Helping hands: utilising service providers

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1. Introduction

When a family set up a private trust company, they typically create a structure and implement operations that address their unique needs and wishes for the administration of their fiduciary relationships. Some families have numerous trusts and entities, multiple generations of family members, extensive family office operations, robust investment management structures, and a significant number of employees already working for the family. Other families may have one or two trusts, only a few family members and no family employees or existing administrative or investment structures. With private trust companies of all shapes and sizes, it is no surprise that the use of service providers by private trust companies is as varied as the families themselves. This chapter looks at the different types of typical private trust company service providers, examines the various considerations for selecting, monitoring and terminating service provider relationships, and discusses the unique considerations involved in utilising affiliated service providers and investment service providers. While this chapter references specific laws and regulations in the United States, in many cases the topics discussed are generally applicable to private trust companies operating globally.

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2. Types of service providers

Private trust companies with smaller operations and fewer employees likely require more help from service providers to properly administer the private trust company and its client accounts, compared with private trust companies with more substantial operations and numerous employees. That said, most private trust companies engage service providers for one or more of the services that follow.

2.1 Administrative services

A private trust company may engage a service provider to maintain the books and records of the private trust company and its client accounts, to pay bills, coordinate and implement transactions, develop budgets and financial reports, assist with audits, manage human resources and payroll services, monitor

custodians, coordinate with other professional service providers on behalf of the private trust company and perform any other administrative services that may be requested by the private trust company.

The amount and type of administrative services utilised by a private trust company may ebb and flow over time depending on its operations and its client accounts. Nonetheless, it is important for a private trust company to have an administrative service provider if it does not have the infrastructure to conduct all of these tasks on its own, especially because a private trust company is subject to the same fiduciary standards regardless of its size. An administrative service provider could be a family office, a multi-family office, a retail trust company, another private trust company or a commercial company dedicated to providing these types of services.

2.2 Office space

Several states, including Florida, Nevada, Wyoming, Tennessee, Texas and Ohio, require a private trust company to maintain an office in the state where it is formed or licensed.[1] Even if a state does not impose this requirement, it is generally best practice to maintain a physical office in the state where the private trust company acts. In many cases, though, the family is not located in the state where the private trust company is formed and does not have existing operations or office space in that state. These private trust companies then need to lease or purchase office space. The private trust company may not need substantial physical space or robust office operations so a traditional office lease may be overly expensive and unnecessary. Instead, a private trust company could incorporate a lease for office space into its agreement with an administrative service provider as a way to bundle physical office space with administrative services. A private trust company also could lease space from a local law firm or commercial service provider that understands the limited office space needs of a private trust company and may have more flexible and cost-effective arrangements.

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2.3 Accounting and tax

As a fiduciary, a private trust company is responsible for maintaining the financial books and records of its client accounts as well as its own operations. It also will need to prepare or coordinate the preparation of income tax returns for itself and its client accounts. A private trust company may receive accounting, tax planning and tax return preparation services as part of its administrative

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1 Fla Stat § 662.1225(1)(a) (2019) (requiring a physical office in Florida for a family trust company or licensed family trust company); Nev Rev Stat § 669A.140(2) (2019) (requiring a physical office in Nevada for a licensed private trust company); Wyo Stat Ann § 13-5-604(a)(1) (2019) (requiring a physical office in Wyoming for a regulated private trust company); Tenn Code Ann § 45-2-1012(a) (2019) (requiring a principal office in Tennessee); Tex Fin Code Ann § 182.202 (West 2019) (requiring a principal office in the state where books and records are available); Ohio Rev Code Ann § 1112.14(A) (West 2019) (requiring a physical office for a licensed private trust company for storing and providing access to records).

services engagement. If it does not, the private trust company will need to perform these services itself or engage a third party to provide them.

2.4 Audit

Some private trust companies are required by their governing documents or state examiners to conduct periodic audits of the private trust company's fiduciary or financial activities. Other private trust companies optionally conduct these examinations. A private trust company typically engages independent accounting firms or audit companies to examine the fiduciary or financial activities of the private trust company and its client accounts, and in some cases, to ensure compliance with applicable laws and regulations.

