

**Meeting between Federal Reserve Board Staff
and Representatives of the American Bankers Association
March 23, 2011**

Participants: Cecilia Calaby and Phoebe Papageorgiou (American Bankers Association); Jason Doren (Silicon Valley Bank); Simon Zornoza (State Street); John C. Tolleson, John C. Tolleson, Jr., and Phillip Taken (Tolleson Wealth Management); and Victor Siclari (Bank of New York Mellon); and Timothy Keehan and Andy Miller (PNC)

Brian Knestout and Christopher Paridon (Federal Reserve Board)

Summary: Staff of the Federal Reserve Board met with representatives and members of the American Bankers Association (“ABA”) to discuss the restrictions on proprietary trading and hedge fund and private equity fund activities under section 619 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (also known as the “Volcker Rule”).

Among matters discussed in the meeting were the ABA’s views regarding: the statute’s definition of “hedge fund and private equity fund” and its impact on mutual funds, exchange-traded funds (“ETFs”), and other fund structures; the definition of “customer” related to the exemption for organizing and offering a covered fund; the scope of the so-called “super 23A” prohibition, particularly with respect to traditional trust and custody functions of banking entities; and the definitions of “sponsor” and “banking entity” under the statute.

A copy of materials provided by ABA in connection with this meeting is attached.

Materials on Directed Trustees

Directed Trustees under Banking Regulation

FRB-SEC Regulation R: Defines “directed trustee” as a trustee that does not exercise investment discretion (see 12 CFR 218.760(h)(3)). Also allows accounts for which a bank acts as directed trustee to be treated as custody accounts (see 12 CFR 218.760(h)(1)(iv)).

Directed Trustees under ERISA

[Department of Labor Field Assistance Bulletin 2004-03](#)

Article on Directed Trustees: <http://www.mnat.com/articles-publications-202.html>

Directed Trustee Statutes cited in Article:

12 Delaware Code Section 3313. Advisers.

(a) Where 1 or more persons are given authority by the terms of a governing instrument to direct, consent to or disapprove a fiduciary's actual or proposed investment decisions, distribution decisions or other decision of the fiduciary, such persons shall be considered to be advisers and fiduciaries when exercising such authority unless the governing instrument otherwise provides.

(b) If a governing instrument provides that a fiduciary is to follow the direction of an adviser, and the fiduciary acts in accordance with such a direction, then except in cases of wilful misconduct on the part of the fiduciary so directed, the fiduciary shall not be liable for any loss resulting directly or indirectly from any such act.

(c) If a governing instrument provides that a fiduciary is to make decisions with the consent of an adviser, then except in cases of wilful misconduct or gross negligence on the part of the fiduciary, the fiduciary shall not be liable for any loss resulting directly or indirectly from any act taken or omitted as a result of such adviser's failure to provide such consent after having been requested to do so by the fiduciary.

(d) For purposes of this section, "investment decision" means with respect to any investment, the retention, purchase, sale, exchange, tender or other transaction affecting the ownership thereof or rights therein, and an adviser with authority with respect to such decisions is an investment adviser.

(e) Whenever a governing instrument provides that a fiduciary is to follow the direction of an adviser with respect to investment decisions, distribution decisions, or other decisions of the fiduciary, then, except to the extent that the governing instrument provides otherwise, the fiduciary shall have no duty to:

- (1) Monitor the conduct of the adviser;**
- (2) Provide advice to the adviser or consult with the adviser; or**
- (3) Communicate with or warn or apprise any beneficiary or third party**

concerning instances in which the fiduciary would or might have exercised the fiduciary's own discretion in a manner different from the manner directed by the adviser.

Absent clear and convincing evidence to the contrary, the actions of the fiduciary pertaining to matters within the scope of the adviser's authority (such as confirming that the adviser's directions have been carried out and recording and reporting actions taken at the adviser's direction), shall be presumed to be administrative actions taken by the fiduciary solely to allow the fiduciary to perform those duties assigned to the fiduciary under the governing instrument and such administrative actions shall not be deemed to constitute an undertaking by the fiduciary to monitor the adviser or otherwise participate in actions within the scope of the adviser's authority.

