SOUTH DAKOTA DEPARTMENT OF LABOR AND REGULATION

DIVISION OF BANKING

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TRUST COMPANY APPLICATION ATTACHMENTS

ATTACHMENT A - DEFINITIONS

The following definitions are intended to provide the applicants with a basic overview of South Dakota Codified Laws (SDCL), Administrative Rules of South Dakota (ARSD), and the South Dakota Division of Banking (Division) interpretations pertaining to the creation of a South Dakota-chartered trust company.

Private Trust Company (ARSD 20:07:22:03)
A private trust company is one that does not engage in trust company business with the general public or otherwise hold itself out as a trustee or fiduciary for hire by advertising, solicitation, or other means and instead operates for the benefit of a family or families, regardless of whether compensation is received or anticipated.

Public Trust Company (SDCL 51A-6A-1(12A))
A trust company that engages in trust company business with the general public by advertising, solicitation or other means, or a trust company that engages in trust company business but does not fall within the definition of a private trust company established by the commission through rules promulgated pursuant to chapter 1-26.

Trust Company Business (SDCL 51A-6A-1(14))
Engaging in, or representing or offering to engage in, the business of acting as a fiduciary for hire.

Fiduciary for Hire (SDCL 51A-6A-1(7))
Acting as an administrator, conservator, custodian, executor, guardian, personal representative, or trustee, for any person, trust, or estate for compensation or gain or in anticipation of compensation or gain.

South Dakota Situs Requirements (SDCL 51A-6A-11.1)
South Dakota-chartered trust companies are generally encouraged to adopt a business model that provides that most, if not all, account administration and corresponding legal, audit, and compliance functions are performed in South Dakota to demonstrate a sound physical presence.

A public trust company shall:

1) Maintain office space in South Dakota for trust company business and for the storage of, and access to, trust company records required by SDCL 51A-6A-30;
2) Hold no less than two quarterly governing board meetings with a quorum physically present in South Dakota each calendar year;
3) Employ, engage, or contract with at least one trust officer or key employee to provide services for the

trust company in South Dakota related to the powers of the company in SDCL 51A-6A-29 and to facilitate the examinations required by SDCL 51A-6A-31; and

4) Perform trust administration in South Dakota.

Office Space (SDCL 51A-6A-11.2)
For purposes of SDCL 51A-6A-11.1, office space in South Dakota for each public trust company shall:

1) Be in premises distinct and divided from the office space of any other entity;
2) Have the name, charter, and certificate of authority of the trust company prominently displayed;
3) Have access to premises in or adjacent to the office space sufficient to facilitate onsite examinations by the division;
4) To the extent the trust company maintains hard copies of any documents required to be maintained pursuant to SDCL 51A-6A-30, have a secure fireproof file cabinet that contains all such hard copies; and
5) To the extent the trust company maintains any record electronically, have a secure computer terminal or other secure electronic device that provides access to such records, including account information, as necessary to facilitate an efficient and effective examination.

Director Approval of Office Space (SDCL 51A-6A-11.3)
Upon application by a trust company, the director may approve office space that does not meet the requirements of SDCL 51A-6A-11.2 if the director determines the nature and degree of risks presented by the trust company are low based upon a review of the size, nature, and number of accounts administered by the trust company, the structure and business plan of the trust company approved by the division, and the number of employees or persons performing services for the trust company in South Dakota.

If the size, risk profile, or rate of growth of a trust company changes, or if a trust company's office space is insufficient to facilitate onsite examinations by the division, the director may impose additional office space requirements.

Trust Administration (ARSD 20:07:22:04)
For purposes of SDCL 51A-6A-11.1, trust administration in South Dakota means that at least three of the following are performed wholly or partly in South Dakota for the accounts under the management, administration, or custody of the trust company:

1) Annual account reviews;
2) Annual investment reviews;
3) Trust accountings;
4) Account correspondence;
5) Completing trust account tax returns; or
6) Distributing account statements.

Notwithstanding the definition above, trust administration as set forth in SDCL 51A-6A-11.1(4) may be satisfied by other means if the director determines the nature and degree of risks presented by the trust company are low based upon a review of the size, nature, and number of accounts administered by the trust company and the number of employees or persons performing services for the trust company in South Dakota.