2.5 Bank and custodial arrangements

Private trust companies generally do not accept deposits or provide custodial services for assets held in client accounts. Instead, a private trust company will select a bank or other financial institution to maintain its accounts and the accounts of its clients. This bank or other financial institution may also custody assets in the client accounts, or the private trust company may enter into a separate custodial relationship for those services. Depending on its jurisdiction and regulatory status, a private trust company may be required to maintain a bank account in the state where it provides fiduciary services.[2] This could be an account at a local or state-chartered financial institution or at a national financial institution with a branch office in the appropriate state.

2.6 Legal

Generally, private trust companies engage attorneys to aid in the formation and ongoing administration of the trust company and to advise on fiduciary matters that may arise for the private trust company's client accounts. This legal representation may be the long-time attorney for the family, a new law firm with extensive experience in private trust companies and their operations, local attorneys familiar with the state-specific regulations impacting the private trust company, or some combination of these attorneys to form a comprehensive legal team.

2.7 Investment services

Some private trust companies employ investment advisers within the private trust company structure to manage the client accounts directly. Other families invest through one or more investment entities managed outside the private

2 For example, Nevada and Wyoming both require a licensed (or chartered) private trust company to maintain a bank account at a state-chartered or national bank having a principal or branch office in the state. Nev Rev Stat § 669A.140(5); Wyo Stat Ann § 13-5-206(a)(ii).

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trust company. If a private trust company does not have its own in-house investment professionals or family investment entities, it likely will engage one or more third parties to provide investment advisory and management services to the private trust company and its client accounts. The unique considerations associated with investment service provider relationships are discussed in more detail below.

2.8 Directors and officers

Some states require a resident of the state to serve as a director or officer of the private trust company. For example, Florida, South Dakota and Ohio require that at least one director of the private trust company be a resident of the state.[3] Texas requires at least a majority of the directors to be residents of the state,[4] and Nevada requires that at least one officer be a resident of the state.[5] Given that the family may not be located in the state where its private trust company operates, there may not be any residents of the state known to the family who can serve as a director or officer. In those cases, the private trust company will need to engage a resident of the state to fulfil this requirement. These individuals are typically local attorneys, employees of commercial administrative service providers, or other local advisers selected by the family. As directors or officers, these individuals will have certain rights and responsibilities over the management and operations of the private trust company, as set out in the governing documents of the private trust company and applicable law. Therefore, it is important for the family to carefully consider who they are hiring to satisfy these requirements because that person may be intimately involved in the governance and decision making of the family's private trust company.

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2.9 Family consultants and additional services

Some private trust companies provide consulting and wellness services to the family in addition to fiduciary services. These private trust companies may develop financial or educational programmes for family members, arrange for health and wellness professionals to advise family members, engage family business consultants, plan family meetings or retreats, and coordinate a variety of other services for the family.

A private trust company may engage one service provider to perform all of the functions described above, or it may hire separate service providers to perform a subset of these functions. The number and types of service providers will depend on the private trust company's internal structure, scope of affiliated

3 Fla Stat § 662.125(2); SD Codified Laws § 51A-6A-13 (2019); Ohio Rev Code Ann § 1112.14(E)(1).
4 Tex Fin Code Ann § 183.103(a).
5 Nev Rev Sat § 669A.140(1) (for licensed family trust companies).

entities and regulatory jurisdiction, and the needs of the family, the private trust company and its client accounts.

3. Selecting, monitoring and terminating service providers

Outsourcing to service providers is one way to obtain expertise not otherwise available internally. It also can improve the services provided to the private trust company's client accounts, manage costs and satisfy certain regulatory requirements. With all of these associated benefits, it is no wonder that more and more private trust companies are engaging service providers to aid in their operations. This reliance on service providers does, though, expose the private trust company and its client accounts to increased risks of:

- disclosure of family information and general loss of privacy;
- greater administrative red tape and regulatory compliance;
- different operating controls and protocols that could result in inconsistent treatment;
- confusion over which organisation or individual has a particular responsibility; and
- lower-quality services or a disruption of services due to issues impacting the service provider that are beyond the control of the private trust company.

A private trust company may review these risks and decide that they are too great or that they cannot be managed effectively. In that case, the private trust company will hire for all of the appropriate functions it needs internally and not utilise any service providers. Alternatively, the private trust company may examine the key risks associated with outsourcing certain functions and determine that those risks can be managed with the appropriate policies, procedures and agreements. In either case, it is important that the private trust company review and understand the risks of engaging a service provider, and once engaged, conduct a regular review of these risks.

