and efficiently with remote access, less lobby traffic, greater emphasis on their online resources, and other mechanisms.

We have had at least one client who is modifying a couple of branch locations to add additional drive-thru lanes while it continues to limit office hours. Perhaps what is old is new again and we will continue to see more drive-thru business. In addition, this bank made a good point as to why it was investing the time and effort to refocus on drive-thru facilities. Unlike in the old days when it was a waste of time to wait in a long line at a drive-thru facility, these bankers made the comment that since everyone is now "on their phone," pulling up to a line of cars and anticipating a 10 minute wait is not a big deal at all because it gives you time to check your email, communicate with other people, keep your business going, etc. A point well-taken that in our multi-tasking environment, a short wait at the drive-thru with your phone in hand may not seem like much of an inconvenience to our customers at all. So, let's rethink how we are using our locations and it may be that some of our offices permanently reduce lobby hours or permanently allow remote working for designated employees.

Bankers Hours Revisited

A final word on branches that is an interesting consequence of the current environment relates to office hours. Community banks in particular are notorious for not having standardization of office hours. One location may be open 9:00 to 4:00, another location is open 9:00 to 4:00 except they are open 4:00 to 5:00 on Fridays and 11:00 to 2:00 on Saturdays. Another location may open early at 7:30 and close on Fridays at 6:30, but on the fourth Tuesday of the month they are also open on Wednesday until 3:35 p.m., etc. You see what we mean. This is not unusual for community banks at all, and occasionally we are beginning to see that has unintended consequences of low employee morale in places, difficulty of rotating customer service representatives for Saturday hours, and other things. So, it may be time to reevaluate even the most basic of issues such as branch hours to determine if, with new investments in technology, more remote capabilities and the like, a standardization of hours and even the possibility of closing lobbies on Saturdays makes sense in order to be more competitive and create more shareholder value through more cost savings. In fact, the way you would market it would not be that you are reducing hours, but, rather, you are going to 24/7 banking through the use of your new online app, remote deposit capabilities, online applications, and the like. The argument is that you are expanding the hours through investments in technology. If you are concerned that you will lose all of the drive-thru traffic you normally have on Saturdays, we would suggest that once you make the change you will simply find that those individuals are miraculously able to come by the bank on Fridays. Just as we initially thought with the onset of COVID that closing the lobby would reduce the number of transactions, we are finding that customers are much more adaptable than we thought and they will simply find other ways to continue to do business with you, because of all the positive benefits you otherwise bring to the table. They are not going to leave and pull their account and go to another organization just because that entity offers the ability to walk into the lobby on a Saturday from 11:00 to noon.

Strategic Planning: Balancing Technology and Timing

In last month's edition of the Board Chair Forum Newsletter we talked about being ready for change and that when change is so unpredictable, it may not be that you are always ready for change, but you can adopt an attitude and a structure that allows you to adapt to and implement change quickly. The key is to be ready for the pace of change. We have seen that become more evident in our fall planning sessions. Take for example, a recent client where we facilitated their strategic plan in the fall of 2019 and we were back recently for the follow-up in 2020. At the 2019 session, there was discussion around implementing new types of technology, trying to use it to attract new customers, and the like. In particular, the organization agreed that from a timing standpoint, they should probably begin the process of thinking about using an "e-suite" of products such as electronic signatures, online applications, and the like. As a result, the thought was that sometime over the next two years they would begin to fully adopt and implement those types of new technologies.

When we followed up at the 2020 planning session, guess what? All of those items had been dramatically accelerated and the bank had already implemented them, and was beginning to reap the benefits of the change. The pandemic and the crisis created a greater customer need, and a greater bank willingness to move forward and expedite the timeframes for implementing strategies. So, while this bank was not really planning to move that quickly, circumstances changed that necessitated a recalibration of the strategic plan, including a focus on the speed at which they were going to begin implementing things. A very positive move by this bank to not be concerned that the strategic planning document says we are doing it over the next two years, when it really needed to be implemented immediately. Be ready for the pace of change to move more quickly than you are expecting.

