SOUTH DAKOTA
Division of Banking

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Trust Company Examination Procedures

South Dakota Codified Laws (SDCL) 51A-6A-31 requires the South Dakota Division of Banking (Division) to examine each trust company at least once every 36 months. SDCL 51A-6A-33 provides that each trust company is required to pay all salary and travel expenses associated with the examination process. Generally, examinations are scheduled for three weeks with at least one week performed on-site.

The examination generally includes a review of internal policies, practices, and procedures; board and committee meeting minutes; affiliate relationships; external and internal audits performed; compliance with applicable fiduciary laws, rules, and principles including South Dakota situs requirements; account administration and compliance with governing instruments; earnings performance including a capital adequacy assessment; asset management; and operations. If any asset management or operations functions are outsourced, the examination will focus on the documentation of the trust company's due diligence review of the provider(s). Transaction testing and the Bank Secrecy Act (BSA) compliance assessment are generally performed in conjunction with the account compliance review. The examination will also include an assessment of Regulation R compliance requirements. BSA and Regulation R guidance can be found on the Division's website.

For purposes of safety and soundness examinations, South Dakota-chartered trust companies are divided into two classes:

Public Trust Company – 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. The commission shall consider the size, number of clients served and the family and other relationships among the clients served, complexity, and related safety and soundness issues as it establishes in rule a definition for the term private trust company. SDCL 51A-6A-1(12A).

Private Trust Company – 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. ARSD 20:07:22:03.

Private Trust Company Examination Procedures

Private trust companies receive a full-scope examination at least once every 36 months or sooner if deemed necessary by the Director, based on the volume and type of fiduciary activities. Upon completion, a composite rating of ***Strong, Satisfactory***, ***Needs Improvement***, or ***Unsatisfactory*** is assigned based on the following definitions:

- ***Strong*** **–** Trust companies so rated are sound in every respect. Any weaknesses are minor and can be handled in a routine manner by management. The institution is in substantial compliance with fiduciary laws and regulations.

- ***Satisfactory*** - Trust companies so rated are fundamentally sound. Any weaknesses are minor and can be handled in a routine manner by management.

- ***Needs Improvement –*** Trust companies so rated exhibit some degree of supervisory concern in one or more areas. Moderate weaknesses are present and are well within management's capabilities and willingness to correct.

- ***Unsatisfactory*** - Trust companies in this group exhibit practices and conditions that may be unsafe and unsound if not addressed. Management may lack the ability or willingness to effectively address weaknesses within appropriate time frames.

Public Trust Company Examination Procedures

Public trust companies receive a full-scope examination at least once every 24 months or sooner if deemed necessary by the Director. Upon completion, a numeric rating of 1 through 5, with 1 being the best, is assigned for individual components, as well as the composite rating. A modified version of the Uniform Interagency Trust Rating System and corresponding MOECA components (Management/Situs, Operations, Earnings/Capital, Compliance, and Asset Management) is used for assigning ratings. Modifications include capital adequacy and South Dakota situs assessments. Composite ratings are assigned based on the following definitions:

- A Trust Rating of "1" is assigned. Administration of fiduciary activities is sound in every respect. Generally, all components are rated "1" or "2." Any weaknesses are minor and can be handled in a routine manner by management. The institution is in substantial compliance with fiduciary laws and regulations. Risk management practices are strong relative to the size, complexity, and risk profile of the institution's fiduciary activities. Fiduciary activities are conducted in accordance with sound fiduciary principles and give no cause for supervisory concern.

- A Trust Rating of "2" is assigned. Administration of fiduciary activities is fundamentally sound. Generally, no component rating should be more severe than "3." Only moderate weaknesses are present and are well within management's capabilities and willingness to correct. Fiduciary activities are conducted in substantial compliance with laws and regulations. Overall risk management practices are satisfactory relative to the institution's size, complexity, and risk profile. There are no material supervisory concerns and, as a result, the supervisory response is informal and limited.

- A Trust Rating of "3" is assigned. Administration of fiduciary activities exhibits some degree of supervisory concern in one or more of the component areas. A combination of weaknesses exists that may range from moderate to severe; however, the magnitude of the deficiencies generally does not cause a component to be rated more severely than 4. Management may lack the ability or willingness to effectively address weaknesses within appropriate time frames. Additionally, fiduciary activities may reveal some significant noncompliance with laws and regulations. Risk management practices may be less than satisfactory relative to the institution's size, complexity, and risk profile. While problems of relative significance may exist, they are not of such importance as to pose a threat to the trust beneficiaries generally, or to the soundness of the institution. The institution's fiduciary activities require more than normal supervision and may include formal or informal enforcement actions.

- A Trust Rating of “4” is assigned. Fiduciary activities generally exhibit unsafe and unsound practices or conditions, resulting in unsatisfactory performance. The problems range from severe to critically deficient and may be centered around inexperienced or inattentive management, weak or dangerous operating practices, or an accumulation of unsatisfactory features of lesser importance. The weaknesses and problems are not being satisfactorily addressed or resolved by management. There may be significant noncompliance with laws and regulations. Risk management practices are generally unacceptable relative to the size, complexity, and risk profile of fiduciary activities. These problems pose a threat to the account beneficiaries generally and, if left unchecked, could evolve into conditions that could cause significant losses to the institution and ultimately undermine the public confidence in the institution. Close supervisory attention is required, which means, in most cases, formal enforcement action is necessary to address the problems.

- A Trust Rating of “5” is assigned. Fiduciary activities are conducted in an extremely unsafe and unsound manner. Administration of fiduciary activities is critically deficient in numerous major respects, with problems resulting from incompetent or neglectful administration, flagrant and/or repeated disregard for laws and regulations, or a willful departure from sound fiduciary principles and practices. The volume and severity of problems are beyond management's ability or willingness to control or correct. Such conditions evidence a flagrant disregard for the interests of the beneficiaries and may pose a serious threat to the soundness of the institution. Continuous close supervisory attention is warranted and may include termination of the institution's fiduciary activities.