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3.1 Selecting a service provider

Once a private trust company decides to engage a service provider, the private trust company then must select the appropriate individual or company to provide the services. The private trust company should fully investigate any potential service provider and document its due diligence in the records of the private trust company. As part of this due diligence, the private trust company generally should assess the factors below.[6]

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6 While the Federal Deposit Insurance Corporation (FDIC) typically does not examine state-chartered private trust companies, its Trust Examination Manual highlights items a trust company should consider in its review of a potential service provider, which can serve as a best practice guide for private trust companies. See FDIC Trust Manual, Section 10.G.2 (2015), available at: www.fdic.gov/regulations/ examinations/trustmanual/section_10/ section_x.html#G2.

(a) Types and quality of services

It probably goes without saying, but the service provider should be able to provide the types of services for which it is being engaged. The service provider also should be able to handle the volume and nature of the private trust company's operations, its client accounts and the assets that are held in those accounts that will be serviced through the arrangement. It is also prudent for the private trust company to verify the quality of services offered by the service provider. The private trust company may have a pre-existing relationship with the service provider or one of its affiliated entities and can rely on its first-hand knowledge of the quality of services. Absent this, it may be beneficial for the private trust company to seek out references, contact names or other sources of review of the service provider's quality of services before entering into the engagement.

(b) Fees

The private trust company should review the fees to be charged by the service provider and then determine if such fees are reasonable and appropriate for the services to be received. It is also important that the private trust company understand any additional fees, expenses or other charges that it will be expected to cover or reimburse so that the private trust company has a complete picture of the total cost of services. It may be appropriate for the private trust company to compare these anticipated fees with other service providers in the same industry.

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(c) Location

A private trust company may consider the location of the service provider as an important factor in making its selection. For example, it may be beneficial to have an administrative service provider located in the state in which the private trust company is licensed to operate as well as one in the state where the family is located. It could also be helpful to have attorneys and accountants in the states where the private trust company operates as well as the states that govern the client accounts (if they are different). In some cases, a private trust company may be required to hire a local service provider to satisfy the private trust company's regulatory requirements (such as a bank for the private trust company's funds or a resident director or officer).[7]

7 As described in footnote 2 above, Nevada and Wyoming both require a licensed (or chartered) private trust company to maintain a bank account at a state-chartered or national bank having a principal or branch office in the state. Florida, South Dakota, and Ohio all require an individual who is a resident of the state to be a director of the private trust company. Fla Stat § 662.125(2); SD Codified Laws § 51A-6A-13; Ohio Rev Code Ann § 1112.14(E)(1). Texas requires at least a majority of the directors to be residents of the state. Tex Fin Code Ann § 183.103(a). Other states, such as Nevada, require an individual who is a resident of the state to be an officer of the private trust company. Nev Rev Stat § 669A.140(1) (for licensed family trust companies).

(d) Financial strength and viability

Before engaging a service provider, the private trust company should review the financial strength and viability of that company or its parent company. This may involve reviewing financial statements, audit reports and state records as well as searching for pending or threatened financial or legal claims. If the service provider enters bankruptcy, is involved in a litigation matter or otherwise closes its doors, it will not only disrupt the services provided to the private trust company and its client accounts but it also may entangle the private trust company in those proceedings.

(e) Audit or supervisory evaluations

Depending on the functions being outsourced, the private trust company may want to request any audit or supervisory evaluations prepared for the service provider. This will ensure that the service provider is in compliance with all applicable regulations, has the authority and ability to provide the requested services, and is generally in good standing.

(f) Policies, procedures and controls

The private trust company should, and in some cases must, review certain policies, procedures, and controls of the service provider. It is important that the private trust company engage service providers that maintain similar operating policies and procedures as the private trust company, have appropriate internal controls, and generally have business standards that correspond to the private trust company's business standards. This will ensure consistent and high quality services for the private trust company and its client accounts.

Some states, like Nevada and New Hampshire,[8] require private trust companies to have business continuation plans as well as physical and information security policies. If the private trust company is engaging a service provider for office space or to maintain its records, then the private trust company likely will need to rely on the business continuation plans and physical and information security policies adopted by the service provider. Therefore, the private trust company should review the service provider's policies to make sure they are consistent with the objectives of the private trust company and satisfy the applicable state regulatory requirements.

