

Select Entity Type	Enter name and city	Date of Exam	
Charter #		Prepared By	

5 - COMPLIANCE (Risk Focused)

ASSIGNMENT OVERVIEW

These procedures evaluate the adequacy and effectiveness of trust account administration, including a review of agency, custodial, corporate, estate, employee benefit, individual retirement, and ESOP accounts. The examination should determine the extent of compliance with the governing instrument, applicable law, regulations, and industry standards. The assessment of compliance and account administration encompasses a review of the capability and expertise of management, the effectiveness of policies, procedures, and controls that ensure the administration of accounts is prudently performed as to protect the fiduciary from liability.

A conflict of interest is inherent in a transaction where the fiduciary exercises any discretion with mutually opposing interests involved. Transactions involving conflicts may breach a fiduciary's basic duty of undivided loyalty to the beneficiary and can result in significant contingent liabilities. Some conflicts cannot be avoided in the normal course of business, and the examiner must be aware of these circumstances and exercise proper discretion. Certain controls should be present to avoid or minimize conflicts and ensure proper disclosure and review. When there is evidence that a trustee has engaged in self-dealing, proper remedial measures should be taken and an assessment of potential civil liability made in the examination.

INSTRUCTIONS

Examiners must follow the requirements in the Examiner Bulletin addressing Guidelines for Procedures and Work Paper Documentation for Trust Examinations.

All examiners performing these procedures must be listed above in the "Prepared By" section. Comments and findings for each step should be made in the comment box below each question. Reference to work paper documentation should also be included here. Documentation is to be sufficient to allow an audit trail of the examiner's thought process and all significant findings. Items to Consider within the core analysis are not required to be commented on unless there are significant issues. The intent is to assist the examiner in expanding their thought process and analysis of that area.

Information on the Summary of Findings page must tie back to the findings noted within the procedure. The SEIC/EIC will determine which information in the Summary of Findings will be included in the Report of Examination.

The EIC/AEIC or designee should review this procedure when complete. Acknowledgement that this procedure has been reviewed by the EIC/AEIC or designee will be indicated on the SCOPE FORM.

EXAMINERS ARE RESPONSIBLE FOR EXERCISING SOUND JUDGMENT AND UTILIZING REASONABLE INVESTIGATIVE AND ANALYTICAL SKILLS TO ARRIVE AT AN ACCURATE ASSESSMENT OF THE RISK PROFILE OF THIS SEGMENT OF THE INSTITUTION'S OPERATIONS. PERFORMING ALTERNATE PROCEDURES NOT LISTED WITH THESE GUIDELINES MAY BE NECESSARY TO COMPLETE THIS RISK ANALYSIS.

CORE ANALYSIS PHASE

#5 - COMPLIANCE

1. Prior Criticism

1. Determine whether deficiencies noted in the last examination and most recent internal/external audit have been addressed and/or corrected by management. Detail how deficiencies were corrected. *Include a copy of audit exceptions and/or prior examination criticisms and management response in work papers or indicate the page number in the prior report of examination where the deficiencies are noted, or summarize exceptions/criticisms below, if applicable.*

Comment:

2. Self-Dealing and Conflicts of Interest

2a. Evaluate how the institution manages risk associated with conflicts of interest and use of potential sources of insider information. Consider the following management strategies:

- Adequate policies with consideration given to state and federal laws
- Compliance with requirements set forth in federal and applicable state law.
- Appropriate client disclosures
- Proper reporting to the Board
- Obtaining legal opinions and court approval when necessary

Comment:

2b. Determine whether cash management and own-bank deposit procedures are appropriate **and** in compliance with Texas Property Code (TPC) §113.057. *Note: Uninvested cash refers to cash in an account that is awaiting permanent investment or distribution. Cash management refers to the effective and efficient management of cash held in fiduciary accounts as well as operating bank accounts.*

Address the following:

- Is there an automated cash management program which automatically sweeps uninvested and available cash balances into one or more short-term investment vehicles?
- Is there a formal system for monitoring and reviewing uninvested funds?
- Are own bank deposits being held? If so, determine the suitability and compliance with TPC §113.057.
- Are securities pledged appropriately for own-bank deposits over FDIC insurance limit?