If the size, risk profile, or rate of growth of a trust company changes, the director may, to the extent it is deemed necessary, require additional administration be performed in South Dakota to satisfy the requirement in SDCL 51A-6A-11.1(4) as defined by this section.

Officer and Key Employee (SDCL 51A-6A-17)
The term officer does not include individuals who are not involved in the ongoing policy making or management of the trust company.

The term key employee does not include an employee whose primary responsibilities will be limited to clerical or support duties.

Interstate Activity
While this definition does not apply to private trust companies, it may be a helpful resource for the applicants of a private trust company that will rely on individuals or entities located in other jurisdictions (Host States) for administrative and operational support.

SDCL 51A-6A-58 allows existing South Dakota-chartered trust companies (public or private) to establish trust service offices (TSOs) both in South Dakota and in Host State jurisdictions after first applying for and obtaining the approval of the Director. SDCL 51A-6A-1(15) defines a TSO as any office, agency, or other place of business at which the powers granted to a South Dakota trust company are exercised. SDCL51A-6A-29 provides a broad definition of trust company powers. Trust company powers exercised at a location other than that identified on the certificate of authority for South Dakota-chartered trust companies may require the creation of a TSO.

In addition to Division TSO requirements, Host State regulatory authorities may require an additional application or impose additional conditions on the approval of an application to interstate trust activities in their jurisdiction. An applicant for a TSO may restrict the activities that will be performed in the Host State by including language of limitation in its application to the Division and in any application required by the Host State. The Division may then issue a TSO approval that is limited to the services specified in the application and include the same limitations in the certificate of authority. Certain Host States provide for a limited office approval. The Division is willing to work with trust companies to apply for a limited office approval if preferred by the trust company and if the facts and circumstances demonstrate that the practices and structure of the trust company services performed in the Host State are appropriately limited.

<u>Trust Charter Application Review Process</u>
During the trust charter application review process, the Division conducts a thorough review to identify any trust company powers proposed to be exercised at locations outside of South Dakota. Applicant trust companies must provide a detailed and factual statement describing the services to be provided in any Host State for evaluation by the Division. If it appears that trust company business will be performed by the

applicant in a Host State, the Division may require the applicant to commit to applying for a TSO if and when a trust charter is granted. As an alternative to establishing a TSO, the applicant trust company may modify its application to ensure all trust company business will be performed in South Dakota.

While it is not possible to provide an exhaustive list, the following is a general list of the types of activities, facts, and circumstances that the Division considers during the application process:

- Residence of proposed officers, board members, or other key employees
- Proposed location of meetings of the governing board
- Proposed location of meetings of any committees established by the governing board
- Proposed location of account administration performance
- Proposed location of investment management performance
- Proposed location of account opening/closing, acceptance of fiduciary or custodial appointments, and the execution of documents that create or facilitate the fiduciary or custodial capacity
- Proposed location where discretionary distribution decision will be made
- Proposed location of service provider due diligence review performance
- Proposed location of custody vault
- Proposed location of account files and records in hard copy form, or stored on an electronic server
- Proposed location of marketing services

If the exercise of any trust company powers is to be contracted out to, or performed by, a service provider, the Division will verify that the service providers are appropriately registered, licensed, chartered, exempt, or otherwise not subject to regulation as provided in Host State or Federal law or regulation.

Please note that fiduciary activity cannot be contracted to a service provider that does not have the authority to exercise fiduciary powers. Fiduciary activity is a matter of state law and will vary by jurisdiction but is generally considered to include the acceptance of fiduciary appointments, the execution of documents that create or facilitate the fiduciary capacity, and the discretionary decisions regarding the investment or distribution of discretionary assets. As such, fiduciary functions do not include advertising, marketing, or soliciting for fiduciary business; contacting existing or potential customers, answering questions, and providing information about matters related to their accounts; acting as a liaison between the trust company and the customer (*e.g.*, forwarding requests for distribution or changes in investment objectives, or forwarding forms and funds received from the customer); or simply inspecting or maintaining custody of fiduciary assets.