8 Neither the Nevada Family Trust Companies Act (Nev Rev Stat § 669A *et seq*) nor the New Hampshire Family Trust Company Act (NH Rev Stat Ann § 383-D et seq (West 2019)) specifically require a private trust company to have a business continuation plan, information security policy or physical security policy. However, the examination guidelines and document request forms issued by both states request copies of these policies (and the private trust company's compliance with such policies) during the periodic regulatory examinations. Similar policies may be required during the examinations conducted by other states as well.

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(g) Insurance coverage

It also is prudent for the private trust company to look at whether the service provider has insurance coverage for the services it provides and whether the private trust company believes the amount of coverage is sufficient. If there is an issue down the road with the relationship, it is important that the private trust company knows the service provider has the necessary insurance protection.

(h) Conflicts of interest

A private trust company may wish to engage a service provider that is affiliated with the private trust company, the family for which it operates, or one or more of its directors, committee members or officers. In determining whether to engage this service provider, it is necessary for the private trust company to identify any conflicts of interest that may exist and to address those conflicts in its due diligence. See below for a more thorough discussion regarding conflicts of interest between private trust companies and affiliated service providers.

A conflict of interest may arise even when the private trust company and service provider are not affiliated. For example, some service providers sell certain products or have certain arrangements that they recommend to their clients. This type of relationship may not align with the goals of the private trust company and its client accounts, in which case the private trust company should not enter into the engagement or should clearly identify the appropriate parameters of the service provider relationship up front to avoid a conflict in the future.

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(i) Confidentiality

Engaging a service provider will undoubtedly result in certain information about the private trust company and/or its client accounts being disclosed to that service provider. Many families are sensitive to this type of disclosure so it is important for the private trust company to review the confidentiality policy of any intended service provider and ensure that the policy appropriately limits the exposure of sensitive information. If a service provider does not have a confidentiality policy, the private trust company should consider adding confidentiality provisions to the service provider agreement or having the service provider sign a separate confidentiality agreement to protect family and trust information.

On the other side, a private trust company may be asked to sign a confidentiality agreement for information it receives from the service provider (like its fees), or the services agreement provided by that service provider may contain such language. This likely will come up in the private trust company's due diligence of the service provider or in the negotiations of the terms of the arrangement. The private trust company should carefully review any proposed confidentiality provisions to ensure that they do not restrict the private trust

company's ability to disclose information to its auditors and regulators. Standard confidentiality provisions often include a broad prohibition against disclosure to third parties, and a private trust company should avoid placing itself in a position where it may need the service provider's consent to disclose information to an auditor, regulator or other similar party.

The importance of each of the above factors will vary depending on the services being requested and the type of service provider. Additional factors also may need to be considered for certain relationships (such as investment management and advisory services which are discussed below). Regardless of the various considerations, the private trust company should have a consistent practice for selecting – and documenting the due diligence associated with the selection of – service providers.

3.2 Services agreements

Once a service provider is selected, the private trust company should enter into a written agreement with that service provider to govern the terms of the arrangement. The agreement should clearly outline the respective responsibilities, rights, obligations and liabilities of the parties but also should be flexible where possible and appropriate. The following provisions typically should be included in any agreement with a service provider:[9]

- responsibilities of each party;
- fee to be paid for such services (or the basis for determining the fee) and any expense reimbursements or cost-sharing arrangements;
- frequency of invoices and timing of payments;
- standards for maintaining and retaining documents by both parties, confidentiality of such documentation, and when and how such documentation may be disclosed;
- right of either or both parties to receive any audit or examination reports prepared for the other party;
- right of an examining agency of one party to access the records of the other party related to the services being provided;
- ability of one party to conduct an audit of the other party's operations (usually at the requesting party's expense);
- required insurance coverage (where applicable);
- indemnification and liability of each party;
- procedures for renewing, amending and terminating the agreement;
- return or destruction of hard copies and digital records of all files after termination of the arrangement; and
- dispute resolution and choice of venue for any conflicts regarding the agreement.

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9 See FDIC Trust Manual, *supra*, at Section 10.G.3.

Generally, legal counsel for the private trust company should be involved in drafting and/or reviewing the agreements with service providers, especially those service providers that will provide critical services to the private trust company or its client accounts. These written agreements should be kept with the private trust company records and reviewed periodically to ensure they accurately capture the terms and conditions of the service provider arrangements over time.

