International Bancshares Corporation

February 1, 2024

Via online submission:

Federal Deposit Insurance Corporation
Attn: James P. Sheesley, Assistant Executive Secretary
550 17th Street NW, Washington, DC 20429
Comments/Legal OES; RIN 3064–AF94
https://www.fdic.gov/resources/regulations/federal-register-publications

Re: Comments on Notice of Proposed Rulemaking Regarding Guidelines Establishing Standards for Corporate Governance and Risk Management for Covered Institutions With Total Consolidated Assets of $10 Billion or More: Comments/Legal OES; RIN 3064–AF94

Dear Mr. Sheesley:

The following comments are submitted by International Bancshares Corporation ("IBC"), a publicly-traded, multi-bank financial holding company headquartered in Laredo, Texas. IBC maintains 168 facilities and 257 ATMs, serving 75 communities in Texas and Oklahoma through five separately chartered banks ("IBC Banks") ranging in size from approximately $470 million to $8.9 billion, with consolidated assets totaling approximately $15 billion. IBC is one of the largest independent commercial bank holding companies headquartered in Texas.

This letter responds to the Notice of Proposed Rulemaking ("Notice") by the Federal Deposit Insurance Corporation ("FDIC") regarding Guidelines Establishing Standards for Corporate Governance and Risk Management for Covered Institutions With Total Consolidated Assets of $10 Billion or More ("Guidelines").

The FDIC is seeking comment on proposed corporate governance and risk management guidelines that would apply to all insured state nonmember banks, state-licensed insured branches of foreign banks and insured state savings associations that are subject to Section 39 of the Federal Deposit Insurance Act ("FDI Act"), with total consolidated assets of $10 billion or more on or after the effective date of the final Guidelines. Notably, the FDIC has reserved discretion to apply the Guidelines to institutions with less than $10 billion in consolidated assets if the institution presents a heightened risk or is highly complex, without defining what those thresholds would look like. [Notice at 70394]

The Proposed Guidelines would establish extensive and *enforceable* standards, which have the practical effect of requirements, for covered bank boards of directors, senior management, front line units, independent risk management departments, and internal audit groups of covered banks. The proposed Guidelines would require fundamental changes in board composition, board and management responsibilities and liabilities, and overall corporate governance. These required changes would have a profound impact on how banks operate and their ability to attract and retain the most capable directors, officers, and employees. The Notice indicates that the Guidelines are not intended to represent a significant departure from current bank practices established under the guidance previously provided by the Comptroller of the Currency ("OCC"), the Federal Reserve Board ("FRB"), or the FDIC's own examination program. IBC disagrees with

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this assessment and believes there is a significant gap between the FDIC's intentions and the actual results and consequences that IBC anticipates will be caused by the Guidelines.

Below are IBC's thoughts and comments on the Guidelines, which support its request that the FDIC retract the Guidelines, gather more data, and revise its proposal.

The Guidelines Represent a Significant Departure From Longstanding OCC, FRB, and State Law, Rules and Obligations

1. The proposed Guidelines will apply to FDIC-supervised institutions that have consolidated assets of $10 billion or more, whereas nearly every similar OCC and FRB rule and guideline has set the asset threshold for increased scrutiny and oversight at $50 billion. (See, the OCC's Heightened Standards for Large Institutions, 12 C.F.R. Appendix D to Part 30). The Notice states the FDIC's intention to "harmonize [FDIC] corporate governance and risk management requirements for covered institutions that present a higher risk profile with those applicable to entities supervised by the other federal banking agencies," but the proposed Guidelines set a significantly lower asset threshold than similar OCC and FRB rules. [Notice at 70393]

2. Even now, banking institutions dread reaching the $10 billion threshold due to numerous CFPB rules and guidelines that trigger at that threshold. To also now add these Guidelines will only cause that dread to grow and will likely increase the number of small and mid-sized banks reaching that threshold to seek mergers with larger banks. Merger with a larger institution will be required in many cases because small and mid-sized institutions simply will not be able to comply with the onslaught of new rules and requirements in a cost-effective manner. The Guidelines will cause the banking industry to further concentrate and contract.

