



Real Estate Oversight Guidance

Discretionary investments in real estate include real property of all kinds, including farms, timberland, mines, residences, and commercial. A trustee is responsible for the administration of every type of real property held in discretionary trusts. The proper management of real estate demands an adequate level of knowledge and skill to ensure the property is an appropriate asset for purchase and/or retention and is, to the extent practical, productive of income. For non-discretionary accounts governed by documents that are silent with respect to the oversight of property under management, it is practical for the financial institution to enter into an agreement with the customer that details both the trustee's and the customer's role in managing the property. For example, the contract should identify the party responsible for acquiring and maintaining appropriate insurance coverage for the property, paying taxes, performing inspections and valuations, collecting rents, etc. Regardless of the account type (discretionary vs. non-discretionary), a valuation process should be in place to ensure accurate valuations for reporting purposes and fee assessments, particularly if the management fee is calculated as a percentage of the real property value.

Title Insurance

When acquiring real estate, management should determine the condition of the title to the property as soon as reasonably possible. The best time to remedy any title defects is during the acquisition process. If a defect in title exists at the time of a proposed sale, the delay or expense necessary to remedy it might defeat the transaction. There are two basic methods to ensure that title to property is satisfactory:

1. The trustee may have the title abstracted by an attorney, who issues a certificate that the title is good and indefeasible, except for any defects they might specify.
2. The trustee may have the title guaranteed by title insurance.

Appraisals and Annual Inspections

The trustee must have a program for the appraisal and inspection of all real estate held in discretionary accounts. Per industry best practices, the appraisal program should require appraisals at least every three years for real property held in personal trust accounts. In addition, the trustee must perform periodic inspections of real estate held in discretionary accounts. A routine annual inspection provides the trustee with current knowledge of the condition of the real property so that informed investment decisions can be made regarding their retention and/or disposition. The inspection should be thorough enough to assure that the fiduciary is fully knowledgeable about the present condition and status of the property.

The trustee should exercise discretion in appraising and inspecting some property. Fractional interests in real estate where the trustee has no effective control and residential real estate or other properties occupied by beneficiaries may not warrant periodic appraisals and inspections.

Considering guidelines pertaining to real estate appraisals stated above, trust examiners use discretion depending on a host of circumstances, including the size and type of the real estate in question. Regardless, it is consistent among examiners that appraisals need to be updated every four or five years, at a minimum. In markets where real estate values are fluctuating rapidly and/or substantially, more frequent appraisal updates

are required. An important consideration is that a proper value is established for insurance coverage purposes.

It is in the best interest of the trustee to acquire grantor/beneficiary approval before waiving appraisals and inspections. Please note that the effectiveness of grantor/beneficiary waivers of inspections and appraisals can be disputed, and management should be aware of the constant responsibility to properly administer real estate. As a matter of policy, management should not rely solely on grantor/beneficiary waivers of inspections and/or appraisals, particularly in instances where there are abnormal fluctuations in property value or the condition of the property requires attention.