The

Board Chair Forum

Opening the door to new ideas

Gerrish Smith Tuck, Consultants and Attorneys

December 2024

Christmas, Holiday and New Year's Greetings! What an interesting year 2024 has been! From interest rate concerns to continuing merger and acquisition activity, the proliferation of credit unions continuing to try to enter the community bank space, regulators being regulators, and even a Presidential election that surprised many people because of the margin of victory, we can certainly say that the past year has not been dull. We hope that you and your organization have weathered the storms, enjoyed the good times, find rest during the holidays, and are looking forward to the new year.

As we have done the past two years, we will revisit the holiday classic, *It's a Wonderful Life,* remind you of some of the previous takeaways, and highlight some new issues to consider that we hope you will find both entertaining and beneficial for your organization in the coming year.

So, as always, grab your favorite holiday snack (pumpkin chocolate chip muffins, anyone?) and let's dive in, once again, to one of America's great Hollywood classic movies and see what we can learn!

Happy Reading!

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Board Chair's Summary

We begin our December edition of the Board Chair Forum Newsletter by giving a small background summary of the movie, *It's a Wonderful Life* so that everyone is aware of the key premise involved. Here is the common background again this year.

It's a Wonderful Life **is a 1946 American Christmas film produced and directed by Frank Capra and starring Jimmy Stewart as George Bailey, a man who has given up his personal dreams in order to help others in his community. However, George's thoughts of jumping off a bridge on Christmas Eve bring about the intervention of his guardian angel, Clarence, who shows George all of the lives he has touched and what the world would be like if George did not exist. But, with that overview and summary of the movie plot, don't assume this is just some touchy/feely holiday classic you can put on in the background. This movie has a wealth of information applicable to community banks, directors and the Board Chair! So, set forth below are a few key takeaways (some old and some new) for financial institutions from** ***It's a Wonderful Life.*** **We hope you enjoy this discussion and find some great learning opportunities. Consider these questions:**

- ***Where Was the Board?***
- ***Was Mr. Potter Wrong?***
- ***What Was Potter's Plan for the Future?***

Where Was the Board?

In the movie *It's a Wonderful Life,* the one group that does not get perhaps the attention that is needed is the Board of Directors of the Bailey Building & Loan. Keep in mind, this Board was the typical community bank board comprised of local businessmen apparently from the Bedford Falls area. And yes, given that the film came out in 1946, this was your very typical community bank board which, as many of you have heard us say over the years, was male, stale, frail, and pale! There wasn't much diversity in terms of gender, age, or anything else for that matter. In fact, the biggest concern might be the lack of diversity of thought on the Board. Is that sometimes the problem in your organization?

We often talk about the benefits that boards of directors can have by having more diversity. However, the diversity that is often most needed is diversity of thought so that we do not fall into "group think" and simply go along to get along. That often leads to the directors all following each other "right off the cliff." Occasionally, if not consistently, we need directors to stand up and articulate a different point of view or raise alternative ideas and thoughts if, for no other reason, to spur creative and strategic thinking.

If you recall from the movie, we have harped for the past two years on the fact that the organization did not do a good job of succession planning, and when George Bailey's father dies unexpectedly, there is no real succession, so the Board seems intent on simply selling the bank. It appears none of the directors are willing to suggest an alternative course of action except for one key director, Old Man Potter. He has a solution – he'll simply buy up all of the shares of the bank from the directors and other stockholders. The Board seems to be willing to let him do that until George, who has apparently on an interim basis stepped in and helped manage the organization in the immediate aftermath of his father's death, and who is apparently not even a shareholder, comes to the Board and makes an impassioned plea to the Board not to sell to Potter. So, the Board of Directors appears to have two choices. They can sell the bank to Potter (setting aside for a minute the potential for insider dealing, breach of fiduciary duties and the like from Mr. Potter as an existing director and stockholder taking advantage of a crisis situation), or the Board can refuse to sell to Potter or to anyone else, take back control of the organization, and try as best they can to maintain its independence over the long run. They, of course, wind up going to George Bailey and telling him if he will step into his father's shoes and take over the job running the organization permanently, they will vote against Potter and will keep the bank independent.

Why would the Board put a family member in such a difficult position? Frankly, that is not all that unusual and we have seen plenty of community and family bank situations across the country where it was clearly made known that if family members did not continue to step up and help run the bank, that it would be sold. Is that appropriate for a Board? Why hadn't the Board insisted on better succession planning? Should the Board have adopted a policy that no insider can acquire a greater percentage of shares than some set amount? Did anyone tell Mr. Potter that if he attempts to buy shares as an insider at a discounted price, that he may have income tax treatment on the value of the shares above the price that he paid? Where was the Board? Were they exercising their independent fiduciary duties or merely going along with whoever has the loudest voice at the time? It appears that they are willing to simply do whatever Potter wants when he is yelling the loudest. When George Bailey stands up and starts to shout, they change their minds and appear to swing their support behind him. Again, it seems this Board is a bit "rudderless," with no independent thinking by any of the individual directors, and they all tend to simply try to act as a group, appeasing whoever seems to be in charge at the moment. Can't we all learn something from that?!

Was Mr. Potter Wrong?

