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Mr. James P. Sheesley
Assistant Executive Secretary
Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429
comments@fdic.gov

Re: Guidelines Establishing Standards for Corporate Governance and Risk Management for Covered Institutions with Total Consolidated Assets of $10 Billion or More (RIN 3064-AF94; Publication Dates: 10/11/2023 and 12/04/2023)

Dear Mr. Sheesley:

The North Carolina Bankers Association (NCBA), the trade association for the banks operating in North Carolina and their approximately 100,000 employees, appreciates the opportunity to provide comments to the FDIC on the proposed Guidelines Establishing Standards for Corporate Governance and Risk Management for Covered Institutions with Total Consolidated Assets of $10 Billion or More (the Proposed Guidelines).

We noted the FDIC's goal with the Proposed Guidelines is to strengthen the corporate governance and risk management practices of large institutions, drawing from the lessons learned during the 2008 financial crisis and recent 2023 bank failures. We respect both this objective and the diligence that FDIC examiners and staff have shown to their responsibilities over the many decades of the agency's existence. Unfortunately, we believe that, if applied in their current form, the Proposed Guidelines would cause significant operational issues for banks and, contrary to the intent, have the net effect of undermining safety and soundness. For the reasons stated below, the NCBA urges the FDIC to withdraw the Proposed Guidelines.

Continuous Examination Process Already Provides Supervisory Tools

The FDIC's continuous examination process uses a $10 billion threshold. Looking back at the five bank failures that occurred in 2023, the FDIC identified the risks – such as liquidity risk management and vulnerability to interest rate changes – at banks like Signature Bank and First Republic well in advance of the failures. Rather than impose new corporate governance standards on already closely supervised institutions, the FDIC could more effectively use its existing regulatory tools like the continuous examination process, paired with supervisory recommendations and appropriate enforcement of matters requiring board attention.

Independent Director Requirements Will Drive Away Long-Serving Directors

The Proposed Guidelines would impose board composition expectations, including that "[t]here

should be at least a majority of independent directors on the board." Given that banks with over $500 million in assets are already required to meet independent audit committee standards under Section 36 of the FDI Act and part 363 of FDIC's regulations, the FDIC should explain its rationale for such a sweeping change.

We noted in the Proposed Guidelines, "An independent director is generally a director that is (a) not a principal, member, officer, or employee of the institution, and (b) not a principal, member, director, officer, or employee of any affiliate or principal shareholder of the institution." The net effect is to prohibit directors serving on a bank holding company board from serving on a wholly-owned bank's board. There is only a limited exception appearing in a footnote explaining that an independent director at a holding company may also serve as an independent director of an institution if the holding company conducts limited or no additional business operations outside the institution, as long as they are not a principal, member, director, officer, or employee of any other institution or holding company affiliate.

The FDIC has chosen to deviate in the board composition requirement from both the norm and the standards used by the other federal banking agencies. The FDIC should assess the massive impact on banks being able to find and retain qualified directors as well as assess the impact on the efficiency of their operations if they are forced to jettison long-serving insider directors who have contributed to the growth and success of their banks.

Fiduciary Duty Expansion Is Complicated by State Law Considerations

The Proposed Guidelines would require directors to consider, "the interests of all its stakeholders, including shareholders, depositors, creditors, customers, *regulators, and the public* [emphasis added]." In contrast, standards like those in North Carolina require a director to act in good faith, with the care an ordinarily prudent person in a like position would exercise under similar standards, and in the best interests of the corporation. Adding a layer to consider the interests of "regulators" and "the public" is a muddy standard at best. We urge the FDIC to reject standards that are too unspecific and amorphous. Directors should also not be put in the position of trying to reconcile their longstanding and well-established fiduciary obligations under state law and new, conflicting stakeholder obligations created under the Proposed Guidelines.

