PRIVATE TRUST GROUP OF AMERICA

Practice Management for Bank Trust Departments

Creating a Professional Oasis in a Retail Environment

(NOTE: The following article was contributed by John Larrabee, managing partner of a family trust practice in Charlotte, North Carolina and an advisor to Private Trust Group of America.)

Having spent the early part of my professional career working within and managing trust departments for large law firms, and later as the managing partner of a private family trust office, I have learned to appreciate the importance of a sound Practice Management program and the overall value it can add to the success of a professional organization. Admittedly, I was not an easy convert to the disciplined approach that characterizes a successful Practice Management program; but as I gradually began to see the positive results it could produce – not just in terms of profitability, but in terms of the quality of client relationships, the depth of professional commitment to each client and the reciprocal loyalty of each client to the individual attorney or firm, I gained a much better understanding and appreciation for the overall benefits it could bring to a firm and its clients.

It was with this commitment to the soundness of a good Practice Management program that I thought Sandi Lotito was onto something when she approached me with the idea of starting Private Trust Group of America. She, too, was familiar with the disciplined approach of working in a professional services environment where expectations are high and accountability is paramount to the overall success of the firm. Sandi also had experience with auditing bank trust departments, which gave her the impression that they could benefit greatly from some of the Practice Management principles she had learned over her long career in managing trust operations for large law firms and from her observations as a bank auditor.

What we both failed to understand is that the practices and expectations of a professional services firm are vastly different than those of bank trust departments, which is quite perplexing given the strong correlation between the professional nature of providing legal, accounting and investment services and those very similar services expected of a professional trustee. I believe the disconnect is directly attributed to the fact that most bank boards and executive committees view their trust departments and trust officers as just another part of retail banking when, in fact, they should be treated more like the professional service firms that they emulate.

The purpose of this paper is to discuss some similarities that bank trust officers share with other professionals such as attorneys, accountants and investment advisors, and to point out some of the advantages of treating them as a "professional services group" within the bank rather than just another part of retail banking. After all, providing trust services is a highly specialized profession that demands many of the same skills required of those professional groups. As an extension of that discussion, we will examine some of the advantages of establishing a Practice Management program to gain better control of the department's finances and improve its overall business focus.

Professional Similarities

Other than the obvious handicap of operating in a highly regulated business environment, bank trust officers and other professional trustees share many similarities with attorneys, accountants and investment advisors. They must have a sound knowledge of the legal doctrine of fiduciary law in order to understand and interpret trust agreements that are uniquely drafted to satisfy the whims of each client, as well as being mindful of nuances in the trust agreements that could pose legal challenges or result in potential conflicts between beneficiaries. Professional trustees must also be aware of the proper tax treatment of different types of trusts and apply accepted trust accounting standards to report all trust activity. In addition, they are expected to have at least a basic understanding of investment concepts and principles so they can be conversant with trust beneficiaries about their financial goals and objectives, asset allocation, risk tolerance, etc.

The similarities do not end there. Just as attorneys, accountants and investment professionals frequently occupy the central gatekeeper role in their clients' business, personal and financial affairs, many professional trustees also fill that role. Professional bank trustees, however, could do a much better job of earning that designation if they could only create the professional environment in which to do so. Adopting and actively managing a carefully designed Practice Management program will allow bank trustees to do just that – but they must first re-evaluate their current business model and learn how to distinguish themselves from retail banking.

Business Models and Attitudes Must Change

Before delving into the merits of establishing a professional services group and implementing a Practice Management program, it is important to take a critical look at some of the underlying reasons that bank trust departments are viewed as part of the retail culture of banking. Be forewarned that this section may not be well received by some trust department executives, but I hope it will cause others to take a thoughtful inventory of their current business model and realize that they may want to consider adopting some of the policies and practices of their more successful counterparts in the legal, accounting and investment professions.

Like many retail businesses, most banks are "run by the numbers", which results in department heads being so focused on the "budget" that they lose sight of what it takes to build a successful service business. Rather than building a "professional services practice", trust department executives struggle to increase last year's revenue by an arbitrary number, usually tied to inflation, while holding the line on expenses. This may, in part, be attributed to the transactional nature of retail banking, which has become commoditized to the point that banking services are not unlike selling widgets that may come in different sizes and shapes, but all with the same mark-up.

Bank trust departments have been drawn into this retail environment because senior management frequently lacks an appreciation for the professional nature of providing fiduciary services. The lack of appreciation can be pervasive throughout the bank and often filters down through every single position within the trust department, usually with the undesirable results of projecting a less than professional image to the bank's trust clients. In some cases, this lack of appreciation is justified.