While Old Man Potter (fantastically played by the famous Lionel Barrymore) is certainly portrayed as the villain in the movie, is he wrong? The answer is yes, he's at least wrong in his attitude and approach and his view of how a community bank should run itself. But, just because we don't like his approach and attitude, or maybe even his mission for the bank, that doesn't mean his ideas are necessarily wrong or shouldn't at least be given some consideration. Again, as tough as it may be, does a board of directors of a community bank need to consider the input and opinion of "disfavored" board members? Keep in mind, Mr. Potter has been successful in his own businesses, he appears to approach things from a business-minded standpoint, he wants the bank to reduce its past due ratio and charge off loans that are bad rather than hoping customers will eventually pay. In addition, it is arguable that he truly believes he is doing a good service for people by offering to buy their shares rather than letting the regulators take over the organization where shareholders will lose all of their money. It also reasonable to assume he does not expect to lose money on the transaction, so he must clearly be anticipating recapitalizing the bank once he acquires it. You would assume he then wants to help it grow to the next stage of its life. So, technically speaking, Potter is not wrong in his actions to try to turn the bank around, but let's just say he has a different philosophical approach on how to do that. Doesn't that sound like some of our board members? Candidly, some of our boards might need a little more Potter and a little less George to occasionally get them through some rough patches, rather than being wishy-washy about the future. However, we certainly prefer George Bailey and his father's methods of running the bank and the culture they instilled in the organization better than Potter!

What Was Potter's Plan for the Future?

If you would allow us a little creative liberty, we would like to make some assumptions about things that were not directly explained in the movie, but certainly could have occurred, looking at the state of community banking currently. Potter was willing to "save" the organization by giving everyone 50 cents on the dollar for their shares. That would have put him in total control. Keep in mind, though, the bank still had a liquidity crisis because Uncle Billy had lost most of the bank's capital (which

Potter found and apparently kept for himself). So, Potter would have to recapitalize the bank himself. In addition, George clearly was not going to stay and work for Potter, and, although he was not happy that the Board was going to allow Potter to take over the bank, we would assume George was simply going to head out of town with his wife and pursue his dreams in some other city, forsaking the small town of Bedford Falls where he grew up and the community bank lifestyle. So what was Potter's next move?

He certainly would have had to find a new President/CEO. Our speculation is that the guy referred to in the movie as "his little bean counter" likely would have been installed on an interim basis to manage the affairs of the bank (it seems like he probably would have gotten along well with the regulators in the movie), Potter would have removed the board members who were loyalist to the Bailey family, and replaced them with likeminded men of his own persuasion, he probably would have then put enough capital in to get the regulators off his back and began a process of growing the bank. Is that such a bad thing for Bedford Falls? In the time of the movie, residents of Bedford Falls likely would not have had other places to borrow money. There was no internet, most lending was confined to local communities, and the movie even indicates that Potter had acquired or was attempting to acquire the other bank in town that was having problems as well. Perhaps Mr. Potter was trying to grow the bank to a sufficient size that he could get one of those very lucrative credit union offers to acquire his new "toy." After all, Potter does not really care that the community banking model that the Baileys set up is followed. He is looking out for himself! Our only hope is that if Potter is acquiring all the shares, hopefully, he at least had to deal with the way the friendly federal regulators have been acting this past year, requiring numerous and sometimes ridiculous change-in-bank-control filings, mandating information about Mr. Potter's ownership and practices dating back decades, and requiring antiquated filings that have no real bearing on his current ownership. Sound familiar to anyone?

The bottom line is that we don't really know what Mr. Potter's plans were, but you can rest assured that whatever course he took was likely not in the best interests of the customers and communities that the Bailey Building & Loan served. We do assume if he had acquired control, that he would have applied for a name change for the organization. Perhaps he would choose "The Potter Pillage and Pay"!

So, once again, the movie points out the benefits of long-term community bank independence when we realize that George did agree to take on a management succession position, wound up staying long-term, greatly benefitted himself, his family, his community, and the multiple parties he served. As a result, it truly was a wonderful life for George Bailey.

Meeting Adjourned

It's a Wonderful Life shows us that the Board has a role to play that may require action rather than passivity. The Board Chair has a role to play in standing up to directors that are being difficult, causing problems, or obstructing the smooth operation of the organization (keep in mind Mr. Potter apparently was not the Chairman). But we also must recognize that differing points of view can be a source of strength, not a liability, if they are managed appropriately, so all directors should have an independent mind and voice in the affairs of the organization.

Finally, the community bank Board should consider the long-term prospects of the strategic actions it takes. If the Board fails to require management to plan for succession, if the Board allows a stockholder they don't particularly care for to acquire increasingly large amounts of stock, it can create future problems. If the Board doesn't focus on core banking principles like organizational liquidity, the organization runs the risk of regulatory concerns. But, notwithstanding all of those potential headwinds, we end with the line we have ended with the past two years because we believe it's true: The life of a smalltown board, the life of a community-based financial organization, and even owning stock in a community bank, can truly present a wonderful life for the individuals, the organization, its employees, customers, and the communities that it serves. It is truly a wonderful life to be a community banker and it is truly our blessing to have the opportunity to continue to represent community banks and to have so many of you as our clients and friends. Merry (post) Christmas, Happy Holidays, and wishing you a wonderful, prosperous and blessed New Year!

Until next time,

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