Director Eligibility Requirements – Demographics Versus Experience

The Proposed Guidelines state that a "board should consider how the selection of and diversity among board members collectively and individually may best promote effective, independent oversight of covered institution management and satisfy all legal requirements for outside and independent directors. Important aspects of diversity may include: social, racial, ethnic, gender, and age differences…." We certainly agree in the value of a board being diverse. However, this proposed standard that a board consider existing and potential directors' race, ethnicity, gender, and age is almost certainly going to face legal challenges. We encourage the FDIC to carefully weigh how to foster board diversity without creating new litigation risk for institutions. The FDIC should also continue to prioritize that directors have relevant banking expertise as there is no substitute for experience.

Harm to Bank Operations

In our view, there is a critical distinction between the role of bank executives – managing a bank day-to-day – and bank boards – providing oversight. However, under the Proposed Guidelines, boards must continually "ensure" the smooth functioning of the bank at practically every level of its operation. The term "ensure" is used 69 times in the notice and the Proposed Rulemaking. If the FDIC forces a board to be involved in operational decision-making to the degree identified in the Proposed Rulemaking and makes board members guarantee or "ensure" bank conduct, then bank executive management has been hamstrung. In addition to the bank no longer being nimble, board members have become full-time managers and have assumed massive amounts of personal liability.

Under these circumstances, many directors may choose to retire and fewer new individuals will be willing to serve. The most qualified – those with excellent discernment of risk – will turn their time and talents elsewhere, weakening the functioning of banks and of the overall industry.

Losing the Role of the Board in Providing Strategic Vision

Among the changes made by the Proposed Guidelines are new requirements to "create and quarterly review and update, as necessary, a risk profile that identifies [the covered institution's] current risks. Based upon its risk profile, the covered institution should have a comprehensive written statement, that is reviewed quarterly and updated, as necessary, that establishes risk appetite limits for the covered institution, both in the aggregate and for lines of business and material activities or products." After providing more details, the Proposed Guidelines go on to require that a board "review and approve the risk appetite statement at least quarterly, or more frequently, as necessary, based on the size and volatility of risks and any material changes in the covered institution's business model, strategy, risk profile, or market conditions." The expectation that a board should delve into the risk appetite with this frequency is unrealistic. The risk here with the change is that it prioritizes form over substance and could turn the process into a rubber stamp exercise which would be counterproductive. Much of the board's focus should be on the big, strategic picture, not in the weeds to the degree described in the Proposed Guidelines.

Applicability to Regional and Community Banks

The Proposed Guidelines note in the title field that they apply to "Covered Institutions With Total Consolidated Assets of $10 Billion or More." However, many pages into the Proposed Guidelines, the FDIC included this statement: "Upon notice to the institution, the FDIC reserves the authority to apply these Guidelines, in whole or in part, to an institution that has total consolidated assets less than $10 billion, if the FDIC determines such institution's operations are highly complex or present a heightened risk that warrants the application of these Guidelines." This reservation of authority is in direct contradiction with the titling. If the future intent of the FDIC is to examine regional banks or community banks, even if only on a discretionary basis, then for full transparency – and so all potentially affected institutions can comment – this should have been stated in the initial summary and conspicuously set out within the Proposed Guidance.

Needed Alignment with OCC and the Federal Reserve

The Proposed Guidelines contain numerous, new requirements. If the intent is to provide guidelines instead of a regulation, then there should be flexibility granted to banks in developing appropriate

procedures. An important reference point would be the OCC and Federal Reserve's heightened corporate governance standards, which are more principles-based. To the extent that the FDIC does move forward with a rulemaking or guidance in some form, the FDIC should, like those other agencies, establish a similar covered institution threshold at $50 billion or more and apply it only to insured state nonmember institutions that raise legitimate safety and soundness concerns.

Dominant Policymaker Standard Based on an Unfounded Premise

The Proposed Guidelines would define a "dominant policymaker" as "management, a director, a shareholder, or any combination thereof." CEOs and executives would fall within the proposed standard's dominant policymaker definition. The proposed standard starts with the premise that directors are "excessively influenced" by dominant policymakers. In our view, no director's judgment should be presumed to be impaired simply based on the existence of a "dominant policymaker." Directors already have fiduciary requirements to exercise prudence and independent judgment. They can, and do, challenge executive management and have both authority and responsibility to obtain from executive management and others all the data and materials they need to make well-informed decisions.