Take the case of the manager of a $100 million trust department with five people in operations. When told that outsourcing operations could save him a minimum of three full time positions, his response was, "I know, but of the three people that I would have to let go, one has been with the bank for 13 years, one for 8 years and one for 5 years." His mistake was confusing "positions" with "people". Positions can, and in many cases should be eliminated. People, on the other hand, cannot be eliminated. If the position is no longer necessary, the person filling that position can be assigned to other duties within the department, re-assigned to another area of the bank or, as a last resort, terminated. It is admirable for a bank to provide a benevolent work environment, but it can and should be done without compromising the very reason of its existence – which is to make a reasonable profit.

I recently attended a conference of trust department executives from different parts of the country and had the opportunity to sit at one of the vendor sponsored dinners next to the manager of a $150 million trust department. During our dinner conversation, the subject of bank trust departments providing "advisor friendly" trust services to financial advisors came up. The conversation ended almost as soon as it began because this "trust department executive" could not get past the thought that he could never do business with financial advisors because they will not relinquish custody of their client's assets to the bank. Instead of listening to ways to mitigate the potential issues of a bank serving as a trustee without having full custody of its clients' assets, he could only count the number red flags that prevented him from even <u>considering</u> the idea – notwithstanding the fact that the OCC is satisfied that it can be done if some simple precautions are taken.

These are just two quick examples of the prevailing attitudes I have encountered when speaking with bank trust department executives from around the country. I could cite scores more – maybe even hundreds. Until these business models and attitudes change, no Board of Directors or Executive Management Committee worth its salt will ever give its trust department proper recognition. Recognition comes with respect, and respect must be earned. Until trust department executives understand that they operate in a professional world and not a retail environment, they will never earn that respect.

<u>Creating a Truly Professional Environment</u>

The legal and regulatory requirements of an institutional trustee represent the gold standard of the financial services world, and there is no greater calling in the banking industry than that of a professional trustee. Among many other responsibilities, a trustee must have an appreciation for the legal interpretation of trust documents and estate planning techniques; be current on new tax laws and regulations; have a clear understanding of trust accounting rules, principles and concepts, and possess at least a working knowledge of investments. In fact, much of the bank's trust business emanates from practitioners of the three professional disciplines of law, accounting and investment management, so it is within that professional circle that trust officers travel. Unfortunately, too many bank trust departments lack the Practice Management structure to effectively compete with their more successful competitors in those professions.

The trust department's physical surroundings should reflect the stature of a successful professional office but, more importantly, its people should have a very solid understanding of how the principles of law, accounting and investing affect their ability to perform their jobs and win the respect of their clients. Nothing will put a client more at ease than speaking with a trust officer who is knowledgeable about the legal, accounting and investment issues that affect his/her financial well-being, yet is confident enough in his/her gatekeeper role to call upon outside experts when necessary. And nothing will gain the attention, respect and accompanying support of senior bank management more than the high profile role model of a professional trust department executive and his/her staff.

Creating the right physical environment and having a professionally trained staff will have an enormous impact on overall attitude throughout the bank, but it is only window dressing unless accompanied by a formal Business Plan that has a comprehensive Practice Management program at its core.

A Business Plan Does Not Have to be Complicated, but it **MUST** be in Writing

Business plans for bank and trust company trust departments usually exist only in theory, if at all. Some trust department executives carry the concept around in their heads, but I have yet to meet one who has a formal, written Business Plan that sets out the goals and objectives for creating a successful department within the bank or trust company.

No matter how brilliant the trust executive is, a Business Plan floating around in his/her mind is not of much value unless it is transferred to a written document that can be shared with everyone who will have a role to play in its success – from the Board of Directors down to the lowest position within the trust department. The plan does not have to be the equivalent of one for a start-up company seeking equity financing, but it should provide sufficient detail to enable management to channel resources in the direction that offers the greatest opportunity for success.

A trust department's Business Plan should take a long range view of up to five years into the future, but it should also be a working document that is constantly monitored and adjusted to take into account new business opportunities and changing market conditions. Once the initial Business Plan has been drafted and accepted by senior management and staff, a formal review of the plan should be undertaken at the beginning of each fiscal year, and an informal review should be conducted approximately six months later to determine if any mid-year adjustments are necessary.

The Business Plan sets long-term departmental goals, creates the framework for implementing them and provides direction for achieving them. However, even the most brilliantly crafted Business Plan, complete with lofty goals, principles and ideas, cannot succeed unless it is accompanied by a Practice Management program that can transform it into the reality of a successful business.