Officers and key employees of affiliated service providers are often appointed as trust company officers and key employees. Please note that any functions performed, at the service provider location, by these officers and key employees on behalf of the trust company while acting in their capacity as a trust company officer or key employee may require the need to create a TSO. However, these same officers and key employees may provide trust company services from the servicing entity location if they are acting in their capacity of an officer or key employee of the service provider, the servicing agreement between the trust company and service provider

clearly identifies the services being provided, and the services are non-fiduciary in nature (unless the servicing entity is authorized to exercise fiduciary powers). During the trust charter application process, proposed officers and key employees that reside outside of South Dakota may be required to provide a detailed written description of their duties and responsibilities, intended travel frequency, and the duration of time they will spend in South Dakota fulfilling said duties and responsibilities.

Interstate Account Management

If accepting trust accounts that are administered under the laws of a state other than South Dakota pursuant to governing document language, trust company management should implement procedures to ensure the trust accounts are managed in compliance with that state's regulation. Prior to acceptance, management must perform and document a thorough review of the applicable laws under the governing document to ensure the trust company has the expertise, or access to the expertise, needed to manage the trust accounts in compliance with applicable law.

Trust Service Office Application Process

The Division utilizes an Application for Interstate Trust Activities (Interstate Application) to facilitate the TSO approval process. The Interstate Application is not intended to replace the forms various state regulatory authorities currently utilize to approve intrastate activities for the institutions that they charter and regulate. If a TSO is required, South Dakota-chartered trust companies are directed to complete and submit to the Division the Interstate Application. When deemed complete, the Division makes arrangements to forward the Interstate Application to the Host State regulatory authority for notice and comment. After receiving any comments and ensuring that any additional requirements by the Host State regulatory authority are addressed by the applicant trust company, the Division will publish notice in the impacted Host State trade area as required by SDCL 51A-2-16. Following a 15-day period for comment, the Director is provided an additional 15 days to issue a decision on the application, and, if approved, the Director will issue a certificate of authority that must be openly displayed at the TSO location. A fill-in version of the Interstate Application can be accessed on the Division's website.

Applicable Provisions of South Dakota Codified Laws

SDCL 51A-6A-58. Establishment of trust service offices--Application. After first applying for and obtaining the approval of the director, one or more trust service offices may be established and operated by a trust company incorporated under the laws of this state or by an out-of-state trust institution, if and to the extent that the state, territory, or district in which the out-of-state trust institution is chartered or licensed to engage in trust company business grants authority for a trust company organized and doing business under the laws of this state to establish an office in that state, territory, or district. An application to establish and operate a trust service office or to relocate an existing trust service office shall be submitted and approved in the manner set forth in SDCL 51A-6A-4.

A trust company may establish a trust service office in another state, territory, or district and may conduct any activities at that office that are permissible for a trust company under the laws of that state, territory, or district subject to the laws of this state and subject to the rules, orders, or declaratory rules of the commission or the director.

The provisions of this section do not apply to a private trust company unless the governing board decides to

establish a trust service office in another state, territory, or district.

SDCL 51A-6A-1(15). "Trust service office," any office, agency, or other place of business at which the powers granted to trust companies are exercised either by a trust company other than the place of business specified in a trust company's certificate of authority or within this state by an out-of-state trust institution.

SDCL 51A-6A-29. Powers of trust company. A trust company may exercise the following powers necessary or incidental to carrying on a trust company business, including:

1) Act as agent, custodian, or attorney-in-fact for any person, and, in such capacity, take and hold property on deposit for safekeeping and act as general or special agent or attorney-in-fact in the acquisition, management, sale, assignment, transfer, encumbrance, conveyance, or other disposition of property, in the collection or disbursement of income from or principal of property, and generally in any matter incidental to any of the foregoing;

2) Act as registrar or transfer agent for any corporation, partnership, association, limited liability company, municipality, state, or public authority, and in such capacity, receive and disburse money, transfer, register, and countersign certificates of stock, bonds, or other evidences of indebtedness or securities, and perform any acts which may be incidental thereto;

3) Act as trustee or fiduciary under any mortgage or bond issued by a person;

4) Act as trustee or fiduciary under any trust established by a person;

5) Act as fiduciary, assignee for the benefit of creditors, receiver, or trustee under or pursuant to the order or direction of any court or public official of competent jurisdiction;

6) Act as fiduciary, guardian, conservator, assignee, or receiver of the estate of any person and as executor of the last will and testament or administrator, fiduciary, or personal representative of the estate of any deceased person when appointed by a court or public official of competent jurisdiction;

7) Establish and maintain common trust funds or collective investment funds pursuant to the provisions of chapter 55-6; or

8) Act in any fiduciary capacity and perform any act as a fiduciary which a South Dakota bank with trust powers may perform in the exercise of those trust powers.

