

## **Risk Mitigation and Best Practices Policy**

### **Insurance (Errors & Omissions and Directors & Officers)**

The Town of Lunenburg presently delegates the management of specific investments of trust accounts which fall under the purview and oversight of the Board of Trust Fund Commissioners, to a Private Trust Company (PTC) which as of the writing of this policy is Bartholomew and Company. The PTC holds a fiduciary role and insulates the town from risk to some extent (specifics are contained in the contract agreement between the Town of Lunenburg and Bartholomew and Company). This contract document is held in the office of the Treasurer. Unless otherwise specified in the individual trust documents, by declaration of that specific trust, the contract with Bartholomew and Company is the controlling document outlining the insurance based on the risk of investments. Any and all people including directors and officers of the PTC are insured and bonded. This should be available for periodic review annually by the Board of Trust Fund Commissioners.

### **Trust Administrative Memorandum**

A trust administrative memo (TAC memo) should be available for inspection by the Board of Trust Fund Commissioners, that has been prepared by either the trustee of the individual trust, trust counsel, or the operating team of a PTC to ensure that all parameters are covered in governance including but not limited to the nature of trust assets, the issues in the trust, and the administrative activities necessary under both state and federal law and within the trust document. Verifying that all aspects of management and operation are clearly written out for review by the Board of Trust Fund Commissioners.

The Board of Trust Fund Commissioners should review this memorandum annually or whenever changed within the year, which should spell out the following 3 parts clearly, in an understandable language.

The TAC Memo should contain the following which should be reviewed by the Board of Trust Fund Commissioners:

- A table summarizing salient information
- A descriptive section summarizing the trust provisions as well as setting out observations by the administrative team (supra)
- A table listing outstanding routine tasks that need to be addressed as part of the trust “on-boarding” process.
- The memorandum should also address any gaps such as the lack of strong retention language in the trust document or lack of authorization to delegate investment authority, or limitation on investments – often found in older documents.

- If the role of the PTC reaches unacceptable levels of risk in the management, sufficient to warrant a refusal of the appointment as the right person to manage the fund, this should be raised before the commission to understand what issues are involved in refusing to act (often there is no clear succession).

In the case of a PTC, the commission needs to be able to review the TAC memorandum and ask questions, relying on the administrative team of the PTC to prepare these memoranda and raise issues of interest or concern to the commission.

The commission should hold Quarterly Communications with Beneficiaries along with the PTC as a best practice, and that the commission have regular and frequent communication with the trust beneficiaries. In the case of a PTC, quarterly meetings or communications with beneficiaries and Trust Commissioners and an annual in-person review are integral to the function of the commission. The quarterly review process ensures constant communication between the commission and the beneficiaries and enables the commissioners with the PTC to minimize confusion or missed expectations with respect to trust management, diversification of investments and operation. Quarterly beneficiary communications should consist of a trust administration and investment letter, and/or a PowerPoint summary. Additionally, a call may be conducted by the commission with the administrative team of the PTC. Annual reviews are typically more in-depth, should be in person, and should include a broader group (attorney, CPA, investment committee of PTC the finance director and treasurer, town manager and selectboard and finance committee) and include any outside investment managers, if any, and should include an invite of the benefactors of the trust.

### **Commission Best Practices**

- Do understand the implications of the Prudent Investor Act and MGLA 203C et seq. and the Principal and Income Act MGLA 203d et. seq. on trust management.
- Do understand your rights and responsibilities as a commission MGLA Ch. 41 Sec 45 and Lunenburg Charter Article 3 section 3-8
- Do create a philosophy for the PTC to follow in the creation and operation of the enterprise.
- Don't let donor knowledge, personal views, or prejudices obscure legal obligations as a commission.
- Do focus on collaboration and consensus. Ensuring that all parties act in sync and that beneficiaries receive sufficient financial planning and education about the importance of trusts for their long-term financial well-being.
- Do have clear, repeatable metrics for making investment decisions, implementing trust structure and distribution decisions.

- Do understand trust documents and distribution provisions.
- Do recognize and use the flexibility offered to commissions under MGLA, charter and the Principal and Income Act (as applicable) to ensure that the best result for the beneficiary is obtained while balancing the fiduciary obligations of the trust.

### **Bottom Line**

The Board of Trust Fund Commissioners should be dependable to oversee the funds. These investments are very important decisions for ensuring wealth is managed and distributed according to the declaration of trust and law. This will provide for the best rate of return for the investment pool in the long term. It is a core element of any long-term wealth management strategy.

Commissioners must have a full understanding of the issues, responsibilities, and time involved in the process and have the resources and objectivity required to be effective. All aspects involve significant legal considerations and many tradeoffs in terms of control or tax savings. It is imperative to work with the qualified PTC and their advisors to obtain expert advice in crafting a long-term strategy and designing the investment pool to shape the needs which the trusts benefit.