3. The Guidelines would apply to state non-member banks and do not consider applicable state laws. This will lead to inconsistencies between banks and unknown exposures to covered banks and boards. For example, the Guidelines appear to be inconsistent with the governing corporate law of the states in which covered banks are chartered. The Guidelines would establish a mandatory constituency requirement (and add to the list of constituents), which has been rejected in every state.

4. The Guidelines add another agency rulemaking to the list that potentially runs into the Supreme Court's newly strengthened and evolving major questions doctrine. While Congress has clearly authorized prudential regulators to supervise banks and promulgate related standards, the evolving doctrine may reduce the degree of deference federal courts give to agency discretion, absent clear and specific congressional authorization. If the corporate governance of banks is classified as a major question of public policy, then federal banking authorities would need to point to clear congressional authorization for them to prescribe corporate governance mandates.

The Guidelines Should Provide Time For Compliance and the On and Off Ramp Timelines Should Be Revised

1. The Guidelines as drafted would be effective immediately for institutions with over $10 billion in consolidated assets and would provide no transition period to allow institutions to achieve compliance. The Guidelines do not provide for a transition period to achieve compliance with new, enforceable requirements. The FDIC would expect covered

institutions to be fully compliant on the effective date of the final Guidelines, meaning a covered bank could be forced to immediately change its board composition and quickly find additional independent directors. For small and mid-sized community banks that could be drawn into this, that is particularly troublesome. For example, IBC excels at diversifying its management team and staff up, down, and across its various business units. These women, underrepresented minorities, and members of the LGBTQ+ community that work in essential and important day-to-day roles that impact the perspectives, decision making and oversight, and internal controls of the company would not qualify as independent directors to satisfy mandated board member independence requirements. Moreover, small and mid-sized community banks subject to the Guidelines will face aggressive challenges in identifying qualified independent directors because most, if not all, are located and have their primary geographic footprints outside of the largest metro areas. IBC is unique, in part, because it is a large public company (a true community bank) headquartered in a very small city. To satisfy the independent director requirement, IBC would likely have to recruit an independent director from outside its headquartered community which would place an undue burden of travel, expense and loss of time, for that director to travel to attend meetings. Since IBC recruits active directors involved in the communities it serves, many candidates are not willing or able to accept a director position due to the necessary time commitments. IBC doesn't recruit from the "professional director pool," but instead seeks community leaders that serve as a part of their community engagement at a very modest stipend. If an independent director is asked to serve from a community outside of IBC's headquarters, it will mean a greater loss of time for that director, as it will require increased travel, and overnight stays, further frustrating the services of the director. Moreover, recruiting directors that serve for substantial pay would impact the entire director pay structure at most small and mid-sized community banks, resulting in a significant new cost burden and realigning incentives and mission simply to ensure the elusive (yet somehow still narrow) concept of diversity. All of IBC's holding company directors are in Laredo allowing convenient access for meetings. Given IBC's hands-on, community focus, in-person meetings are critical to the culture and success of IBC and its board. Since each of IBC's subsidiaries operate in different cities with their own separate boards, director diversity and independence is achieved for the enterprise as a whole. Executives and other leadership talent is very difficult to find, recruit, and maintain. The new requirement places even more of a burden on IBC to potentially consider placing an unqualified member on the board to simply to satisfy an arbitrary requirement.

2. The Guidelines are incredibly problematic for all covered institutions as the quick action required and potential turnover cannot be good for or supportive of safe and sound bank operations. The loss of institutional knowledge, the lack of time to conduct sufficient searches and due diligence, and the ramping up of new directors would absolutely be a detriment to a bank's safety and soundness. The Guidelines would also require covered banks to create new systems, processes and protocols. The need for stakeholders to have time to thoroughly review these requirements is particularly important because the Guidelines do not provide for a transition period to achieve compliance. So not only will covered banks be undergoing significant changes at the highest levels of their organization, but they will also need these new directors and managers to be completely competent in the new Guidelines and familiar enough with the Bank to implement compliance with the Guidelines. With no compliance transition period, this is simply an impossible task.

