

Article submitted for 2008 Trust Consciousness Week:

MANAGING INVESTMENT RISKS THROUGH SPECIAL TRUST SERVICES

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So much has been said and written about the investment products and services available through the trust departments. Through the years, the concept of investing through a trust institution acting as fund manager has evolved, with the choices ranging from portfolio management done through investment management accounts, living trusts, pre-need trust funds, retirements funds , other personal and corporate trust funds, to common trust funds that have since been replaced by unit investment trust funds.

We turn our attention this time to direct fixed income investments and capital market instruments issued by institutions in the financial markets and see how the presence of a trust institution helps enhance public confidence in these investment products.

Developments of late in the trust business points to the expanding role that trust departments now play in the financial system, particularly aimed at strengthening these fixed income and equity investment products, in the process mitigating the risk of investing, a factor most especially important in times of uncertainty.

Let us examine several of these financial products needing the services of a corporate trustee in the category of special trusts.

Syndicated Loans, Bonds and Long-term Commercial Papers. Private bonds and long-term commercial papers (CPs) have been sold of late with credit-enhanced features. Rules governing these issues today require the appointment of a Collateral

Trustee to either take custody of collaterals in the case of secured issues, or otherwise serve as Facility Agent to monitor the issuers' covenants, duties and obligations under these loans, bonds or commercial papers. Bonds and commercial paper issuers likewise, are required by SEC rules to appoint a trust entity to perform roles as Receiving Agents or Sinking Fund Managers to handle the payment of interests and the redemption of principal obligations. All told, the rules provide the enhancement that makes the loan funder, bondholder or CP investor feel more comfortable with his investments while the obligation has not matured, or while the note or bondholder has not sold or traded his holdings in the secondary market.

Mutual Funds. Open-end investment companies organized under the Investment Company Act have increased in number over the last few years, making diversified investments within the reach of even the smallest of investors. These funds, therefore, contribute in no small measure to the financial system by reaching out to individuals of modest wealth. Again, while the more prominent player in a mutual fund is the fund manager or the sponsoring fund management company, a mutual fund cannot be offered without contracting the services of a trust entity acting as Custodian of the securities into which the fund is invested, and a Stock and Transfer Agent ensuring the issuance and cancellation of shares representing the participants' investment in the mutual fund.

Initial Public Offering (IPOs) of a Common Stock. Even while the economy grapples with risk and uncertainty, the development of a strong Philippine capital market rests heavily on the increase in the number of new companies whose shares are being made available for trading to the public through the Philippine Stock Exchange. But then again, while the more visible players involved in an IPO appear to be the investment

banks, underwriters and broker-members of the exchange, IPOs cannot be licensed without certain roles being performed by the trust entities. Thus, a company going into a public listing of its shares for the first time needs to appoint a Stock and Transfer Agent for the purpose of controlling the issuance and cancellation of shares as they are traded. Likewise, the presence of a trust department acting as Receiving and Custodian Bank for the proceeds of the IPO is required, to assure that such proceeds are disbursed for the specific purposes for which they have been represented to be spent in the work program laid out in the IPO's prospectus. A trust institution also needs to be appointed as Dividend Paying Agent for cash and stock dividends that may have to be prospectively paid by the issuer. Lastly, listing rules require the appointment of a trust entity acting as Escrow Agent to hold the shares of the principal owners of the company to prevent them from trading on their shares during the mandated "lock-up" period.

Unsecured Subordinated Debts or Tier 2 Capital of Banks. As early as 2003, banks have been allowed to borrow from the public through unsecured subordinated debts that qualify as Tier 2 capital in the determination of their Capital Adequacy Ratios (CAR). Again, as a form of investor protection, Bangko Sentral ng Pilipinas rules on the licensing of these securities requires the appointment of an independent Public Trustee to monitor the issuer banks' compliance to its covenants under said obligations, the appointment of a Registry to handle the issuance of the securities resulting from such subordinated debts, and the appointment of a Paying Agent, who again, should be a trust entity other than the issuer's own trust department, to act independently in handling these various functions related to such issuance.

As more financial and investment instruments develop in the local debt and equity market, opportunities for the offering of special trust services will grow as a way to enhance the features and mitigate the risk of investing in them.