ATTACHMENT B – STATEMENT OF PRINCIPLES OF TRUST MANAGEMENT

The board of every South Dakota-chartered trust company, both private and public, is required to adopt the Statement of Principles of Trust Management (Statement) at the first organizational meeting. The board should document a thorough review of the Statement annually to ensure ongoing compliance.

The following is an example of the Statement structure, the italicized sections provide additional detail and need not be included in the adopted resolution. The actual language adopted by the board should be revised to identify trust company-specific oversight responsibilities, taking into consideration the size, complexity, and risk profile of the trust company. However, the board cannot exclude or minimize any Statement principles.

<u>Statement of Principles of Trust Management</u>

The board, by proper resolution included in its minutes, should:

1. Designate an officer, qualified and competent, to be responsible for and administer the activities of the trust company. In addition, the board should define the officer's duties.

2. Name a trust committee consisting of at least three directors/managers to be responsible for and supervise the activities of the trust company. The committee should include, where possible, one or more directors who are not active officers of the company.

Nothing herein is intended to prohibit the board from acting as the trust committee, or from appointing additional committees and officers to administer the operations of the trust company. When delegating duties to subcommittees and/or officers, the board and the trust committee continue to be responsible for the oversight of all trust activities. Sufficient reporting and monitoring procedures should be established to fulfill this responsibility.

The trust committee should:

a. Meet at least quarterly, and more frequently if considered necessary and prudent to fulfill its supervisory responsibilities;

b. Approve and document the opening of all new trust accounts; all purchases and sales of, and changes in, trust assets; and the closing of trust accounts;

c. Provide for a comprehensive review of all new accounts for which the company has investment responsibility promptly following acceptance;

d. Provide for a review of each trust account, including collective investment funds, at least once during each calendar year. The scope, frequency, and level of review (trust committee, subcommittee, or disinterested account officer) should be addressed in appropriate written policies which give consideration to the company's fiduciary responsibilities, type and size of account, and other relevant factors. Generally, discretionary account reviews should cover both administration of the account and suitability of the account's investments, while non-discretionary account reviews should only address account administration;

e. Keep comprehensive minutes of meetings held and actions taken; and

f. Make periodic reports to the board of its actions.

3. Provide comprehensive written policies which address all important areas of trust company activities.

4. Provide competent legal counsel to advise trust officers and the trust committee on legal matters pertaining to fiduciary activities.

5. Provide for adequate internal controls including appropriate controls over trust assets.

6. Provide for an adequate audit (by internal or external auditors or a combination thereof) of all fiduciary activities, annually. The findings of the audit, including actions taken as a result of the audit, should be recorded in its minutes.

   If a trust company adopts a continuous audit process in lieu of performing an annual external audit, management must report a thorough internal review of trust company operations and administration to the board quarterly. The internal review should include, but is not limited to, documentation of trust company assets, liabilities, and equity position; trust company financial performance; assets held in trust accounts, both discretionary and non-discretionary; and any non-ordinary transactions. Additionally, internal controls and segregation of duties must be periodically assessed if the trust company adopts a continuous audit process in lieu of annual external audits. Internal audits may be performed, on an activity-by-activity basis, at intervals commensurate with the level of risk associated with that activity. Audit intervals must be supported and reassessed regularly to ensure appropriateness given the current risk and volume of the activity. For specific activity examples, refer to the Division's Internal Audit Guidance located on our website.

7. Receive reports from the trust committee and record actions taken in its minutes.

8. Review the examination reports of the trust company by supervisory agencies and record actions taken in its minutes.

ATTACHMENT C – STATEMENT OF PRINCIPLES OF TRUST MANAGEMENT - CUSTODIAL

The board of every South Dakota-chartered trust company, both private and public, is required to adopt the Statement of Principles of Trust Management (Statement) at the first organizational meeting. The board should document a thorough review of the Statement annually to ensure ongoing compliance.

