



FIRMA

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Training Conference

Top Risk Issues Facing Corporate Trust  
In Today's "Heightened Standards" World

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# Top Risk Issues Facing Corporate Trust in “Heightened Standards” World



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## Today's Topics

- Setting the Table – Corporate Trust
  - Indenture Trustee and other Trustee Appointments
  - Multiple Agent Level Appointments
- Internal Oversight – Mitigating Risks
  - The First Line of Defense: The Business
  - The 2<sup>nd</sup> and 3<sup>rd</sup> Lines
- Regulators and Regulatory Risks
  - Multiple agencies, multiple perspectives
- Where does all this lead? Risks from Claims in Litigation and Court Decisions
  - Unprecedented challenges and precedents being made
- Lessons to Learn

# Top Risk Issues Facing Corporate Trust in “Heightened Standards” World

## Setting the Table: “But We’re Different!”

- Reg. 9 and the Indenture Trustee
  - Directed prior to Event of Default
  - Is a “Prudent Person” a Fiduciary?
  - Corporate Trustee do not accept discretion

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## Setting the Table: “But We’re Different!”

### *Are your deals Wolves in wolves’ clothing?*

- Other Trustee Appointments
  - Often incorrectly administered as escrows
  - Getting client direction does not remove fiduciary duties

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## Setting the Table: What do your agreements say?

- Other Agency Appointments
  - Escrow Agent
  - Collateral Agent
  - Depository
  - Account Bank
- Non-Standard account agreements

**Are you sure discretionary, unwanted, or otherwise misunderstood language is not hidden away in your deal docs?**

# Top Risk Issues Facing Corporate Trust in “Heightened Standards” World

## Internal Oversight: Procedures, Controls, Testing

- The First Line of Defense: The Business
  - Owner of risk
  - Understand the risks
- Process evaluation (mapping or flows)
  - Risk identification
  - Inherent Risk
  - Controls
  - Residual Risk

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## Internal Oversight: Procedures, Controls, Testing

- Procedures
  - The age old question: Is less really more or is more truly more?
  - Appropriate levels of detail to be useful, but not so much that when you move your inbox, you need to change your procedures
  - Procedures are not controls – they contain controls

And remember . . .

Adherence to procedures is beneficial to mitigate not only operational, but also litigation risks



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## Internal Oversight: Procedures, Controls, Testing

- Other Controls
  - Segregation of Duties
  - Dual Control
  - Maker / Checker
    - Multiple Checkers?
  - System Permissions
  - Authorizations and Limits
- Controls should leave audit trails

Effective Controls are Measurable and Testable

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## Internal Oversight: Procedures, Controls, Testing

- The First Line: Testing
  - Business should either conduct its own testing or otherwise validate effectiveness of controls
  - Testing is owned by First Line, though should be arm’s length and independent
  - Focus on High Risk items, i.e.:
    - Documents (account reviews)
    - Payments (authorizations and approvals)
    - Cash flows or waterfall calculations (financial models)
    - Coding changes (system permissions)

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## Internal Oversight: When did we get so many lines?

- Second and Third Lines of Defense
  - Need to be partnerships and collaborations!
    - Not competitions
  - Collectively manage resolution of identified issues

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## The Regulators and Regulatory Risks

- Multiple agencies, multiple individuals = multiple perspectives
  - “ . . . but I know it when I see it!”
- A relationship which is better without surprises
  - both ways
- You should be regularly discussing:
  - Areas of Regulatory focus
  - Changes to the business
  - Interpretation of Regulations

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## The Regulators and Regulatory Risks

- Regulations
  - Application of existing Regulations: “Look what I found!”
  - New Regulations
  - “Regulatory Creep”
    - Reg. AB

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## Risks from Claims in Litigation and Court Decisions

- Corporate Trust deals typically include corporate entities (escrows, project finance) and investors (debt financings) both sophisticated and small
  - If something goes wrong, someone points the finger at the bank . . . REGARDLESS
- Unprecedented claims are being made in lawsuits
  - Any and every time you stepped beyond the 4-corners of your agreement
  - Any and every time you did not follow your agreement
  - Every list and procedure
  - Every issue identified: self-ID’ed; compliance ID’ed; audit ID’ed, regulator ID’ed

**All are subject to the discovery process and will be used by plaintiffs**

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## Risks from Claims in Litigation and Court Decisions

- Post financial meltdown, courts have been sympathetic to claims made, including:
  - Implied discretionary or fiduciary duties raising our levels of care from being directed by
    - Simply being named a “trustee”
    - Exercising “discretion” therefore extending role beyond the contracted duties
    - Regulations overriding account documents
  - Citing any examples of “missteps” by bank to demonstrate pattern of negligence
    - Failing to follow any bank procedures or industry best practices
    - Existing or previous issues as evidence of ongoing negligence
- Court decisions have established “bad” precedents which may be followed in the future
- Corporate Trustees have settled rather than risking the above, further emboldening claims

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## Lessons to Learn: Ways to Mitigate Top Risks

- Know Your Book of Accounts – Know what your accounts agreements say
  - Strong acceptance process
  - Experienced, reliable People
- Strong, workable procedures
  - Identified risks with mitigating controls
- Testing program
- Collaborative relationships between LOB, Risk Partners and Regulators
- Need to stay current on application of existing and new Regulations