Compliance with TPC §113.057 Deposits by Corporate Trustee With Itself

Select Response

Comment:

2c. If there are insider transactions, determine compliance with Texas Property Code §[113.052](#) and §[113.053](#) regarding the lending of trust funds and the purchase or sale of trust property by the trustee, to or from the trustee or an affiliate; a director, officer, or employee of trustee or affiliated institution; a relative of the trustee; or the trustee’s employer, partner, or other business associate. Utilize asset reports and the Officer’s Questionnaire to identify any of these types of transactions.

Comment on the following, as applicable:

- Each transaction was approved by the Board and by the beneficiary;
- The file contains adequate documentation of the asset’s market value and the underlying circumstances;
- Legal opinions or court guidance were obtained for transactions that appear particularly sensitive; and
- The institution has satisfactory written policies and procedures relating to insider transactions, and compliance with policy should be noted.

Note: Absence of full disclosure and proper documentation should result in examiner criticism and remedial action.

Transactions with Director, Officer, Employee	Select Response
If Yes, Compliance with TPC § 113.052 Loan of Trust Funds to Trustee	Select Response
Compliance with TPC § 113.053 Purchase or Sale of Trust Property by Trustee	Select Response

Comment:

2d. Identify any transactions in which assets held in a fiduciary capacity in one account have been sold to itself as fiduciary in another account.

Assess whether the transactions are fair to both accounts, and whether such transactions are permitted by the governing document and applicable TPC §[113.054](#) Sales from One Trust to Another.

Applicable transactions? <i>If Yes, Indicate compliance and provide comments.</i>	Select Response
If Yes, Compliance with TPC § 113.054 Sales From One Trust to Another	Select Response

Comment:

2e. Review a listing by account of current holdings of stock in the institution, the parent company, or any affiliates. Assess whether holdings are in compliance with Texas Property Code §[113.055](#) regarding the Purchase of Trustees Securities and TPC §[117](#), the Uniform Prudent Investors Act. *(Such securities may be retained only upon written instructions from the beneficiary and must meet the requirements of the*

Uniform Prudent Investors Act.)

Consider the following:

- Does the institution have policies and procedures relating to the purchase, retention and voting of its own securities?
- Are the voting rights of own-bank shares passed on to beneficiaries where possible?
- Are there methods to ensure that, where necessary, the trustee votes own-bank shares solely in the best interest of the beneficiaries?

Compliance with TPC [§113.055](#) Purchase of Trustee's Securities

Select Response

Compliance with TPC [§117](#) Uniform Prudent Investors Act

Select Response

Comment:

2f. Trust Department Only: Determine whether personal securities transactions are reported quarterly as required by [12 CFR 344.9](#) for nonmember banks or [12 CFR 208.34\(g\)\(4\)](#) for member banks. Indicate compliance and comment.

Compliance with applicable regulation:

12 CFR 344.9 (nonmember) or 12 CFR 208.34(g)(4) (member)

Select Response

Comment:

2g. Assess whether the institution has appropriate disclosures in place in connection with securities trading regarding "soft dollar" arrangements and [12b-1 fees](#). Determine if disclosures have been provided to clients.

Comment:

2h. Determine the level of risk exposure to the trust company/trust department as a result of transactions between the institution and its related organizations, and the operations of relevant affiliates.

Consider the following:

- Written agreements
- Transactions that are not arm's length and in the best interest of the trust company
- Breach of fiduciary duties while dealing with affiliates
- Impropriety
- Lack of prudence
- Violation of laws and regulations between the entities

- Contraventions to trust policies in dealing with the affiliates, contingent liabilities with affiliates
- Knowledge of any potential/actual litigation claims with affiliates or between affiliates and trust entity

If there is a significant change or a problem with an affiliate relationship that transacts business with the trust entity, discuss with the EIC and summarize below.

Include a comment in the report of examination on complex organizational relationships and important risks presented by affiliates to the safety and soundness of the trust company. If there has been no change since the previous examination, a limited review and summary could be performed.

Affiliate Relationships?
If yes, provide a comment.