3.3 Notifying clients of service provider

In general, a private trust company is not required to affirmatively disclose the use of service providers to its clients. In some cases, however, it may be appropriate or even necessary for the private trust company to disclose such engagements. The method and amount of disclosure will depend on the private trust company's governing documents and applicable law and may vary by service provider and the nature of services. The more services a private trust company delegates, and in particular the more critical services it delegates, the more it would seem that the private trust company should disclose the service provider arrangements to its clients as best practice, even if not required by applicable law or regulations.[10] However, each private trust company should evaluate whether to disclose service provider arrangements on a case-by-case basis and discuss with legal counsel.[11]

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3.4 Monitoring a service provider

It is one thing for a private trust company to monitor its own directors, officers and employees where it has full control and oversight. It is more difficult for a private trust company to maintain oversight over a service provider that has its own goals and purposes, its own business plan and management, its own policies and procedures, and its own officers and employees. Nonetheless, the private trust company should regularly review and monitor its service providers.

In reviewing service providers, the private trust company should consider the following criteria as it deems appropriate:

- experience and performance;
- business reputation;
- financial condition;
- insurance coverage;
- compliance with legal and regulatory requirements;

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10 See FDIC Trust Manual, *supra*, at Section 10.G.5.

11 Some states, such as New Hampshire, require a private trust company to notify the applicable banking commissioner or state regulatory agency when it engages or terminates an accounting firm to audit the private trust company's financial statements and when it obtains or changes a fidelity bond or errors and omissions insurance policy from an insurer. The private trust company should review all applicable regulations to ensure that it provides any required notices to the appropriate parties.

- key personnel and ability to retain essential knowledge in support of the activities;
- information technology used;
- business continuation plans;
- use of subcontractors;
- scope of controls, privacy protections and audit programme; and
- the amount of fees paid relative to the value added by the service provider.

Summaries of each service provider arrangement can be prepared and maintained by the private trust company to aid in its review. These summaries should document the scope of services provided to the private trust company, contact information, cost of services, renewal terms and any other pertinent information regarding the service provider relationship.

As a matter of best practice, the private trust company should review each service provider, using the service provider summaries where appropriate, regularly (eg, annually) or otherwise as circumstances dictate. If there is an issue with a particular service provider, the private trust company should review that service provider more frequently until the issue is resolved to the satisfaction of the private trust company (or the relationship is terminated). If the private trust company has a longstanding relationship with a service provider and no issues have come up with that service provider, it may be appropriate for the private trust company to review that service provider on a less frequent basis. Each review should be documented in the files of the private trust company.

3.5 Terminating a service provider

If the private trust company determines that a service provider is no longer necessary or is no longer providing quality services, the private trust company should terminate the service provider arrangement. If there is a written agreement in place, the private trust company should review the terms of that agreement and follow the appropriate steps to terminate the relationship. If there is no written agreement or the agreement is silent on a party's right to terminate, the private trust company should examine the appropriate state law to determine the process for terminating the arrangement. Legal counsel should be involved any time the private trust company is considering terminating a service provider.

Upon termination, the private trust company should complete any of its remaining obligations under the agreement and ensure that the service provider does the same. This may include paying outstanding fees, executing documents, returning documents, and collecting work papers and confidential information. Should a disagreement arise in the termination, legal counsel should be consulted and the dispute resolution provisions of the agreement should be followed (where applicable and appropriate).

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4. Affiliated service providers

A private trust company may wish to engage a service provider that is owned or controlled by the same family that owns and/or controls the private trust company, or by one or more decision makers for the private trust company (an 'affiliated service provider'). Frequently, this could be a family office engaged for administrative services, a family investment management company engaged for investment services, or another entity providing services to the private trust company. Hiring an affiliated service provider may have significant benefits for the private trust company and the family. There likely will be efficiencies in the management and operations of the private trust company and the affiliated service provider, consistent business philosophies, a general understanding of the family and its unique circumstances, greater privacy, and lower overall costs for the family's operations. That said, the affiliated nature of these arrangements may raise some additional considerations that are not present with a third-party service provider.

Engaging an affiliated service provider could under certain circumstances be considered self-dealing for the fiduciary decision makers of the private trust company (and the private trust company itself) or a general conflict of interest for the non-fiduciary actors of the private trust company. Therefore, before engaging an affiliated service provider, the private trust company should review the trust instrument and applicable state law to determine if and how it can engage that affiliated service provider. In some cases, it may be appropriate for the private trust company to notify the trust beneficiaries of the engagement or take certain other actions to avoid any misunderstandings or issues in the future. The private trust company should consult legal counsel when making this determination.