### **Risk Mitigation Through Regular Reviews and Delineated Investment Approach**

A fundamental obligation of commissioners is to ensure regular and frequent communication with trust beneficiaries, and the PTC including quarterly reviews that address the following areas or topics:

- **Overview or Summary of Trust Operations:** This summary will include income earned, distributions and investment performance. Dependent on custodial platforms, the generation of these reports should be mostly routine with some manual work needed to polish and collate information.
- **Investment Review:** In addition to the performance reporting of trust assets, the commissioners with the guidance of the Private Trust Company (PTC) will provide a broad market overview as well as a discussion of the tactical and strategic asset allocation of the trust, review of the investment policy guidelines and distribution provisions, with a summary of what this means to the beneficiary and the trust long term. Outside managers (finance director, treasurer) may join for all or part of this review, depending on logistics (in the case of multiple managers, it is best to have one member of the administrative team handle this, perhaps in conjunction with the Investment Committee of the PTC with the Commission). The investment review should also be consistent with the Investment Committee and PTC's investment approach and philosophy around trust management and approved by the Board of Trust Fund Commissioners.

- **Principal and Income Review:** There should be a review at each quarterly meeting, with an in-depth review annually of the principal and income accounts of the trust, including what this means for beneficiary cash flows and taxes.
- **Outstanding Issues or Questions:** This may reflect longer-term trust projects or objectives plus status updates on each area. For example, a decision to continue distributions to allow a beneficiary to raise income in their individual account to provide for a special project which might have a target goal of wealth to be moved over and progress reports on this objective.
- **Next Steps and Outlook:** Each review will conclude with a summary of changes to objectives and the outlook for future trust investments or distributions.
- **Manage Taxation of Trusts:** The commission with the PTC needs to review, at least annually, the state and federal tax returns of the trust in conjunction with the distributions and investment objectives of the trust. PTC shall provide tailored support in the management of tax liability and ensuring a tax-aware approach is applied to all trust management and investments

### **Investment Philosophy and Investment Policy Statements**

Every trust should have a stated approach to investment management, recognizing a specified trust may have a personal bias and might be at odds with the trust's investment needs. The Prudent Investor Act is predicated on a belief that there is no ability to efficiently capture market alpha, or outperformance of a benchmark, through active management. It favors an index-based approach to trust management where low fees and strong adherence to a portfolio's benchmarks ensure the trust will keep pace with its asset allocation. This will require the beneficiary of the expendable trusts to coordinate a detailed needs plan of at least a minimum of 5 years for the best practices approach with a minimum pool investment number to be held in the account, which they will not drop below that dollar amount so as not to interfere with the overall rate of return of the pool. Under this belief, the focus is on strategic asset allocation with tactical tilts in the portfolio balance to reflect market conditions. The strategy is executed through exchange-traded funds (ETFs), option overlays and capital protected strategies. The Private Trust Companies (PTCs) by active management will have to explain how this approach benefits the portfolio and enhances the trust, such as through a diversified investment allocation. Moreover, the commission is responsible for ongoing review and oversight of the investment manager(s) and needs to articulate the timeframe for achieving such performance. The commission must also be willing to request the dismissal and or reappointment of a manager if necessary. Furthermore, the commission needs to

recognize the long-term nature of the trusts they will be overseeing. Strategic asset allocations allow for long-term focus of portfolios. However, with the dislocations in the market post the Great Financial Crisis of 2008, we must reflect on the “modern portfolio theory” and whether this is sensible in today’s ever-changing market really makes sense. The commissioners will need to understand the differences between an efficient investor mindset and a behavioral finance approach. They also need to recognize that sector or other “bets” may not be appropriate for a trust portfolio. A commissioner must employ a standard of care: The Prudent Investor Act requires a standard of conduct, not outcome or performance. A commissioner’s performance is judged on whether they exercised reasonable care, skill, and caution in the overall investment process—not on the appropriateness or riskiness of individual holdings and income yield.