3. The Guidelines only provide a six-month "on-ramp" and twelve-month "off-ramp" for reaching or falling under the $10 billion threshold. IBC urges the FDIC to allow at least twelve months for both on and off ramps related to the asset threshold.

The Guidelines Are Inappropriately Vague and Ambiguous

1. While almost a throwaway line, the Notice states that the FDIC "reserves the authority to apply the proposed Guidelines, in whole or in part, to institutions with less than $10 billion in total consolidated assets if the FDIC determines that the institution's operations are highly complex or present heightened risk." [Notice at 70394] The Notice provides no further insight into what the FDIC would consider a "highly complex" institution or one that represents a "heightened risk." If this Guidance is to be binding, it needs to be clear when it will apply. What makes an institution "highly complex"? Will those institutions be provided the same on and off ramps to comply with the Guidance? Can an institution challenge the FDIC's determination that it is "highly complex" and thus subject to the Guidance? This catchall clause gives the FDIC far too much discretion to subject institutions to onerous obligations without sufficient due process.

2. Furthermore, the Notice defines "front line units" as "those units that, in general, generate revenue or reduce costs for the covered institution." [Notice at 70394] IBC believes this definition is not clear enough. What should be considered "reduc[ing] costs"? Legal departments certainly help organizations reduce costs, but IBC would not expect them to be included in the definition of front line units. IBC asks the FDIC to provide a clear definition of front line units.

Board and Management Issues

1. The Guidelines are far more prescriptive than descriptive, and will unnecessarily hamstring small and mid-sized institutions further hurting competition in the industry. The enforcement and compliance mentality is intense and the use of "ensure" throughout the Guidelines is at odds with the FRB and OCC approaches. Moreover, the overuse of "ensure" further complicates and erodes the independence and duties of the board and management. The Guidelines conflate the duties and responsibilities of the board and management of covered banks. The Guidelines are inconsistent with well-established duties and responsibilities of a board and management, and would radically alter the eligibility requirements for covered bank directors, thus creating not only inconsistency but conflict.

    a. Role of the Board: The FDIC's repetitive use of the word "ensure" (used nearly 70 times in the Notice) raises concerning implications regarding the fiduciary duty and responsibility of the board of a covered institution. The well-established role of the board is to oversee and hold management accountable. Additionally, the Guidelines' requirement that "the board, in supervising the covered institution, should consider the interests of all its stakeholders, including shareholders, depositors, creditors, customers, regulators, and the public" raises a potential conflict with well-settled law. [Notice at 70404] Moreover, these requirements would significantly conflict with state laws. The Guidelines' new overlay risks being at odds with many "shareholder value" states. Even in those states, directors often look to creditors, customers and depositors but weigh them according to the facts at hand as they consider long term interests. The Guidelines may also conflict with duties applicable to directors under "stakeholder state" standards because

although those standards broaden duties beyond shareholder value, the particular formulation can and does vary by state. Moreover, even in stakeholder value states, the consideration is almost always discretionary. Finally, the Guidelines' vague reference to "the public" as a stakeholder is highly unusual. While the broadest-drafted stakeholder states allow directors to consider the interests of "the community" or "the economy of the state and nation," the former is limited to a specific geographic area and the latter is confined only to the economic interests of the state or nation. By contrast, "the public" is not limited in any way, which will make it difficult for directors of regional banks to consider all potential interests of the public over an undefined area.