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Once the private trust company determines that it can engage an affiliated service provider, it should address any potential conflicts of interest attending such engagement. The private trust company should have a policy of discussing if and when its decision makers can engage in transactions on behalf of the private trust company, or any client accounts in which those individuals may have a potential conflict (including hiring an affiliated service provider). Generally, this policy should include a process for the private trust company to identify potential conflicts, review those potential conflicts to determine whether they can be managed or resolved, and, if they can, approve the transaction despite the potential conflict. Regardless of the process used, the private trust company should ensure that it is acting within its duty of loyalty and in the best interests of its client accounts when engaging an affiliated servicer provider.

The use of affiliated service providers is extremely common and provides many benefits for the private trust company. Notwithstanding the additional considerations discussed above, most private trust companies make use of some

form of affiliated service provider, consistent with applicable law and regulations.

5. Investment advisory and management service providers

Many private trust companies engage service providers to invest and manage the assets of their client accounts. Even private trust companies with in-house investment professionals may still hire outside investment service providers. Engaging investment service providers has its own set of considerations that private trust companies should be aware of as they enter into those arrangements. Notably, it is important for a private trust company to understand if and when it is formally delegating investment authority to an investment service provider and when it is simply engaging an investment service provider for advice. The terms of these engagements and the responsibilities and liability of the private trust company in each situation vary significantly.

In the United States, many states have adopted the Uniform Prudent Investor Act, which requires a trustee to "invest and manage trust assets as a prudent investor would, by considering the purposes, terms, distribution requirements, and other circumstances of the trust".[12] The prudent investor rule is the default rule governing a trustee's investment of trust assets.[13] It can be expanded, restricted or otherwise modified by the terms of the trust instrument.[14] Therefore, a private trust company, like any trustee, will be subject to the terms of the trust instrument, the prudent investor rule, or both, when making investment decisions for a trust account. If a private trust company engages another party to provide investment management or advisory services to its client accounts, the private trust company must ensure that the service provider is familiar with the prudent investor rule and the trust instruments so they can manage the trust investments accordingly.

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5.1 Delegation to investment service provider

The Uniform Prudent Investor Act, which has been adopted at least in part by most states in the United States, allows a trustee to delegate its investment and management functions to a third party.[15] In doing so, the trustee must "exercise reasonable care, skill, and caution in (1) selecting an agent; (2) establishing the scope and terms of the delegation, consistent with the purposes and terms of the trust; and (3) periodically reviewing the agent's actions in order to monitor

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12 Uniform Prudent Investor Act § 2(a) (Unif Law Comm'n 1994) (UPIA).

13 UPIA § 1(b). For example, a trust instrument may require that the trustee hold a certain asset or asset class indefinitely, allow the trustee to maintain investments without maintaining a diversified portfolio, or permit the trustee to take on additional investment risk that would otherwise not be permitted under the prudent investor rule.

14 *Ibid.*

15 UPIA § 9(a).

the agent's performance and compliance with the terms of the delegation".[16] This delegation "is not limited to the performance of ministerial acts. In appropriate circumstances, delegation may extend, for example, to the selection of trust investments or the management of specialised investment programmes, and to other activities of administration involving significant judgments."[17] For example, in *In the Matter of the Estate of Younker*, the Surrogate Court of New York County held that a corporate trustee was permitted to delegate its investment authority over four trusts to a family financial adviser.[18] The court found that the terms of the will establishing the trusts explicitly permitted the trustee to utilise various agents to provide investment advice and permitted the trustee to delegate discretionary powers.[19] The trustee asserted that it exercised reasonable care, skill and caution in selecting the family financial adviser as the investment service provider for the trusts, that it would maintain continued oversight over the adviser, and that the engagement would be cost-effective for the trusts.[20] Given this arrangement, the court concluded that the trustee was permitted to make a complete delegation of its investment authority under the terms of the trusts and the Uniform Prudent Investor Act.[21]