### **Investment Policy Statements**

Once the investment approach is identified and articulated, each trust must have a formal written Investment Policy Statement (IPS). The IPS sets forth the investment philosophy and typically addresses several topics, including:

- The time horizon of the trust and its impact on investment selections
- Trust distribution or income requirements and the attendant impact on investments
- Risk tolerance of the trust and trust beneficiaries
- Incorporating large concentrated positions into the asset allocation
- Diversification or hedging strategy to mitigate the risk
- Performance benchmarks for the trust and each asset class
- Restrictions on asset allocation to force rebalancing of trust portfolios
- Timing or manner of portfolio rebalancing

Investment Policy Statements may also reflect trust-specific techniques. For example, if the grantor of a grantor trust has retained the power of substitution, the IPS might outline the impact on trust management. The Prudent Investor Act imposes a duty on all parties to pursue an overall investment strategy with reasonable risk and return objectives to meet present and future distribution requirements. In constructing a portfolio investment strategy, commissioners must consider the risk tolerance of the trust and the beneficiary’s relevant circumstances. Also, commissioners are required to diversify assets unless they reasonably determine, with the assistance of the PTC, it is in the best interest of all the beneficiaries not to diversify.

objectives and adhering to the Prudent Investor Act of that trust ESG will not be a required factor to include in investment. The commission will consider all investment opportunities as guided with the advice of the PTC.

### **Explicit Policies and Procedures to Mitigate Risk**

The following are highlights of how a distribution policy will be applied:

- A recitation of distribution provisions in the trust documents
- The commissions interpretation of these documents through the use of a trust summary or gap analysis
- Any philosophical approach or belief that will be used when reviewing special distribution requests
- The timing and manner of distributions
- Clear expectations of the beneficiary regarding the receipt of distributions

Distribution policies of this design are important for the management of trust assets. Which provide commissioners and investment managers with guidelines for when cash is needed from the portfolio and the amount of liquidity to be kept on hand.

### **Fiduciary Policies and Procedures**

Trusts benefit from having strong, detailed fiduciary policies and procedures. The Private Trust Company (PTC) board will approve the operational policies and procedures that dictate how the PTC will manage all aspects of the trust except for which duties of disbursements are managed by approval of the Board of Trust Fund Commissioners. The PTC will provide clear, repeatable processes, and ensure that its administrative processes are consistently applied, and this commission will understand what must occur before any action can be taken. For example, special distributions of trust assets might require the beneficiary to submit a memorandum, which will be reviewed by X members of the commission within Y time horizon. By providing this type of clarity, the PTC can manage commission expectations regarding how quickly they can access cash in a portfolio, increasing the emphasis on their personal liquidity to provide emergency funds or just expendable as needed for use.

### **Guidelines for Recordkeeping**

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- **Tax Compliance.** The commission needs to ensure that all trusts comply with requisite state and federal income tax reporting.etc.
- **Custody and Reporting.** The commission and PTC will work with a selected custodian to facilitate the creation and maintenance of reporting mechanisms for all trusts. Regardless of whether a PTC chooses to staff its own educated team of employees, the custodial and reporting functions are usually licensed by and through the town treasurer. Most important is the custodian's ability to perform principal and income accounting for the trusts, track tax and other considerations, provide oversight of investment activity (collection of dividends and interest), and deliver accurate performance reports, ideally independent of the PTC or subcontract it out to the managers of the PTC
- **Beneficiary Meetings and Communications.** The commission will need to hold quarterly and annual beneficiary meetings. Maintaining copies of all meeting materials and beneficiary communications and others should be part of the recordkeeping requirement.
- **Audit.** The PTC has its own audit committee who will oversee the audit process (if an audit occurs), sign off on the audit, and submit it to the commission for review. The PTC must hire outside parties to objectively audit both the PTC's corporate work and trust administration.

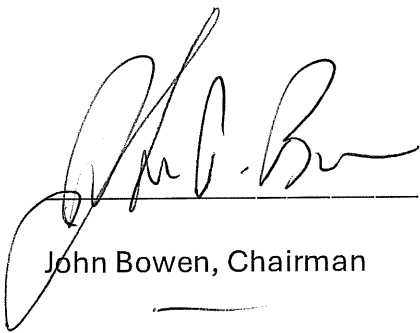
### **Public Education**

While the quarterly meetings provide a great platform for communication, the commission needs to err on the side of overcommunicating. They should evaluate what each beneficiary needs to understand, the topics discussed during the meetings and then address these educational gaps through tailored programs, in writing, outlining their fund, delivered either individually or in small groups. For every trust, the commission will build consensus and collaboration with the beneficiaries to ensure they understand decisions and the tradeoffs, even if they don't like them. The commission will establish a strong paper trail in terms of communication, education and outreach to show that the beneficiaries were aware of the actions and understood the decisions.


### **Severability**

If any provision or provisions of this policy is or are declared unconstitutional or inoperative by a final judgment, order or decree of the supreme court of the United States or of the supreme judicial court of the commonwealth, or by the superior court of the Commonwealth the remaining parts of said chapter shall not be affected thereby.

Signed on This 24<sup>th</sup> day of July 2025 by the elected members of the Lunenburg Massachusetts Board of Trust Fund Commissioners as was voted into enactment.



John Bowen, Chairman



Richard Howard, Vice Chairman