I now live within a few miles of one of the big NASCAR tracks located just north of Charlotte, North Carolina, which has given me a new perspective on America's number one spectator sport – and the chance to apply an auto racing analogy to explain how ineffective a Business Plan is without an accompanying Practice Management program. A lot of time, energy and money go into building a competitive race car and assembling a championship racing team responsible for getting it across the finish line – preferably in first place. Regardless of the car's power or the racing team's talent, it will not get off the starting line or compete in the race without the fuel to start the engine and keep it running. Similarly, a trust department with a well written Business Plan supported by a highly motivated and professional team of trust officers will not get off the starting line or compete in the race for wealth management services without a Practice Management program that will ignite the staff's energy and keep it sharply focused on the winning track to success.

Practice Management Basics

Practice Management has always been an important business concept for professional service organizations such as law firms and accounting firms. These professionals understand the vital role that Practice Management plays in the efficient day-to-day operation of their businesses, and how important it is to the overall success of their firms. Bank trust departments could benefit greatly by following their examples.

There is no one-size-fits-all Practice Management program. Although there is some commonality in the manner in which professional service organizations address Practice Management issues, there are also some nuances based on practice specialties and firm culture. Private Trust Group of America is working on a guide to help bank trust executives design a program that will take into account some of the common practices they share with other professional service providers, but with proper consideration for some of the differences that make bank trust executives stand apart from their colleagues in the legal, accounting and investment professions. In the meantime, here are a few ideas to get you started.

Establish Benchmarks, Set Expectations and Demand Accountability – One of the primary functions of an effective Practice Management program is to establish a set of standards and benchmarks that hold people accountable and can be directly linked to a person's contribution to the organization's success – which is usually measured in terms of compensation. It is important that every aspect of the Practice Management program is monitored by someone with the authority to establish benchmarks, set expectations and demand accountability. This is generally handled through a "firm committee" or "practice management team" that has the ability and the authority to control behavior by influencing compensation, if necessary.

Pay Special Attention to Fees and Avoid Open-Ended Discounts – Bank trust departments are notoriously blind to opportunities in which they can provide premium services for an additional fee. Set a fair fee schedule that can be justified by the services offered and do not deviate from it without committee approval. Listing fiduciary standards and explaining regulatory oversight will help justify service levels and fees.

Establish a written statement outlining the services to be included in the fee arrangement and have a schedule of additional fees for extra services or "pass thru" charges that are incurred on behalf of the client. It is equally important to limit discounts to a specific period or event, after which normal fees apply, and to turn business away if a client is shopping for the best rates around. Customers look for short-term bargains – clients look for long-term relationships.

Case/Client Management – Attorneys and accountants refer to this as "case management," but the same principles apply to bank trust departments. Trust officers must be constantly monitored to be sure they have adequate resources, are providing appropriate services to the bank's clients and are managing their time well enough to have positive results for the department. Clients should also be closely monitored to be sure they are being well-served, are satisfied with the services they are receiving and are representative of the department's definition of an ideal client for the department to service.

Define the Trust Department's Ideal Client – The trust department's service offerings, the experience of its staff and the general demographics of the bank's geographic footprint will help define the profile of its ideal client. If the ideal client has been properly defined, approximately 60% of the department's clients should fit the profile; 30% will fall below the ideal client's definition, and 10% will exceed those standards. If either side of the 60% band increases or decreases significantly, the business model has changed and the necessary adjustments should be made to keep it on course.

<u>Sales & Marketing</u> – Whether it's a result of their heavily regulated business environment or the inbred conservative nature of one generation of trust officers training the next, many bank trust officers are far too passive in asserting their claim to the "gatekeeper" role in their clients' affairs. To take command of what has historically been a natural role for bank trust officers, they must move aggressively to reclaim that position. One way to do that is to turn what is often considered a regulatory burden into a marketing advantage by explaining to their clients that bank trustees are actually held to a higher standard than some of their less regulated competitors.

<u>Accepting New Business</u> – Temptations to accept new business simply to keep it out of the hands of a competitor should rarely, if ever, be condoned. All new business should be approved by the appropriate oversight committee and the profitability (or lack thereof) of every single relationship should be tied to the compensation or incentive plan of the individual(s) responsible for introducing the new business and/or managing the relationship.

