
GERRISH'S MUSINGS

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Dear Subscriber:

Greetings from Tennessee, Indiana, Illinois, Kansas, Ohio, Wisconsin, Pennsylvania, Iowa, Missouri, West Virginia, and Kentucky!

A DYSFUNCTIONAL BOARD

We have often written over the years in Musings about what we view as dysfunctional community bank boards. Fortunately, these are relatively few and far between. We ran into an unusual situation a few months back where a community bank board of directors had a disagreement on a significant issue and actually had a split vote, where a little better than a majority of the board wanted to move in one direction and the remainder of the board wanted to move in another.

One of the outside directors asked us whether they now qualified as a “dysfunctional board.” Our answer was no, not at all. What the board exercised was its ability to have robust discussion and disagree on even the most basic issues, yet do so with candor, civility, and honest respect for each other. That is the opposite of a dysfunctional board.

The dysfunctional board is one that consists of members who disagree, hold grudges, have underlying, undisclosed agendas, parking lot meetings regularly, take things personally, and put their own best interests above the best interests of the bank. That was not this board at all.

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CAPITAL RAISING CONSIDERATIONS

We recently had an interesting discussion with a Board of Directors as it relates to the right time to raise capital. This particular bank was not in immediate need of capital. However, the general belief among the board was that capital will likely be needed sometime in the next five or so years. This will be to support growth and promote stock liquidity through share repurchase transactions.

The issue the directors wrestled with is when is the right time to raise capital. The bank is currently performing well, and is not in need of capital today. Given the bank's strong performance, certain of the directors advocated for raising capital today. Other directors took a different view, indicating that the holding company should wait to sell equity until closer to when it is needed, because the presumption is that the per share sales price will be higher at that point, allowing capital to be raised with less dilution to existing shareholders.

The conundrum is not one that is unique to this community bank. Many *Musings* readers have likely heard the comment that the best time to raise capital is when you don't need it. Of course, the counter to that argument is why raise capital and dilute your existing shareholders when you don't have a current need. This is the capital conundrum, and one that many boards wrestle with as part of their strategic planning process.

SUBORDINATED DEBENTURES

We are beginning to see a renewed interest in bank holding companies issuing Subordinated Debentures for capital raising purposes. If you are not familiar, Subordinated Debentures are typically a 10-year interest-only debt. The interest rate is typically fixed for five years and then floats for five years. The debt is unsecured and requires a bullet payment of principal at maturity. (Please note that for community banks less than \$3 billion in total assets, the "subordinated" part of the subordinated debt is not necessary.) What is necessary is to generate cash in the holding company that can be downstreamed into the bank as capital or kept at the holding company for other corporate purposes.

We assisted many bank holding companies in issuing Subordinated Debentures from about 2021 to 2023. When rates began jumping up, interest in Sub Debt as a capital raising alternative waned. Now that rates appear to be heading down rather than up, interest in issuing Sub Debt seems to be returning.

If your holding company is looking for cash to increase bank capital, repurchase shares, support an acquisition or other uses, Subordinated Debentures may be an appropriate strategic alternative. The rates are coming back down, and we are currently seeing five-year fixed rates in the 6% to 7% range.

THE MOTIVATION FOR GROWTH

We facilitated numerous strategic planning sessions over the fall where the discussion has involved the pursuit of growth. What is interesting is that growth means different things to different boards. Some boards talk about growth in terms of total assets, loans or deposits. Other boards talk about growth in net income. Others talk about geographic growth. Others talk about growth through the addition of new lines of business.

Our experience is that most community banks are looking to grow. Many boards seem to adopt the view of Big Tom Callahan in *Tommy Boy*, in that “you’re either growing or you’re dying. There ain’t no third direction.” If your board has this type of mentality, we see it as important not only to identify a desire to grow, but to also identify and define the type of growth your community bank is looking to achieve.

REGULATORY RELIEF

For most of the banks in the country, the FDIC is the primary federal regulator. For over 1,000 national banks and thrifts, however, it is the OCC. Both the confirmed Comptroller of the Currency of the OCC, Jonathan Gould, and the not yet confirmed Chairman of the FDIC, Travis Hill, are not only saying all the right things about regulatory relief, (you can review their speeches on their respective OCC and FDIC websites), but are actually causing their agencies to do the right thing.

A few weeks ago, Travis Hill, as Acting Chairman of the FDIC, indicated that his thought is that consumer compliance exams should be much less frequent than they are now, primarily because the agency is going to focus on financial risk, not process issues. Last week, the FDIC updated its Consumer Compliance Examination Schedule. That schedule is contained in a Financial Institutions Letter issued by the FDIC and indicates “Institutions will generally be on an examination cycle of 66-78 months, 54-66 months, or 24-36 months, depending on their asset size.” The bottom line of all this is a typical community bank may not see a compliance examination but once every five years. We don’t know that there is anyone in the community

bank arena that would be shedding a tear about that development, except possibly Compliance Officers. Even still, those Compliance Officers will continue to need to do their job, they will just be harassed on a less regular basis by the friendly federal regulators.

The bottom line is for banks that have good CRA and Compliance ratings, the examinations will be few and far between.

BOARD MICROMANAGEMENT

We have been getting a number of questions lately, both directly and as a result of meetings with community bank boards of directors, with respect to where the line is on board micromanagement. As most *Musings* readers know, the Board's job is to provide oversight to management, be a credible challenge to management, and the like. This is the "noses in, fingers out" philosophy espoused by many over the years.