Select Response

Comment:

3. Account Administration

3a. Determine the adequacy of new account acceptance and account termination procedures. Describe weaknesses identified and summarize findings in the comment section below.

Consider the following for account acceptance practices:

- Administrative Committee(s) approval process for all administered accounts (ie the committee's assessment of the type and character of the potential account, type of assets to be transferred, area of expertise, governing document, potential conflicts, and overall complexity of the account).
- Adequacy of Account Acceptance Policy and pre-acceptance review process.
- Checklist utilized to ensure all pertinent documentation is obtained.

Consider the following for account termination practices:

- Proper receipts or releases obtained prior to any transfer or distribution of assets.
- Review of closed accounts duly recorded in the minutes of the appropriate committee as provided in the Statement of Principles of Trust Management.
- Unless the governing document contains exculpatory language, documents are obtained as required for the final accounting, court discharge and/or direction to terminate.
- Appropriate termination policies.
- Checklist is used to ensure all actions have been taken prior to account closing.

Comment:

3b. Based on the examiner account review, determine whether account documentation adequately supports the institution’s administration of accounts. Consider the following factors for effective documentation practices:

- Synoptic records summarize provisions of the governing document.
- Distribution practices are in accordance with the governing document, established policy guidelines, and supported by written direction.
- Adequate documentation on successor and co-trustee appointments.
- Written authorization is obtained on all co-trustee related transactions
- Tickler system is adequate for administrative and operational duties.
- Account files are well maintained and provide sufficient documentation of the institution’s execution of duties.
- Documentation deficiencies appropriately identified, monitored, reported, and corrected in a timely manner.

Comment:

3e. Confirm that the institution acts impartially in investing, managing, and distributing trust property to all beneficiaries or class of beneficiaries.

Refer to TPC [§113.051](#) General Duties, TPC [§116](#) Uniform Principle and Income Act, and TPC [§117](#) Uniform Prudent Investor Act.

Comment:

3f. Discuss documentation exceptions and determine the adequacy of policies for the following:

- [Estates](#)
- [IRA’s](#)
- [Employee Benefit Accounts](#)
- [Corporate Trust or Agency Accounts](#)

Determine if accounts are administered in accordance with governing instruments, internal policy and procedures, applicable laws, and industry standards. Refer to [Appendix](#) for guidance.

Comment

3g. Determine the adequacy of the institution’s administrative review process and procedures.

Consider the following:

- Are reviews performed in compliance with the Statement of Principles and conducted at least once each calendar year?

- Are the reviews performed by an appropriate committee or administrative officer?
- Do minute books or other records document accounts reviewed?
- Are administrative reviews performed in compliance with the established policies and procedures?
- Are documentation exceptions reported and monitored accordingly.

Comment:

4. Policies and Procedures

4. Determine whether the institution has adequately developed and implemented a written program to comply with the Securities and Exchange Commission (SEC) and Federal Reserve Bank (FRB) Regulation R and Gramm-Leach Bliley Act of 1999 (GBLA). Refer to the **Reference Material** for guidance.

Note: Although a final record-keeping rule for Regulation R has yet to be issued by the SEC and FRB, institutions will be evaluated, until such time, on industry standards and best practices supported by examination guidance issued by the FRB and Federal Deposit Insurance Corporation.

Comment:

5. Final Analysis

5. Complete the **Summary of Findings**. Refer to **SM 1002** for guidance on ratings.

SUMMARY OF FINDINGS

#5 - COMPLIANCE

Describe all strengths evident from the evaluation.

Describe all weaknesses evident from evaluation, including violations of law/regulation/rules; noncompliance with Departmental policies/guidelines; internal policy deficiencies/noncompliance; internal control weaknesses; MIS problems; and deficiencies in management supervision.

Determine why weaknesses exist and comment on management's response and plan of action. Identify bank personnel making the response.

SUMMARY RISK RATING ASSIGNED: Select Rating

Risk Rating Definitions:

1-Strong; 2-Satisfactory; 3-Less than satisfactory; 4-Deficient; 5-Critically deficient; NR-Not Rated

Provide copy of this page to EIC/AEIC. Receipt and review of this form by the EIC/AEIC will be evidenced by his/her initials in the appropriate column for this procedure on the SCOPE FORM.