b. Independent Judgment: The Notice states that policy making should not be dominated or excessively influenced by one policy maker. [Notice at 70395] While IBC agrees that, in a vacuum, no one individual should excessively influence policymaking by the board, it also should not be the case that directors and board members are prohibited or second-guessed for agreeing with an individual's independent judgment when that individual has a lifetime of experience with financial institutions. Agreement with an experienced and competent individual should not be per se evidence that a board member is not exercising their own independent judgement. If the FDIC takes that position, it will be the FDIC that is undermining management's independent judgment.

c. Role of the Board Risk Committee.

   i. The Guidelines are unnecessarily limiting and prescriptive and do not allow covered banks the discretion or flexibility to structure their Risk Committees as best suits their institutions. All banks should have the authority to implement a risk and oversight framework that is specifically tailored to their institutions' complexity and risk profile. Instead, the Guidelines require the following of the Risk Committee:

      1. [A]n independent committee of the board that has, as its sole function, responsibility for the risk management policies of the covered institution and oversight of the risk management framework. [Notice at 70406]
      2. [D]ocument and maintain records of its proceedings, including risk management decisions; and... review and approve all decisions regarding the appointment or removal of the CRO, and ensure that the CRO's compensation is consistent with providing an objective assessment of the risks taken by the covered institution. [Notice at 70406]
      3. Reviewing reports from the CRO [Notice at 70396]
      4. Stay abreast of the risks of the covered institution, including any internal or external changes that may affect the institution, and make recommendations accordingly. [Notice at 70396]
      5. [O]verseeing the compensation and performance management of the CRO [Notice at 70396]
      6. [O]versight of the covered institution's risk management function and the risks of the institution itself. [Notice at 70396]

ii. Additionally, the FDIC should ensure that covered institutions, especially small and mid-sized banks, are allowed to rely on the risk management policy of their parent holding companies. In many cases, the holding company is in the best position to implement and oversee an enterprise-wide risk management committee. Often, the underlying subsidiary bank relies on the resources of the holding company specifically to help provide guidance and requirements regarding risk policies and procedures instead of carrying its own unique risk management policy and committee. Many institutions are not required to create and implement their own unique risk regimes due to their size and risk profile not reaching the obligatory thresholds. Again, this is a clear instance of the FDIC's proposal conflicting with and undermining settled positions of other federal and prudential bank regulators. Forcing each subsidiary bank to have its own risk management committee is duplicative, an undue strain on resources, and will unfairly burden smaller subsidiary banks. These small subsidiary banks will now need to expend resources and will no longer be able to rely on economies of scale provided by their parent holding companies. Leveraging the resources and expertise of a parent holding company is one of the only ways many small and mid-sized community banks are able to effectively govern and control costs sufficiently to both operate in a safe and sound manner and compete with large institutions. Taking away one of the few cost and resource saving options community banks have to stay competitive will simply continue the accelerating trend of these community banks closing or being merged into the handful of behemoth bank institutions. This will also exacerbate the already steep challenge of finding a sufficient number of qualified individuals to serve in these myriad roles, which already unfairly affects small and mid-sized community banks because of their geographic locations (more rural/suburban vs. large metro) and need to compete against large institutions for the same qualified personnel. The Guidelines are just another step in undermining smaller institutions' ability to compete against large banks.

iii. As a more general matter, the governance standards outlined in the Guidelines writ large would require covered banks to establish and operate a complex, formal risk management framework. The financial cost and time required by the board and management to stand up such programs, build systems and sustain them would impose a significant burden on those covered banks. Even more significantly, many affected banks are located outside of major metropolitan areas, making it difficult to recruit and retain talent with the specialized experience needed to satisfy the agency's expectations.

iv. Moreover, the CRO will now be independent from the CEO and will report to independent Board members. Many institutions, including those near and barely over $10 billion in assets have dual CEOs and CROs. How will a dual CEO/CRO function under the Guidelines? Not all state laws require or allow direct CRO reporting to the Board. Would the Guidelines trump state law to the contrary?

v. IBC's Audit Committee follows the Institute of Internal Auditors guidelines for evaluating the Chief Audit Executive. IBC is not aware of any related

industry guidelines for CROs and other related positions and departments. What are the FDIC's expectations regarding the requirement that institutions establish compliant and appropriate performance management programs?