One of the primary jobs of the Board of Directors is to select the CEO for the bank. It may also be to select the number two. Generally, the Board's job does not dip much below that unless there are unusual circumstances. In the perfect world, the Board would select only the CEO of the bank and that individual would select his or her supporting cast. If, however, an entire retool of management (i.e., management succession in a big way) is going to occur, then it is not unusual for the Board to be involved a little deeper down in the organizational chart. Is that micromanagement? We don't think so.

If a Board is seriously micromanaging, then that generally tells us that the Board does not trust its existing management and needs to find management it does trust. Since most board members in a typical community bank are not community bankers, having the board member trying to micromanage a bank when he or she does not fully understand the business is probably not the best way to enhance shareholder value. Just a thought.

REDEMPTION VALUES

We have recently had a number of different board discussions regarding bank holding company stock redemptions. As *Musings* readers know, we are big fans of bank holding company stock repurchase transactions. The bank holding company repurchase transaction provides a benefit to the selling shareholder in the form of receiving desired cash. It also provides a benefit to all the remaining shareholders in the form of increased ownership percentage, return on equity, earnings per share and dividends per share. In our view, it is a win-win for all involved.

One of the issues that almost always has to be addressed in a share repurchase transaction is the per share repurchase price. Many holding companies wrestle with this issue, because they do not have market trading that establishes a fair market value. In addition to this conundrum, another wrinkle that is often added in from a selling shareholder is that of what could be obtained in a sale of the entire organization.

Not surprisingly, some selling shareholders advocate that their shares ought to be repurchased at a price that would be received if the entire organization were to be sold. They often argue that they will not push for the sale of the holding company if they are paid at a level that would be received in a sale. The counterargument is that the minority position they represent is not a control position and does not warrant a higher purchase price.

In our experience, minority shareholders are typically bought out at minority prices. We do not typically see circumstances where a board believes it is appropriate or in the best interests of the remaining shareholders to pay a minority shareholder what is essentially a control premium that would be obtained if the entire organization, rather than the minority block, were sold.

THE BIG BANK THREAT

We have recently been assisting one of our community bank clients with a check fraud issue. The circumstances are such that one of the bank's customers deposited a check with all of the signatures of the payees. The bank followed the appropriate deposit procedures and protocol related to the deposit. Almost five months later, one of the nation's largest banks provided a notice of required refund to the bank based on an alleged fraudulent signature. There are multiple issues related to the circumstances, including the validity of the signature and whether the big bank's customer acted with "reasonable promptness" as it relates to the request for a refund.

We were recently on a telephone discussion with an in-house lawyer for the big bank. We talked through the various issues. Not surprisingly, we each took different views of the circumstances and the party responsible for bearing the loss. That is not a big deal, and we recognize reasonable minds can differ.

What we found notable about the discussion was the big bank lawyer's threat as to what would happen if our client did not refund the money. Simply put, the in-house lawyer said our community bank client would be put on this big bank's "do not pay list." The lawyer said that would mean the big bank would basically refuse to do any further business with the community bank, and would essentially refuse to remit payments and the like. The lawyer told us that this

would be extremely embarrassing for our community bank, and that it absolutely would “end badly” for them. We asked the big bank lawyer to put in writing exactly what was being threatened. As of distribution of this *Musings*, we have not received the requested writing from the big bank’s lawyer. We are not holding our breath that it will come anytime soon.

In our view, the lawyer’s actions were pretty egregious. We certainly recognize reasonable minds can differ over the party responsible to bear the loss associated with check fraud. We do not see it as appropriate for big banks to threaten to ostracize community banks simply for the hope of extracting a settlement related to a transaction. We wish it was simply the big bank lawyer having a bad day. Our expectation is that is probably their *modus operandi*.

CUSTOMER EXPERIENCE

Most community banks can be described as “relationship” banks. What that means is that the issues regarding customer experience are critical. At virtually every planning session we facilitate for a community bank, the customer experience discussion occurs.

The goal for most community banks is not just to have appropriate products and services, but make the use of those products and services by the customer “frictionless.” This almost by definition translates into a good customer experience, at least for the products and services utilized, not necessarily for the interaction with bank personnel.

One community bank we were recently visiting with had, over the years, established what they referred to as an “Obstacle Committee.” The Obstacle Committee’s goal is to do just what it sounded like, and that is identify and seek to eliminate the obstacles to a frictionless customer experience. We view that as a good way to approach the entire customer experience issue

CONCLUSION

It definitely appears that Winter is here in many parts of the country. This will be the last *Musings* before the Thanksgiving holiday weekend. We wish all of you a very happy Thanksgiving and some quality time with friends and family.

Stay safe. See you in two weeks.

Jeff Gerrish

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Upcoming Webinars and In-Person Presentations:

- November 14, 2025 – Oregon Bankers Association - Northwest Bank Directors Series - (Virtual) “Critical Information for Community Bank Directors and Officers” (Greyson Tuck, Presenter) Registration: [Critical Information](#)
- December 4, 2025 - Independent Community Bankers of America (Webinar) “Preparing Today for Community Bank Leadership Tomorrow” (Greyson Tuck, Presenter) Registration: [ICBA Webinar - Preparing Today for Community Bank Leadership Tomorrow](#)
- January 26-27, 2026 – Barret School of Banking, Community Banking Board Chair Forum at the JW Marriott Marco Island Beach Resort, Marco Island, Florida (Jeff Gerrish, Philip Smith, and Greyson Tuck, Facilitators) Waiting List: [Community Banking Board Chair Forum](#)
- January 29-February 1, 2026 -Southwestern Graduate School of Banking, Assembly for Bank Directors at The Ritz-Carlton O’ahu, Turtle Bay, Hawaii (Jan. 30) (Jeff Gerrish, Presenter) Registration: [SWGSB Assembly for Bank Directors](#)