

Introduction to Management

This section addresses the overall capabilities of the board of directors and management, in their respective roles, to identify and control the risks of a savings association's trust and asset management activities. Boards of directors and management have multiple responsibilities in governing the activities of a trust department, particularly with regard to fiduciary activities and the fundamental duty of loyalty. Examiners should ensure that the board and management have established clear guidance regarding acceptable risk exposure levels. Another responsibility of management is to ensure that appropriate policies and practices of the trust department are established and followed. Examiners must also determine the ability of the board of directors and management, in their respective roles, to plan for, and respond to, risks that may arise from changing business conditions or the introduction of new activities or products. Examiners assess management and boards of directors on whether sound risk management practices, such as the following, are in place: establishing and maintaining active oversight by the board of directors and management; hiring and retaining competent personnel; instituting adequate policies, processes and controls that consider the size and complexity of the savings association's trust and asset management activities; and establishing effective risk monitoring and management information systems.

Responsibilities of the Board of Directors

The board of directors is ultimately responsible for all aspects of the savings association's trust and asset management duties. Directors are responsible for retaining and performing general supervision over the exercise of trust powers. If the directors fail to properly exercise these duties, they will increase the overall risk of the savings association and may be held liable for any losses to account beneficiaries. In discharging its authority, the board of directors may delegate duties and responsibilities to such committee(s), director(s), officer(s) or employee(s) as it deems appropriate. However, the board retains ultimate responsibility for all delegated matters and must maintain the proper degree of control and supervision over those it has empowered.

The board of directors must be sufficiently independent of corporate affiliates and personal conflicts of interest to properly serve the interests of the savings association. In many cases, OTS has imposed conditions in the chartering process that at least 40 percent of the savings association's board of directors must be individuals who are not officers or employees of the savings association or any affiliate of the savings association. Another condition that may be imposed is to have at least one member of the savings association's board of directors be an individual who is not an officer, director or employee of the savings association or any of the savings association's affiliates. When evaluating management, the examiner should determine whether such conditions have been imposed and the savings association's compliance with them.

The examiner should review the actions of the board of directors, noting any deficiencies or failure to carry out its duties. The management system and organization should also be reviewed to assure it has an appropriate framework to carry out the trust and asset management responsibilities of the savings association. The board, the number of which will often be determined by the size of the trust department and the complexity of the accounts administered, may utilize trust committees.

OTS §550.150 states that the savings association's board of directors is responsible for the proper exercise of its fiduciary powers. The regulatory and examination approach taken by OTS also emphasizes the ultimate responsibility of the board of directors over all trust and asset management activities. In other words, the board is responsible for all matters pertinent to the trust department. This would include responsibility for

compliance with applicable law and the standards of fiduciary conduct. Illustrative (but not inclusive) examples of such overall responsibility would include: responsibility for ensuring that a system of policies and procedures is adopted, practiced and monitored; responsibility for the prudent investment and disposition of property held in a fiduciary capacity; ensuring that adequate management is in place to control risks; ensuring that an annual audit is conducted; and, ensuring that a record of pending litigation is kept.

In addition, it is important for the board to ensure that the trust department's management information and data processing systems are adequate to provide the type and quantity of reports necessary to assess and monitor the trust department's performance. The quality of information provided to boards of directors in board and committee reports is critical in their decision-making processes. Not only must the board carefully review information provided by management but they must also ensure that the information is complete and contains all pertinent information required to oversee the trust function. Further, the board should ensure that corrective action is effectively implemented when deficiencies are reported. Section 550.150 further states that the board may assign the administration or any function related to the exercise of fiduciary powers, as it may consider proper. However, generally accepted fiduciary principles provide that certain functions cannot or should not ordinarily be delegated including, in part, approval of significant new services or lines of business, approval of formal policies and selection of senior management. Even with proper delegations, the board retains ultimate responsibility and, if the board assigns functions to individuals or committees, it must monitor the assignments to ensure that they are being properly performed. All such actions taken by individuals or committees should therefore be properly recorded in the minutes (or a similar record). While it is not necessary that all written records be specifically approved, such records should be available for the board's inspection. The board should also be closely monitoring fiduciary services performed on behalf of the savings association by another institution or entity. These services must be performed under a written agreement in accordance with §550.180. The agreement should clearly delineate the services to be performed by the other entity.

Policies, Procedures and Internal Controls

The directors should formulate and implement suitable policies, procedures and internal controls (collectively referred to below as "policies") to promote sound trust and asset management administration. Comprehensive, well-developed policies, assuming they are followed, monitored and enforced, are one of the most effective methods of promoting operating efficiency, ensuring compliance with laws and fiduciary principles and deterring losses. The scope and detail of policies adopted by the board of directors for the trust department should take into account the savings association's size, complexity and trust and asset management risk profile. While the need for and content of policies will therefore vary between institutions, written policies should ordinarily be in place for the following areas:

Federal Securities Laws: Written policies and procedures are specifically required by §550.140(b) to ensure that any decision or recommendation to purchase or sell any security is not made by fiduciary officers and employees using material inside information.

Conflicts of Interest: Policies should be established to cover those areas where the interests of the fiduciary account might conflict with those of the savings association itself (i.e. in its role as lender), its directors, employees or its affiliates. Examples of conflict situations include, the purchase of own-institution or affiliate obligations (i.e., stock, mortgages); purchase of proprietary mutual fund shares for discretionary trust accounts; purchase of assets from or sales to directors, affiliates or other interested persons; or purchases or sales between fiduciary accounts. Policies and written agreements should also be established regarding transactions with affiliates, including affiliated broker dealers so as to comply with OTS regulations regarding transactions with affiliates. 12 CFR §563.42(b).

Asset Management: Policies should be established to demonstrate compliance with applicable state prudent man or prudent investor laws or applicable federal law such as ERISA when the savings association makes investment decisions for discretionary accounts. Investment policies should exist that are designed to promote preservation of principal, diversification of portfolios, establishment of individual account investment objectives, production of income (including prompt investment of income and principal cash) and to prevent speculation. The board should also ensure that any delegation of investment activity (e.g., investment advisory services) is pursuant to a written agreement whereby the savings association retains ultimate investment oversight and responsibility.

Account Administration: Policies should be established to assure that all trust and asset management accounts are administered in a consistent manner and in accordance with the terms of the governing instrument and applicable law. Examples of such policies include, acceptance of accounts (including cofiduciary and successor appointments); account set-up; account reviews; overall administration (including tickler systems; receipts and disbursements; possession and control of assets; account documentation requirements) and account termination procedures.

Operations: Policies should be established to assure the integrity and accountability of the trust department's systems and internal controls. Examples of such policies include, storage and handling of assets; separation of duties; processing and reconciliation of transactions; document filing and maintenance; outsourcing; and standards for information technology systems.

Personnel: Policies should be established regarding the appropriate size and qualifications of staff, organizational structure and employee ethics. The latter policy should address acceptance of gratuities and bequests from customers or other interested parties and any personal services rendered, benefits gained and/or influences exerted by the employee to or from the customer.

Business Development and Profitability: Policies should address the nature and type of the trust and asset management business to be solicited, fees to be charged (including discounts, waivers or compensating balances), marketing strategies and the overall goals and objectives of the savings association in offering and providing trust and asset management products and services.

A number of other policies should be adopted to cover certain specified activities. These are addressed in the relevant sections of the handbook and include, for example, proxy voting, securities trading and brokerage placement policies as well as the establishment of audit, compliance and risk management programs. Specific policies required are specified in §550.140.