2. Conflation Between Responsibilities of Board and Management.

    a. The Guidelines repeatedly require the board to "establish", "ensure", and affirmatively act regarding management personnel, instead of a board's true purpose which is to actively oversee and hold management accountable. The FDIC's use of "establish" versus "review/approve" confuses and conflates the roles of the board and management. The board appropriately selects the CEO, while other executives would generally be selected by management, subject to board approval. In an unprecedented upheaval of norms, the Guidelines would require the board to select and appoint "executive officers." {Notice at 70396] Those executives and management then are charged with "establishing" and "ensuring" appropriate policies, procedures, training, and other oversight of the day-to-day personnel. The board should not be in the weeds in regards to this oversight.

    b. The Guidelines require that boards must approve certain fundamental policies at least annually. [Notice at 70405] While providing some examples of fundamental policies that are essentially addressed in other regulations, the Guidelines don't go beyond that to define what is a fundamental policy. The Guidelines, as written, could inundate the board with policies that are best left to managers of the various business lines of the bank. This is also another instance of the FDIC's proposal conflicting with other bank regulators' guidelines and rules. For example, the OCC expressly exempts many policies from board approval because not doing so "would be burdensome" and take focus away from the board's general oversight and compliance functions.[1]

3. Liability of Board and Management.

    a. The Guidelines would increase the potential liability of covered bank directors and officers far beyond that applicable to all other corporations. To wit, the Guidelines appear to make board members potentially liable to both consumers and the general public under the standard of simple negligence. This is a wholly novel approach that will have a dramatic impact on banks and their ability to recruit and retain qualified directors. Bank boards have historically been charged with governing the bank and not directly managing the bank. The Guidelines fundamentally upend that precedent. IBC believes there should be a strong, ongoing distinction between governance and management functions and duties.

    b. The Guidelines would have significant implications for banks' ability to attract and retain qualified directors. Because the Proposed Guidelines include prescriptive requirements for the composition and duties of the bank board, stakeholders will need time to evaluate and consult with others regarding the impact on FDIC-

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[1] *See* 79 FR 54518 at 54526 ("The OCC believes that board or risk committee approval of material policies under the Framework would be burdensome, and that these policies should be approved by management instead.").

supervised banks in recruiting and retaining qualified personnel including directors. The Guidelines provide that "[e]ach member of the board has a duty to safeguard, through the lawful, informed, efficient and able administration of the covered institution, the interests of the covered institution and to oversee and confirm that the covered institution operates in a safe and sound manner, in compliance with **all** laws and regulations." [Notice at 70404, emphasis added] This provision creates both an expansive duty on directors, as well as unnecessary regulatory burden. Moreover, as written, this provision suggests the board must independently validate the work of independent risk management and the audit function, which is a wholly inappropriate function of the board.

c. The expansion of fiduciary responsibility on the board, coupled with the enforcement bias set forth in Notice, will discourage individuals from serving on boards, and will likely prompt existing directors to reconsider their service and/or demand much higher payment for their services. There will also be heightened litigation risk stemming from the increased fiduciary responsibility, as well as potential conflicts between actions required by the Guidelines versus those required by applicable state law.