The following is an example of the Statement structure, the italicized sections provide additional detail and need not be included in the adopted resolution. The actual language adopted by the board should be revised to identify trust company-specific oversight responsibilities, taking into consideration the size, complexity, and risk profile of the trust company. However, the board cannot exclude or minimize any Statement principles.

<u>Statement of Principles of Trust Management</u>
The board, by proper resolution included in its minutes, should:

1. Designate an officer, qualified and competent, to be responsible for and administer the activities of the trust company. In addition, the board should define the officer's duties.

2. Name a committee consisting of at least three directors to be responsible for and supervise the activities of the trust company. If possible, the committee will include at least one director that is not an active officer of the trust company.

Nothing herein is intended to prohibit the board from acting as the trust committee, or from appointing additional committees and officers to administer the operations of the trust company. When delegating duties to subcommittees and/or officers, the board and the trust committee continue to be responsible for the oversight of all trust activities. Sufficient reporting and monitoring procedures should be established to fulfill this responsibility.

The committee should:

a. Meet at least quarterly, and more frequently if considered necessary and prudent to fulfill supervisory responsibilities.

b. Provide for comprehensive oversight of the account opening and account closing processes, as well as the oversight of all purchases, sales, and/or changes in account assets utilizing predefined asset review factors.

An effective asset oversight program is generally an extension of the internal account review process and can help mitigate risks associated with prohibited transactions and fraudulent activity. Examples of predefined asset review factors include, but are not limited to, asset types, surname comparison, participant ownership interest in entities held, unsecured promissory notes exceeding a predetermined value, above average promissory note rates of return, past-due promissory notes, multiple accounts holding the same investments exceeding a predetermined aggregate value, asset increases/decreases above or below a predetermined level, undelivered assets exceeding a predetermined timeframe, and any suspicious activities. Management should assign risk levels or risk

ratings to the different account, asset, and transaction types based on the risk levels. Those in the higher risk categories should be "flagged" and subject to escalated review procedures, with a focus on potential prohibited transactions and fraudulent activity.

c. If applicable, provide for a prompt comprehensive review of all new accounts for which the trust company has investment responsibility.

d. Provide for an adequate account review program utilizing an account sample that is commensurate with the account population and other relevant risk factors. The scope, frequency, and level of review (committee or disinterested account officer) will be addressed in appropriate written policies that give consideration to the trust company's responsibilities, type and size of account, asset type, and other relevant factors.

   Relevant risk factors may include account type and size, customer residence, administrative officers, asset classification, stale-valued assets, physical location of the asset, high asset returns/growth, new accounts, closed accounts, complaints, etc. An effective account review program generally identifies the accounts, transactions, or assets "flagged" during the asset oversight program.

e. Keep comprehensive minutes of meetings held and actions taken.

f. Make periodic reports to the board of its actions.

3. Provide comprehensive written policies which address all important areas of trust company activity.

4. Provide competent legal counsel to advise management on legal matters pertaining to trust company activity.

5. Provide for adequate internal controls including appropriate controls of account assets.

6. Provide for an adequate audit (by internal or external auditors or a combination thereof) of all trust company activity, annually. The findings of the audit, including actions taken as a result of the audit, should be recorded in meeting minutes.

   If a trust company adopts a continuous audit process in lieu of performing an annual external audit, management must report a thorough internal review of trust company operations and administration to the board quarterly. The internal review should include, but is not limited to, documentation of trust company assets, liabilities, and equity position; trust company financial performance; assets held in trust accounts, both discretionary and non-discretionary; and any non-ordinary transactions. Additionally, internal controls and segregation of duties must be periodically assessed if the trust company adopts a continuous audit process in lieu of annual external audits. Internal audits may be performed, on an activity-by-activity basis, at intervals commensurate with the level of risk associated with that activity. Audit intervals must be supported and reassessed regularly to ensure appropriateness given the current risk and volume of the activity. For specific activity examples, refer to the Division's Internal Audit Guidance located on our website.

7. Receive committee reports and record actions taken in its minutes.

8. Review the examination reports of the trust company by supervisory agencies and record actions taken in its minutes.