

# Regulator Open Session

Fiduciary and Investment Risk  
Management Association, Inc.  
Conference

## Federal Reserve Bank of Boston

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# Disclaimer

Any views that I express here are my own and may not necessarily reflect those of the Board of Governors of the Federal Reserve, my colleagues in Federal Reserve System or the Federal Reserve Bank of Boston.

# Role of the Federal Reserve

As Central Bank of the United States, the Federal Reserve has four general duties:

- Conducting the nation's monetary policy by influencing the money and credit conditions in the economy in pursuit of full employment and stable prices;
- **Supervising and Regulating banking institutions to ensure the safety and soundness of the nation's banking and financial system and to protect the credit rights of consumers;**
- Maintaining the stability of the financial system and containing systemic risk that may arise in financial markets; and
- Providing certain financial services to the US government, to the public, to financial institutions, and to foreign official institutions, including playing a major role in operating the nation's payment system.

# Organization of the Federal Reserve



# Supervisory Approach and Organization

- Consolidated Supervisor of Financial Holding Companies (FHCs) and Bank Holding Companies (BHCs)
  - Non-bank subsidiaries
  - Foreign subsidiaries
- Primary regulator of State Member Banks
- Edge Act and Agreement Corporations

# Supervisory Approach and Organization (cont'd.)

- Other Supervisory and Regulatory responsibilities (for discussion only - not an inclusive list):
  - Monitoring compliance with anti-money-laundering provisions of the Bank Secrecy Act and USA Patriot Act
  - Protecting consumers in credit and deposit transactions
  - Regulating transactions between banking affiliates

# Supervisory Approach and Organization (cont'd.)

- Ongoing supervision
  - Largest, most complex organizations
  - Dedicated teams and specialists
  - Cross institution perspectives
- On-site examinations and inspections
  - Periodic
  - Elevated risk profiles
- Off-site monitoring

# Supervisory Approach and Organization (cont'd.)

- Coordination with, and reliance on primary bank regulators and foreign and functional regulators
  - OCC
  - OTS
  - FDIC
  - SEC
  - State Banking
  - State Ins. & Sec.
- Leveraging internal risk control and risk mitigation functions
  - Internal audit
  - Corporate compliance
  - Enterprise risk management



# Horizontal Perspective

- Peer Groups
  - By business and product lines
  - Strategies and objectives
  - Institutional size and complexity
- Knowledge-Sharing Forums
  - Discuss emerging issues and broader risks
  - Identify and share leading practices and institutional response
  - Foster cross communication among dedicated teams and various specialty areas

# Topical Issues

The following topics represent a sample of issues currently being discussed as broad matters of potential supervisory interest. This list is not comprehensive and will vary in relevance among institutions.

# Topical Issues (cont'd.)

- Utilization of Alternative Investments (e.g. hedge funds and private equity funds) for fiduciary clients.

# Topical Issues (cont'd.)

- Key considerations
  - Prevalence of use
  - Suitability
  - Conflicts
  - Disclosures
  - Liquidity
  - Pricing and valuation

# Topical Issues (cont'd.)

- Annual review all assets of each fiduciary account for which the bank has investment discretion to evaluate whether they are appropriate, individually and collectively, for the account.

# Topical Issues (cont'd.)

- Key considerations
  - comprehensiveness of reviews (e.g. all asset classes including special assets)
  - degree of automation in this process
  - tracking committee decisions/actions/follow up on portfolio exceptions

# Topical Issues (cont'd.)

- Open Architecture / Participation of Investment Advisors in Selecting Investments for Trust Accounts

# Topical Issues (cont'd.)

- Key considerations
  - Identification and nature of product offerings
  - Fee structures
  - Performance evaluation and measurement of manager performance
  - Audit/compliance/risk management processes
  - Committee structure and reporting



# Topical Issues (cont'd.)

- Assess the possible effects of the trend toward limiting / freezing defined benefit pension plans and managing the accelerated transfer of pension & retirement funding from employers to individuals.

# Topical Issues (cont'd.)

- Key considerations
  - How have financial institutions altered business planning and strategies in light of this trend?
  - How will this altered business mix affect profitability?
  - What does management see as the major risks and/or challenges and their influence on business decisions?

# Topical Issues (cont'd.)

- Key considerations
  - Do companies anticipate any capacity issues or heightened operational and/or compliance risks as greater numbers of employee-based accounts take the place of single “Plan-based” accounts?
  - For plans that have been frozen – how will investment styles and objectives change over time and how will advisors and administrators accommodate these changing needs?
  - How are BHC/FHC/Banks’ addressing this relative to their own employees plans?

# Continuous Challenges of Risk Management

- Ensure that organizations understand the risks of their activities and their potential impact
- Risks must be recognized and managed across the organization
- Consider the multi-faceted nature of risks (credit, market, operational, compliance) and their linkage to corporate strategies
- Introduction of new products and new strategies
- Operating in more concentrated yet global markets
- Aggregation, elevation and accountability

# Questions

# Biography

**Tim MacDonald** is the Director of Fiduciary Risk Management in the Bank Supervision, Regulation and Credit Department at the Federal Reserve Bank of Boston. In this capacity he is responsible for overseeing efforts to enhance the overall quality of supervision with respect to operational risks associated with fiduciary activities and enhance knowledge management and consistency of approach.

Tim has over 24 years experience in the financial services industry including supervision and regulation, advisory, retail and commercial banking and securities trading and portfolio management. His regulatory experience includes 14 years with the Federal Reserve System where he has been actively engaged in addressing many of the industry's leading issues including, preparation efforts for the Basel II Capital Accord, corporate governance, enterprise-wide risk management, mutual fund market timing transgressions, Mergers & Acquisitions and peripheral risks attendant to industry consolidation.

In his previous assignment as Directing Examiner and Central Point of Contact Tim lead high-level teams dedicated to supervising Large Complex Banking Organizations. He was responsible for all areas of supervision, including Basel II preparedness and economic capital reviews, and collaborated extensively with other bank regulatory agencies (both domestic and international). Tim is frequently called upon to lend his expertise to strategic initiatives for the Boston Reserve Bank and at a System level, and has addressed internal and industry groups on the topic of the Federal Reserve's supervision program.

Tim has been a CFA charterholder since September, 2000, he received an MBA in Finance from Northeastern University and a BA in Economics from Fairfield University.