Charles G. Cooper
Commissioner

TEXAS DEPARTMENT OF BANKING

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February 8, 2024

Via Electronic Submission

Mr. James P. Sheesley
Assistant Executive Secretary
Attention: Comments/Legal DES (RIN 3064-AF94)
Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429

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)

Dear Mr. Sheesley:

The Texas Department of Banking (DOB) submits these comments in response to the Federal Deposit Insurance Corporation's (FDIC) recently proposed guidance entitled, "Guidelines Establishing Standards for Corporate Governance and Risk Management for Covered Institutions with Total Consolidated Assets of $10 Billion or More" ("proposal"), set forth in the Federal Register, published on October 11, 2023.

The DOB charters and regulates 213 banks with combined total assets of $433 billion. Of the 213 banks, five banks are FDIC insured, non-member banks over the $10 billion threshold contemplated by this proposal. Nationwide, approximately 3,700, or 79%, of all banks are state chartered. Sixty of these banks would be affected by the proposal. As the chartering authority and the primary regulator of these banks, state bank regulators have a unique perspective and interest in their well-being. The FDIC did not discuss this proposal with the DOB or, to my knowledge, any of our state colleagues prior to its release.

The DOB has significant concerns with the proposal, including the following:

1. Insufficient justification is provided as to the need for the new requirements as there is existing corporate guidance which was mentioned in the proposal. Before new guidance is issued, a thorough analysis of why the existing guidance is insufficient should be performed. The after-action reports of the two regional banks that failed in March of last year reveal there were failures by the banks' boards and management to observe existing guidance, and a failure of bank regulators to appropriately address shortcomings.

2. In Paragraph II.A., the proposal states: "The board, in supervising the covered institution, should consider the interests of all its stakeholders, including shareholders, depositors, creditors, customers, regulators, and the public." This listing of the general obligations of bank directors introduces confusion and may conflict with existing corporate governance requirements already established by state law which has evolved over decades. In Texas the proposed guidelines could

conflict with the fiduciary standards which currently apply to directors under Texas law. In a recent opinion, the Supreme Court of Texas, in *Matter of Est. of Poe*, 648 S.W.3d 277, 286-87 (Tex. 2022), ruled "Directors owe a fiduciary duty to their corporations in the actions they take as directors. A director's fiduciary status creates three broad duties: duties of obedience, loyalty, and due care. These fiduciary duties run to the corporation, not to individual shareholders or even to a majority of shareholders. […] [A] director's fiduciary duty includes a duty to dedicate uncorrupted business judgment for the sole benefit of the corporation." The Fifth Circuit Court of Appeals, in *Gearhart Indus., Inc. v. Smith Int'l, Inc.*, 741 F.2d 707, 719-20 (5th Cir. 1984), agreed, also stating "the directors' duties of loyalty and care run to the corporation, not to individual shareholders or even to a majority of the shareholders," then continued to explain that "a cause of action for breach of directors' fiduciary duties belongs to the corporation and cannot be brought by a stockholder in his own right, nor can the shareholder directly prosecute the suit in the name of the corporation." Requiring the board for a covered institution to consider the interests of the additional entities listed in the guidelines, in addition to the corporation, would directly conflict with established state law.

Aside from the potential conflicts, the list of parties whose interests the board should consider is extremely broad and, thus, raises further questions and creates confusion. For example, do the interests of each of the listed stakeholders carry the same weight? For the term "regulators," what regulator is contemplated – FDIC, State, or Consumer Financial Protection Bureau (CFPB), and does it refer to the regulator examining the bank on-site, or the one in the regional office, or the Washington, D.C. office? Similar questions could be asked as to every other listed party in interest as well.

3. The proposal establishes a new requirement that the board "should include a majority of outside and independent directors." This exceeds the Office of the Comptroller of the Currency (OCC) requirement that two members be independent, and there is no specific number set by the Federal Reserve Board (FRB). No justification is provided for this position. Furthermore, the fact that a bank board member who is also a holding company board member may not be considered as independent is problematic. While there appear to be some exceptions, this limitation for a holding company director also serving on the bank board is not properly justified. Nearly all banks covered by this rule proposal have a holding company structure, and overlapping board membership is a regular occurrence. Holding companies are supervised by the FRB, yet the FRB does not impose similar prohibitions. Creating such a limitation will undoubtedly cause disruption to existing companies and potentially reduce the existing talent pool available to serve on bank boards.

4. The proposal introduces guidelines that cause director duties to intersect with clear management responsibilities. Existing guidelines, both state and federal, indicate that management is responsible for the day-to-day operations of the bank, and the board is responsible for selecting and overseeing management. In the "*OCC's Director's Book – Role of Directors for National Banks and Federal Savings Associations,*" it states "The board's role in the governance of the bank is clearly distinct from management's role. The board is responsible for the overall direction and oversight of the bank – but is not responsible for managing the bank's day-to-day." Broadly, the proposal's usage of words requiring the board to "ensure" or "confirm" actions taken by management has a completely different connotation than the current standard of "overseeing of management and holding management accountable." Merging directors' duties with management responsibilities is clearly improper and results in the board overseeing its own work product.

The proposal introduces a high level of confusion along with what appears to be a vast increase in the responsibilities of the board and, therefore, individual directors. The DOB fears that this will further limit the potential pool of capable directors. A plausible result of an increase in prescriptive guidelines might be an increase in compensation required by directors in order to offset the significant increase in complexity and risk inherent in the new requirements. Since the proposed rule is not properly tailored to the complexity or size of the bank, it is logical to assume there will be significant expenses disproportionately impacting the smaller banks, which will most likely cause further bank consolidation.

5. The proposal establishes different standards for a state non-member bank than for state member banks and national banks without a justifiable reason. If the proposal is adopted, the threshold for the proposed increase in standards will be $10 billion for state non-member banks. In contrast, the OCC's heightened standards commence at $50 billion and the FRB's enhanced prudential standards for bank holding companies is $100 billion. This disparity means that state regulators, along with the FRB, will be examining member banks under different requirements than we would, along with the FDIC, when examining non-member banks. This inconsistency is counter to existing standards and practices, and the proposal does not provide any justification for this size disparity. The FDIC only states that its proposal is for "large, more complex institutions." This can hardly be considered as tailoring regulations to the size and complexity of individual banks.

6. The proposal is to be implemented through Section 39 of the FDI Act and would issue the proposal guidelines as Appendix C to Part 360 of the FDIC regulations. Therefore, failure to meet the guidelines could be considered a safety and soundness issue. As mentioned previously, much of this proposal and the terms utilized are confusing. Additional problematic examples include the proposal's requirement that boards "set an appropriate tone," establish "a corporate culture," and "articulate an overall mission statement." Items such as these can be extremely subjective and though important, should be addressed as principle-based guidance, not enforceable guidelines. As written, the proposed guidelines may lead to a "check-the-box" mentality instead of an attitude of robust corporate governance.

In summary, keeping our banks operating in a safe and sound manner is an important function that all bank regulators share, and proper corporate governance is certainly necessary for this to succeed. The DOB believes that the FDIC proposal misses the mark. For the reasons indicated above, this proposal is fatally flawed and should be withdrawn. If the proposal continues, it seems appropriate for future deliberations to be held in a formal public meeting to foster transparency, open discourse, and debate among the FDIC board members, and which will allow for an open discussion of potential conflicts of interest.

Sincerely,

[redacted]

Charles G. Cooper
Commissioner
Texas Department of Banking