(f) For purposes of this section, the term "adviser" shall include a "protector" who shall have all of the power and authority granted to the protector by the terms of the governing instrument, which may include but shall not be limited to:

(1) The power to remove and appoint trustees, advisers, trust committee members, and other protectors;

(2) The power to modify or amend the governing instrument to achieve favorable tax status or to facilitate the efficient administration of the trust; and

(3) The power to modify, expand, or restrict the terms of a power of appointment granted to a beneficiary by the governing instrument.

Uniform Trust Code [SECTION 808. POWERS TO DIRECT.](#)

(a) While a trust is revocable, the trustee may follow a direction of the settlor that is contrary to the terms of the trust.

(b) If the terms of a trust confer upon a person other than the settlor of a revocable trust power to direct certain actions of the trustee, the trustee shall act in accordance with an exercise of the power unless the attempted exercise is manifestly contrary to the terms of the trust or the trustee knows the attempted exercise would constitute a serious breach of a fiduciary duty that the person holding the power owes to the beneficiaries of the trust.

(c) The terms of a trust may confer upon a trustee or other person a power to direct the modification or termination of the trust.

(d) A person, other than a beneficiary, who holds a power to direct is presumptively a fiduciary who, as such, is required to act in good faith with regard to the purposes of the trust and the interests of the beneficiaries. The holder of a power to direct is liable for any loss that results from breach of a fiduciary duty.

Comment

Subsections (b)-(d) ratify the use of trust protectors and advisers. Subsections (b) and (d) are based in part on Restatement (Second) of Trusts § 185 (1959). Subsection (c) is similar to Restatement (Third) of Trusts § 64(2) (Tentative Draft No. 3, approved 2001). "Advisers" have long been used for certain trustee functions, such as the power to direct investments or manage a closely-held business. "Trust protector," a term largely associated with offshore trust practice, is more recent and usually connotes the grant of greater powers, sometimes including the power to amend or terminate the trust. Subsection (c) ratifies the recent trend to grant third persons such broader powers.

A power to direct must be distinguished from a veto power. A power to direct involves action initiated and within the control of a third party. The trustee usually has no responsibility other than to carry out the direction when made. But if a third party holds a veto power, the trustee is responsible for initiating the decision, subject to the third party's approval. A trustee who administers a trust subject to a veto power occupies a position akin to that of a cotrustee and is responsible for taking appropriate action if the third party's refusal to consent would result in a serious breach of trust. See Restatement (Second) of Trusts § 185 cmt. g (1959); Section 703(g)(duties of cotrustees).

Frequently, the person holding the power is directing the investment of the holder's own beneficial interest. Such self-directed accounts are particularly prevalent among trusts holding interests in employee benefit plans or individual retirement accounts. See ERISA § 404(c) (29 U.S.C. § 1104(c)). But for the type of donative trust which is the primary focus of this Code, the holder of the power to direct is frequently acting on behalf of others. In that event and as provided in subsection (d), the holder is presumptively acting in a fiduciary capacity with respect to the powers granted and can be held liable if the holder's conduct constitutes a breach of trust, whether through action or inaction. Like a trustee, liability cannot be imposed if the holder has not accepted the grant of the power either expressly or informally through exercise of the power. See Section 701.

Powers to direct are most effective when the trustee is not deterred from exercising the power by fear of possible liability. On the other hand, the trustee does have overall responsibility for seeing that the terms of the trust are honored. For this reason, subsection (b) imposes only

minimal oversight responsibility on the trustee. A trustee must generally act in accordance with the direction. A trustee may refuse the direction only if the attempted exercise would be manifestly contrary to the terms of the trust or the trustee knows the attempted exercise would constitute a serious breach of a fiduciary duty owed by the holder of the power to the beneficiaries of the trust.

The provisions of this section may be altered in the terms of the trust. See Section 105. A settlor can provide that the trustee must accept the decision of the power holder without question. Or a settlor could provide that the holder of the power is not to be held to the standards of a fiduciary. A common technique for assuring that a settlor continues to be taxed on all of the income of an irrevocable trust is for the settlor to retain a nonfiduciary power of administration. See I.R.C. § 675(4).