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APPENDIX

Estate and Tax Administration

Consider the following:

- Are estates administered in accordance with the Texas Estate Code?
- Are proper amounts of estimated quarterly taxes paid to the IRS as provided in Section 6654?
- Are tax returns filed in a timely manner? See [Reference Material](#) for a list of types of tax returns.
- Are fair market valuations of estate assets properly obtained?
- Does the institution have procedures to comply with the withholding and related disclosure provisions, as applicable, of the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA)?
- In *estates held open for three years or longer*, determine whether holding the estate open is appropriate.
 - Have as many assets been distributed as possible?
 - Does the situation comply with the institution’s written policies?

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IRAs

Consider the following:

- Has the institution purchased any “collectibles” for any account as defined in IRC Section 408(m)? If so, verify these have been recognized as potential “premature distributions” for tax purposes?
- Are there any hard to value or unique assets, such as limited partnerships, joint ventures, closely-held companies, mortgages, notes, or real estate held in IRA’s? If so, do the files contain appropriate documentation of client direction, parties-in-interest, partnership agreements, or other evidence of ownership, and supporting documentation of valuations of such assets?
- Are there any prohibited transactions noted? If so, the IRA could be subject to Loss of Exempt Status under Section 408(e)(2).
- Does the institution pay premiums, “finders’ fees,” or related incentives to third parties in connection with establishing IRA accounts? If so, verify compliance with 58 Federal Register 35-67, Department of Labor Prohibited Transaction Exemption 93-1.

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Employee Benefit Accounts.

Consider the following:

- Do the files contain the following:
 - Copy of plan and trust agreement, including any amendment (ERISA Sections 402(a) and (b))?
 - Certified copy of the Board Resolution adopting the plan?
 - Determination letter from the IRS?
 - Specimen signatures of persons authorized to give instructions?
 - For *Employee Stock Ownership Plans*, do files contain evidence that the plan has been approved by the IRS?
- Does the institution ensure that duties are executed in accordance with the plan instrument, for the exclusive benefit of plan participants and beneficiaries with the care, skill, diligence, and in accordance with the “prudence” standard of the ERISA, Section 404(a)(1)(B)?
- Does the institution comply with Section 405 of ERISA regarding breach of fiduciary duties by a co-fiduciary?
- Does the institution have procedures to ensure that employee benefit plans comply with the spousal consent requirements of IRC Section 417?
- Does the institution receive any type of remuneration or rebate for investing cash balances? If so, verify that the fee arrangement complies with Section 408 exemptions under ERISA and the sweep fee guidelines established in Department of Labor Opinion Letter 10.422 for employee benefit accounts.
- Does the institution provide the information required by the plan administrator to publish an annual report within 120 days of the plan’s fiscal year-end as required of ERISA 4065, including:
 - Information pertaining to party-in-interest transactions?
 - Reportable transactions exceeding 3% of the current value of assets?
 - Past-due leases and loans as required by ERISA Section 103(a)(2)(B)?
- Does the policy prohibit dealings with parties-in-interest as defined in ERISA 3(14)?
- Do account holdings provide adequate diversification as required by ERISA Section 404(a)(1)(C)?
- Are disbursements and expenditures made in conformity with the fiduciary agreement and supported by written direction from the plan administrator?
- Is there any evidence of prohibited transactions? If so, refer to [Reference Material](#) for guidance.

- Does the institution have accounts that are subject to the directions of an outside investment manager as per ERISA Section 402(C)(3)? If so, refer to [Reference Material](#) for guidance.
- Are there any loans to participants? If so, refer to [Reference Material](#) for guidance.
- Do any plans hold “qualifying” employer securities (QES) or real estate? If so, refer to [Reference Material](#) for guidance.