4. Board Independence and Diversity Mandate. The Guidelines set forth specific considerations for diversity of the board. [Notice at 70395] IBC does not believe this should be part of the guidance. At bottom, institutions should focus solely on experience and competence and not simply diversity for diversity's sake. If there are individuals with identical commiserate experience and competence, demographic diversity might be a tie-breaking consideration. But experience and diversity should trump everything else, especially when it comes to safety and soundness concerns. Even so, IBC strives to create a board of diversified thought, background, perspective, and upbringing. IBC believes it is beneficial for directors to reflect the diversity of IBC's *markets*, as opposed to simply implementing a diversity "check box" or quota system. As noted herein, IBC also excels at diversifying its management team and staff up, down, and across its various business units. But its excellence in this area directly affects its ability and opportunities to fill independent director board positions because the women, underrepresented minorities, and members of the LGBTQ+ community that work in essential and important day-to-day roles that impact the perspectives, decision making and oversight, and internal controls of the company would not qualify as independent directors to satisfy mandated board member independence requirements. Also, IBC fears the results of a hard line numerical board diversification requirement causes concern (1) that boards will not be focused on their main objective of serving shareholders, (2) that qualified and independent directors which best represent a company's shareholder base and community will become harder to find, and (3) that impacts of diversity among highly compensated executive and company-impacting positions and roles will be diminished at the expense of satisfying the proposed board diversification requirement.

<u>The Guidelines Impose an Undue Regulatory Burden</u>

1. The Guidelines require that a covered institution's Risk Appetite Statement be approved by the board at least quarterly. [Notice at 70407] In turn, the Statement must be incorporated in strategic plan, operating plan, capital and liquidity stress testing, risk management processes, M&A decisions, and compensation and performance management programs. Thus, the Guidelines would require quarterly review and updates to all of these plans and processes should the Statement change, but IBC (and most

institutions) already have triggers and review policies and processes for such changes that do not necessarily require full board review and approval. The Guidelines also require the Risk Committee to meet quarterly. IBC requests that the FDIC allow more discretion to institutions, and allow institutions to set their Risk Committee meeting schedule based on the institution's ability to manage its risk and its risk appetite. Managing risk and risk appetite are areas the FDIC could build into the Guidelines to meet its goals. It should not mandate set meetings without any concern for each institution's unique makeup and complexity.

2. The Guidelines also require the board to conduct an annual self-assessment evaluating its effectiveness in meeting the standards of the Guidelines. [Notice at 70396] This would require an annual and expansive board-led compliance exercise. IBC already conducts annual self-assessments of its Audit and Risk Committee. Conducting the same for the full board would be an incredibly onerous burden. IBC believes that the FDIC should limit the required annual self-assessment to risk and audit committees.

3. The Guidelines also contain prescriptive requirements to inform 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, and contains similar requirements for all violations of law and regulations. [Notice at 70397] The Guidelines require a covered bank to timely report violations of said Guidelines to the agency[ies] with jurisdiction. The vague and ambiguous nature of these parts of the Guidelines make this particularly difficult, as it is unclear what is reportable and when it must be reported. Additionally, this requirement would appear to be the first of its kind in federal banking law and does not have precedent in the historical approach of the FDIC or of the other federal bank regulators. Insured banks are subject to a vast and complex array of laws and regulations, both those that are specific to banking and those of general applicability. The Guidelines would include an unprecedented requirement for a covered bank to timely report known or suspected violations of law or regulation to various government agencies without any materiality standard, level of certainty that a violation has occurred or clarity on the timing of such reporting. Stakeholders will require sufficient time to evaluate the legal ramifications, complexities and consequences of this novel requirement, particularly because the question of illegality can often be highly fact-specific and dependent on government and judicial positions that change over time. Furthermore, a requirement to externally self-report on legal issues could be expected to pose significant consequences for attorney-client and other privileges.

The FDIC's current proposed Guidelines appear to be premature and lack sufficient basis to assure the covered institutions and the public that (1) its benefits will exceed its costs, and (2) it will truly further the interest of bank safety and soundness. The FDIC should withdraw the proposal, solicit information, and perform a meaningful cost-benefit analysis. It should then present those findings, and how the FDIC reached them, to the public for comment and critique. Without such actions, there can be no confidence that the Guidelines will be an improvement, rather than a detriment, to safety and soundness.

Thank you for the opportunity to share IBCs views on these matters.

INTERNATIONAL BANCSHARES CORPORATION

Dennis E. Nixon, President and CEO