The Role of the CEO in Hiring Other Executives

The Proposed Guidelines provide that, a "board must select and appoint executive officers who are qualified to administer the covered institution's affairs effectively and soundly." Certainly, a board must select a CEO. However, while a CEO may consult a board when searching for qualified executives, a CEO has historically had responsibility for selecting an institution's other executives. The FDIC should clarify whether the Proposed Guidelines are intended to remove the CEO's authority to select other executives.

Clarify Whether a Board Must Approve All Policies

The Proposed Guidelines provide that "[t]he board is responsible for establishing and approving the policies that govern and guide the operations of the covered institution in accordance with its risk profile and as required by law and regulation." Presumably, the FDIC is not seeking to require boards to approve the thousands of pages of policies that most banks have, but is instead reminding banks that the role of the board is to help monitor risk. If the FDIC goes forward with guidance in some form, this needs to be clarified to identify the types of policies that specifically require board action.

Reporting Violations of Risk Limits

The Proposed Guidelines would require that a board establish processes for "front line units and the independent risk management unit" to "identify known or suspected violations of law or regulations applicable to the activities conducted by their units." In addition, units would "identify breaches of the institution's risk appetite and other risk limits, distinguish breaches based on severity, report on the breach, its impact, and resolution, and establish consequences for breaches of risk limits." And units would "[i]nform front line unit management, the CRO, the Risk Committee, the Audit Committee, the CEO, and the FDIC in writing of a breach of a risk limit or noncompliance with the risk appetite statement or risk management program describing the severity of the breach, its impact on the covered institution, and how the breach will be, or has been, resolved."

Is the intent here to require that front line units and independent risk management units report directly to the FDIC, bypassing management and the board? Perhaps the intent here is to talk about the escalation process, or perhaps create another avenue for whistleblowers. This needs to be clarified as the plain meaning of the provision would suggest that units have a duty to report directly to the FDIC, without giving management and the board an opportunity to apply their expertise to identify which issues are material and promptly address these issues.

Changes Would Undermine the Dual Banking System

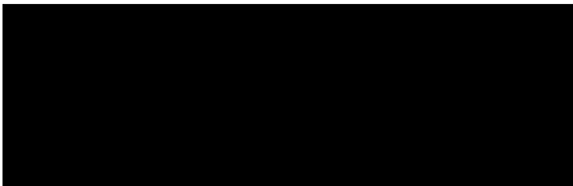
The NCBA is a strong proponent of the dual banking system. However, we believe the Proposed Guidelines would place FDIC-supervised, state-chartered banks at a competitive disadvantage to nationally chartered banks. Among the issues, the new compliance expenses incurred by banks would likely force them to raise the costs of bank products and services to try to cover these expenditures. They also will lose many well-qualified directors who are unwilling to become effectively day-to-day operations managers and absorb substantial, new personal liabilities. We anticipate that adoption of the Proposed Guidelines would drive boards of some banks to consider converting their banks to national charters. We believe this would be detrimental to the stability and vibrancy of the dual banking system.

Conclusion

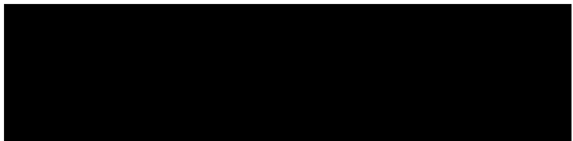
We believe that the Proposed Guidelines should be withdrawn so that the FDIC can reevaluate the numerous unintended consequences on the long-term strength of the banking industry. We urge the FDIC to instead consider alternative approaches.

Thank you for considering these comments. Please do not hesitate to contact us if you have any questions.

Sincerely,



Peter K. Gwaltney
President & CEO



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