A classic mistake many trust officers make is to accept any account, regardless of size. Small accounts with "potential" can divert important resources away from larger, more profitable clients and, if left unchecked, will represent a disproportionate segment of the business model. Periodic reviews will uncover those accounts that have not lived up to their potential so they can be moved to the retail side of the bank. Some very large accounts that will obviously tax the department's service limits and resources should also be avoided. The damage caused by not delivering on a large client's expectations can be significantly greater than any short-term economic benefit derived from accepting the business in the first place.

Leveraging Support Staff – One of the greatest strengths of professional service providers such as attorneys and accountants is their ability to limit the use of non-essential staff. Instead, they leverage paralegals and interns who assist with providing professional services that can be billed at a premium, thus turning an overhead item into a revenue opportunity. They try to invest their financial resources and human capital on the front end of their businesses and avoid adding non-essential, non-revenue producing staff whenever possible.

Risk Management – No business is immune from risks, which take several forms and should be aggressively managed. The key is to mitigate risks without being so paranoid about failing to prevent them that your business becomes paralyzed. The conversation I reiterated earlier about the bank trust department executive who could only think of reasons why he could not work with investment advisors is a perfect case in point.

I am always puzzled by how bank trust officers concentrate so fiercely on making sure that they don't get reprimanded by a bank examiner for some minor transgression that they lose sight of the two-ton elephant standing in the room. Many spend their time making sure that the right boxes are checked on all the government mandated policies and procedures forms, but few pay much attention to properly documenting why decisions are made or recording important client communications. The former might get a mention in an audit report that will get senior management all worked up, but failing to perform the latter could end up in a law suit that ends a career or causes enormous financial harm to the institution.

In my experience, I have only encountered a few who subscribe to the motto of one of my trust officer friends who frequently reminds me, "If an examiner doesn't find something to complain about, I don't think I am doing a very good job for the bank." To be sure, this trust officer takes his oversight responsibilities very seriously – but he does not allow them to define his job. Not coincidentally, the few that I have encountered who follow that mantra also manage some of the most profitable trust departments I have seen. The key is to reach the right balance between vigilance and paranoia.

Economics – Bankers usually take a much more classic business approach to running their operations than attorneys or accountants. Bank trust department budgets are generally "flat lined" to the previous year's budget or are created on the basis of using the previous year's revenue and expenses as a baseline for applying a factor of "1" plus the current inflation rate – or some other arbitrary number. Little attention is paid to the broader and much more important concepts of overall Practice Management that actually drive profits.

Line item budgeting, to the exclusion of the broader concepts and principles of Practice Management, often leads to a stagnant business model that creates diminished expectations and low morale within the department. Under such conditions, the enthusiasm and excitement of working together to create a dynamic business model that motivates people to think beyond their own narrow areas of responsibility and rewards them for achievement gets lost – and the business never reaches its potential.

Of course, budgeting is an important part of any Practice Management program – but it should not be the central focus of the program. In a professional environment, the belief is that aggressively managing all areas of the firm's practice will automatically result in positive bottom line revenue. A good Practice Management program will direct the trust department's focus where it should be – on establishing benchmarks, setting expectations and demanding accountability, all of which will ultimately result in high-quality client relationships; a renewed sense of professional commitment to each client (which will usually be reciprocated in the form of loyalty to the trust officer and his/her bank); and higher profit margins.

Summary

Offering private wealth management and personal trust services has become a contact sport with very aggressive competitors trying to fill the role of gatekeeper for clients who are looking for a central figure to coordinate all of their business, personal and financial needs. Bank trust officers should sharpen their elbows and fight for their rightful place at the table. It all starts with convincing the bank's Executive Committee and/or Board of Directors that the trust department is committed to implementing a Practice Management program that will enhance its standing within the bank; will create a more professional public image, and will result in consistently positive results to the bottom line. Designing and implementing a Practice Management program is the easy part – making the commitment is the challenge, because the program will require an entirely new approach to the way the trust department is managed.

This article was submitted by John Larrabee, managing partner of a family trust practice and an advisor to Private Trust Group of America. John will be assisting PTG in writing a Practice Management Manual for bank trust departments. Please contact him if you have thoughts or ideas that you believe should be included. He can be reached at his Charlotte, North Carolina office: 704-987-0875, or via email at: johnl@northstarfinancialgrp.com.

About Private Trust Group of America

Private Trust Group of America is an employee-owned company specializing in providing administrative and operational support to trust departments and wealth management offices nation wide. With an executive staff that has over 100 years of combined trust and related technology experience, and a professional staff whose average experience exceeds 22 years, Private Trust Group of America offers an unusually high degree of frontline sophistication to its client base.

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