If a trustee complies with all of the requirements of the Uniform Prudent Investor Act (or the applicable state law) for an effective delegation, that trustee should not be liable to the beneficiaries or to the trust for the decisions or actions of the agent selected by the trustee.[22] Instead, the agent will have a duty to the trust to exercise reasonable care to comply with the terms of the delegation and therefore should be liable to the trust directly for any breach of that duty.[23] In *O'Neill v O'Neill*, the court examined whether the trustees of a trust breached their fiduciary duty to the trust beneficiaries by delegating investment authority to Merrill Lynch when the trust assets declined from over $600,000 to approximately $37,000.[24] In its analysis, the court reviewed the facts in light of the Ohio Prudent Investor Act, which adopts the same three requirements for delegation as the Uniform Prudent Investor Act. Here, the terms of the trust expressly permitted the trustee to "delegate discretionary powers to, and rely upon the advice and option of suitable agents and attorneys, but shall not be liable for their neglect, omission, or wrongdoing if reasonable care is exercised in their selection".[25] The court found that the scope of delegation was consistent with the terms of the trust and that the trustee

16 *Ibid.*
17 Restatement (Third) of Trusts Rule § 80, cmt e (Am Law Inst 1992).
18 174 Misc 2d 296 (1997).
19 *Ibid* at 299.
20 *Ibid.*
21 *Ibid.*
22 UPIA § 9(c).
23 UPIA § 9(b).
24 169 Ohio App 3d 852, 861 (2006).
25 *Ibid* at 855.

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monitored the investment service provider by reviewing quarterly and annual statements for the trust investments. In light of these facts, the court held that the trustees did not breach their fiduciary duties and were not liable to the beneficiaries for the decrease in the trust assets.[26]

If permitted by the trust agreement and applicable law, a private trust company may make a complete and effective delegation of its investment authority to an investment service provider. In doing so, the private trust company should not be liable for the actions of the investment service provider. However, it is important that the private trust company and investment service provider are clear about the delegation and shift in responsibility, and that all of the appropriate steps are taken to make an effective delegation. If not, the private trust company may still be liable for the investment activities of the trust even if an investment service provider is acting.

5.2 Engagement for investment advice

A trustee can engage an investment service provider for guidance and advice and not make a complete delegation of its investment responsibility. In this case, the trustee will remain responsible to the beneficiaries and the trust for its investment decisions as opposed to shifting that liability to the investment service provider.

In *Ewing v Ruml*, the income beneficiary of a trust claimed that the trustee breached its fiduciary duties by delegating its investment responsibilities to an outside agent.[27] Unlike in I*n the Matter of the Estate of Younker and O'Neill v O'Neill*, this court concluded that the trustee did not delegate its investment authority to the outside investment service provider but rather only consulted with that investment service provider on a variety of investment matters.[28] Therefore, the court only examined the trustee's liability and did not attribute any liability to the investment service provider.[29] An engagement for investment advice (as opposed to a formal delegation) is usually the default arrangement and the one typically preferred by investment service providers.

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5.3 General considerations

Regardless of whether a private trust company engages an investment service provider by way of formal delegation or only for investment advice, the private trust company should exercise care and diligence in selecting that investment service provider and document its due diligence in the private trust company records. In making its selection, the private trust company should consider:

- the investment adviser's credentials, resources, ownership structure, stability, conflicts of interest and experience;

26 *Ibid* at 859.
27 892 F.2d 168 (2d Cir 1989).
28 *Ibid* at 172.
29 *Ibid*.

- internal investment management strategies and external investment managers used by the investment adviser, and their respective absolute and relative performance;
- reporting capabilities;
- asset allocation and portfolio construction planning;
- communications;
- relationships, if any, with the private trust company or the family;
- fees and overall costs; and
- general reputation and references.

The private trust company also should maintain ongoing oversight and periodically review the investment service provider (even with a formal delegation). This could be done by formal meetings, telephone calls, receipt of periodic statements, online access to account information, or in another manner that gives the private trust company sufficient information about the investment service provider's actions and the performance of the investments. It is generally recommended that the private trust company review an investment service provider at least annually. However, depending on the investments and the private trust company's relationship with the investment service provider it may be prudent to review more frequently. All such reviews should be documented in the records of the private trust company or client account.

6. Adherence to policies and procedures

Many private trust companies have policies and procedures in place to guide the selection, due diligence, documentation and termination of its service provider relationships. Any such policies and procedures should be followed by the private trust company for each service provider engagement. If a private trust company does not have these policies and procedures in place, it should consider adopting them to provide consistent guidelines to govern the private trust company's service provider arrangements.

7. Conclusion

Overall, service providers are an important and often necessary piece of a private trust company's operational framework. Regardless of whether a private trust company utilises only one service provider or dozens, the private trust company should be mindful of the various considerations associated with each of those arrangements in order to promote the effective and efficient management of the private trust company and its client accounts.

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