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Corporate Trusts and Agency Accounts

Consider the following:

- Are there any corporate accounts subject to the Trust Indenture Act of 1939 (TIA)? If so, refer to [Reference Material](#) for guidance.
- Have the following documents been obtained and are they maintained in the file:
 - Original trust indenture and evidence of recording?
 - Original supplements (if any) i.e. instruments perfecting a lien on collateral, if any, trust mortgage, deed of trust, collateral trust, equipment trust, etc.?
 - Certified copy of certificate of incorporation and all amendments to date of issue?
 - Certified copy of by-laws and all amendments to date of issue?
 - Certified copy of resolution of directors authorizing issue and approving terms of indenture?
 - Specimen signatures of company’s officers authorized to sign and certification of their election?
 - Opinion of company’s counsel as to legality of the issue?
 - Opinion of the institution’s counsel approving acceptance of trust and authentication and delivery of bonds and listing of all necessary supporting documents?
 - Approval of regulatory authorities, where required?
 - Stockholders’ resolution authorizing the issue, if required by state law?
- Does the corporate trust ledger (accounting system) properly account for authorized issues, outstanding liability on the issue, bond inventories, and bonds destroyed?
- For older bonds (as most issues are now book-entry bonds):
 - Are procedures in place and responsibility assigned to provide proper safeguards for items being processed such as coupons, bonds in process, unissued bonds, and canceled bonds?
 - Are receipts secured and properly filed for bonds certified and delivered and bonds canceled and returned to obligors?

- Are the trustee’s procedures for paying called bonds, coupons, etc., adequate?
- Are the trustee’s procedures for processing redemptions of municipal securities in compliance with SEC standards?

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REFERENCE MATERIAL

ACCOUNT ADMINISTRATION - ESTATE AND TAX ADMINISTRATION

Types of Tax Returns

- Form 1041 (Federal Income Tax Return),
- Form 709 (Charitable Foundations),
- Form 6019 (Gift Tax Generation Skipping Transfer),
- Form 706 (Federal Estate Tax Return),
- Form 5500 (Annual Report of Employee Benefit Plan),
- Form 1099R (Distributions from Pension, Annuities Retirement, or Profit Sharing Plans, IRAs, Insurance Contracts, etc.),
- Form 5498 (IRA Contribution Information), and
- Form 4972 (Tax of Lump-Sum Distribution).

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ACCOUNT ADMINISTRATION - EMPLOYEE BENEFIT ACCOUNTS

Administrative Practices Relating Specifically to Employee Benefit Accounts.

[Prohibited Transactions](#)

[Outside Investment Managers](#)

[Participant Loans](#)

[Qualifying Employer Securities](#)

Prohibited Transactions

- The institution should have procedures to monitor transactions to determine whether they involve parties-in-interest, as defined in Section 3(14) of ERISA, directly or indirectly, in the:
 - Sale, exchange, or lease of property as per ERISA Section 406(a)(1)(A);
 - Lending of money or other extension of credit as per ERISA Section 406(a)(1)(B);
 - Furnishing of goods, services, or facilities as per ERISA Section 406(a)(1)(C);
 - Transfer to or use of assets by or for the benefit of a party-in-interest as per ERISA Section 406(a)(1)(D);
 - Dealing with plan assets for their own account or in their own interest as per ERISA Section 406(b)(1);
 - Acting in any capacity involving a plan on behalf of a party whose interests are adverse to those of the plan, its participants, or beneficiaries as per ERISA Section 406(b)(2); and
 - Receiving any considerations for their personal accounts from any party dealing with the plan in connection with a transaction involving plan assets as per ERISA Section 406(b)(3);

There should be no evidence or indication that the institution has engaged in a prohibited transaction with a “party-in-interest” as per Section 406(a)(1)(C) under ERISA.

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Outside Investment Managers

- For ***employee benefit plans*** where the company, as trustee, is subject to the directions of an outside investment manager pursuant to ERISA Section 402(c)(3), the institution must:
 - Obtain a statement that the plan administrator or other authorized fiduciary has appointed the specific investment manager as per ERISA Sections 403(a)(2) and 405(d)(1);
 - Obtain a letter from the investment advisor acknowledging its status as fiduciary and, if applicable, its registration as an investment advisor under the Investment Advisors Act of 1940 as per Section 3(38) of ERISA;
 - Obtain a statement naming authorized individuals associated with the investment advisor and providing specimen signatures;
 - Satisfy itself that directions are proper under Section 403(a)(1) of ERISA when it is trustee with Title I responsibilities.
- For individual account ***employee benefit plans***, the institution should monitor investments made pursuant to authorized independent direction of a participant so that such investments do not contradict the terms of the plan or the regulations of the Secretary of Labor (ERISA

Section 404(c)).