Strategic Time Horizons Are Shrinking

As Chairman of the Board or as Directors, you may also want to focus on timing considerations in a number of other areas that may be brought on by the pandemic. For example, what about board succession plans or management succession plans? An open dialogue with fellow board members about their health, their outlook for the future, their desire to remain as board members, their desire to sit for reelection, and other factors, would be appropriate. The unique times we are living in are forcing everyone to rethink their business and personal lives and it may be an appropriate time to have those discussions so that appropriate succession planning can be accomplished. Likewise, that flows into management succession and ownership succession as well.

Consider also, if individuals within your organization are considering early retirement. If so, it can create an emerging liability for an organization if the individuals are heavily invested in an employee stock ownership plan or the organization otherwise faces funding issues for retirement benefits. So, there may be the unintended consequences of a capital crunch, or at least a capital decision to be made in light of the changing environment as well.

Keep the Executive Out of Executive Sessions?

A recurring question we often get relates to the best corporate governance approach toward holding executive sessions. The executive session is intended to be a meeting of non-management, outside board members only. But how do you manage that process if the President, CEO, or other officer is also a board member? Can you keep the executive out of the executive session?

The concern, rightfully so by the executive, is that he or she is a board member and should be able to be present at all meetings of board members, notwithstanding that the individual is an officer. That argument often flows from the idea that they have an equal vote with other board members and therefore should not be excluded from any decision making. While those are valid arguments, if the executive session is handled appropriately, fears can be calmed and the session can be productive without causing board difficulties.

First of all, recognize that the executive session of the Board of Directors is intentionally meant to exclude officers so that outside "independent" board members can meet and discuss things among themselves without the influence of members of management. So, no members of management should be present, regardless of whether they are also a board member. But, most importantly, the Chairman should clarify what can and cannot occur during an executive session. Foremost, what cannot occur is any actual decision making. The executive session is merely intended for discussion points among outside board members, but no actual decisions can or should be made. Therefore, the management members who are board members are not excluded from actual board discussion leading to a decision.

Keep in mind, also, executive sessions are not secret meetings. They should be regularly occurring meetings where the officers who are directors know about them and are advised immediately or shortly following the meetings as to the content of the meetings, any key discussion points and the like. Often, it falls to the Chairman of the Board to sit down with the President or CEO and discuss the items that were brought up during the executive session.

Finally, it is important to keep minutes of the executive session, but only in a summary format, in our opinion. We generally recommend that minutes be topical rather than detailed. For example, the minutes may simply suggest that the outside directors met in executive session and discussed topics including executive compensation and other issues. Again, this would not be detailed minutes, but simply a record to reflect the meetings were held and that certain items were discussed. In this fashion, the Board exercises their fiduciary duties and the management is protected from a board making decisions without them.

Meeting Adjourned

We want to remind everyone, again, about the upcoming Board Chair Forum to be held as a live, in-person event at the Ritz-Carlton in Naples, Florida, January 14 and 15, 2021. We will be making sure we have plenty of room for social distancing, wearing masks where appropriate, and taking other protocols that may be necessitated in the coming months, but we felt it important to continue to hold this live event. We have already had great response and are getting close to our capacity since we will be limiting total attendees, as you might expect, but there are still some spots available and we would encourage you to sign up early so that we can make appropriate arrangements with the hotel consistent with COVID guidelines. You may register or find out more about the event which is sponsored by the Barret School of Banking, in conjunction with our firm, at the following site: Community Banking Chairman's Forum.

It seems we are all in a bit of a quick push toward the end of the year and there are still lots of bank activities ongoing. We also recognize that in the remaining two months of the year, many of us may be simply looking forward to getting 2020 behind us and hoping for a brighter outlook in 2021 on a host of different fronts. Hang in there a little bit longer and we will all come through this together.

In addition, this will be the last edition of the Newsletter prior to the upcoming Presidential election! That event may also hold hope or gloom for you depending on your outlook and depending on the outcome. We here at Gerrish Smith Tuck can confidently say, without hesitation, and with 100% certainty, that the winner of the Presidential election will be . . .

Until next time,

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