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Participant Loans

- Loans to participants and beneficiaries must meet the requirements of Section 408(b) of ERISA and IRC 72(p). These are as follows:
 - Loan balances should not exceed the lesser of \$50,000 (reduced by the excess of the highest outstanding balance owed by the participant during the prior 12 months), or the greater of 50% of a participant’s vested interest or \$10,000.
 - The loan must be repayable within 5 years except for loans used for the purchase of the participant’s principal residence.
 - Level amortization of the loan is required at least quarterly (IRC Section 72(p)).
 - Loans are available to all participants and beneficiaries on a reasonably equivalent basis.
 - Loans bear a reasonable rate of interest.
 - Loans are adequately secured (ERISA Section 408(b)(1)).
- Participant loans are made in accordance with specific provisions set forth in the plan as required by Section 408(b) of ERISA.
 - The document should authorize participant loans.
 - There should be a written loan program.
- The institution monitors the status of participant loans and takes action on past-due accounts as necessary.

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Qualifying Employer Securities

- Accounts hold employer securities or employer real property which comply with Section 407 of ERISA – limitation with respect to acquisition and holding of employer securities and employer real property by certain plans.
- Plans hold only “qualifying” employer securities (QES) and real estate (ERISA Section 407(a)).
- Employer security and real estate holdings meet the 10% limitation under ERISA Section 407(a).
- Dispositions of employer securities or real property between a plan and a party-in-interest conform to ERISA Sections 414(c) (3) or (5) or 408(e) for qualifying property.

- The governing instrument provides for their acquisition and holding as per ERISA Section 407(d)(3)(B).
- The investment is prudent and for the exclusive benefit of participants and beneficiaries as per ERISA Section 404(a)(1)(B).
- Holdings in stock that is not publicly traded and been independently appraised to establish a fair market value to meet the requirement of Internal Revenue Code (IRC) Section 401(a)(28)(C).

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ACCOUNT ADMINISTRATION - CORPORATE TRUST

Corporate Accounts Subject to Trust Indenture Act of 1939 (TIA)

For trusteeships which must comply with the Trust Indenture Act of 1939 (TIA), there should be evidence that the following has been obtained and considered before acceptance:

- The qualification of the indenture and of the institution as trustee under SEC Form T-1.
- The obligor and the institution are complying with Section 312 of the TIA by maintaining lists of bondholders in as current a form as possible.
- The trustee has transmitted to the holders of the indenture securities the reports required under Section 313 of the TIA.
- The obligor has filed copies of the annual reports and the trustee as required by Section 314 of the TIA.
- Other documents have been filed with the SEC as required by Section 314 of the TIA.
- The trustee, on an annual basis, performs an adequate check for conflicting interests as required by Section 310 of the TIA.
- All indenture provisions have been properly complied with before any collateral or mortgage interest is released and an issue is considered closed as required by Section 314(d) of the TIA.
- The trustee has been exempted by the SEC from any conflicts of interest which would otherwise prohibit it from serving.

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REGULATION R

Reference Materials Related FRB/SEC Regulation R

- [DOB Draft Policy Statement on Regulation R](#)

- The joint FRB/SEC final [Regulation R](#) published in the Federal Register on October 3, 2007, see Exchange Act Release No. 34-566501: File No. S7-22-06
- Securities and Exchange Commission Act of 1934
- Gramm-Leach Bliley Act of 1999
- FDIC Trust Examination Manual, [Section 10.F](#)
- FRB Regulation R Guidance: [*Exceptions for Banks from the Definition of Broker in the Securities Exchange Act of 1934 – A Small Entity Compliance Guide \(8/2008\)*](#)
- [FIL-89-2008 Securities Activities of Banks: Exceptions and Exemptions for Banks from the Definition of "Broker"](#)
- [FIL-92-2007 Final Regulation R: Exceptions and Exemptions for Banks from the Definition of "Broker"](#)

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