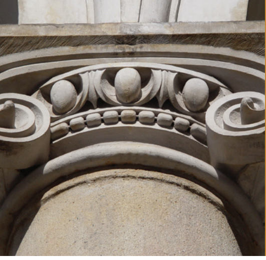

By **David Peterson**

Trust Company Requirements In Top U.S. Jurisdictions

Understand the key regulatory and operational provisions

Practitioners around the world continue to search for the best jurisdiction for their clients. Several states have persisted in adopting legislation to attract trust business both domestically and globally. An often-overlooked component for practitioners is whether their firm or clients may benefit from the creation of a trust company. Practitioners will be better able to help their clients if they understand trust companies as well as the key regulatory and operational requirements in some of the best boutique trust jurisdictions in the United States.

Benefits of Starting Trust Company

Trust companies are sought by individuals, families or companies that are looking to exercise a specific trust power. Most regulated trust companies are formed as non-depository trust companies. Non-depository trust companies can't engage in the business of banking, which means they can't accept deposits or make loans.[1] State law will dictate which specific activities are permissible for the trust company.[2] An application for a regulated trust company usually contains a detailed explanation of why the applicants desire a trust company charter/license and what trust power(s) will be used. Trust companies are most frequently used to serve as a trustee or custodian. The most common reasons for creating a regulated trust company include:

- Private families seeking an exemption from SEC registration under the Investment Advisers Act of 1940 (Advisers Act);
- Private families seeking confidentiality on fiduciary matters;
- Private families holding closely held assets that are unsuitable for traditional corporate trustees;
- Firms seeking to minimize liability for serving as an individual trustee (for example, law firms, accounting firms and registered investment advisors); and
- Firms that have a specific business purpose (for example, custodian) for a trust charter/license.

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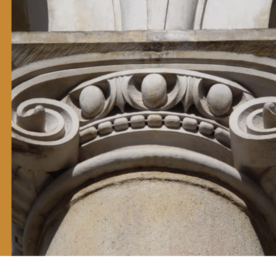
Public vs. Private

What's the difference between a public/retail trust company and a private family trust company (PFTC)? Public/retail trust companies are permitted to serve as a fiduciary with the public and market their services to the public. In South Dakota, a "public trust company" is defined as: 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 doesn't fall within the definition of a PFTC.[3]

A PFTC is one that doesn't 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.[4] Many states define who qualifies as a "family member" for purposes of the PFTC based on kinship to a designated relative.[5] State law can vary regarding these definitions. However, state law consistently dictates that PFTCs shouldn't transact business with the general public.[6]

Regulated vs. Unregulated

What's the difference between a regulated trust company and an unregulated trust company? Regulated trust companies include both public/retail trust



companies and PFTCs. Public/retail trust companies are regulated by state banking authorities because they interact with the general public. PFTCs can be either regulated or unregulated. Nevada, New Hampshire, South Dakota, Tennessee and Wyoming all permit regulated PFTCs. Wyoming and Nevada also allow unregulated PTFCs.[7]

Both regulated and unregulated trust companies are required to complete corporate formation through the Secretary of State. Regulated trust companies are required to submit an application and complete a formal approval process by state banking authorities. They're also subject to examination by state banking authorities in the state where the trust company was chartered/licensed. The timing and frequency of examinations as well as the cost will vary based on the state.

What advantages do regulated or unregulated PFTCs offer? Regulated PFTCs offer family offices a potential exclusion from the need to register as an investment advisor with the SEC. The Advisers Act excludes domestic banks from the definition of "investment adviser."[8] Trust companies supervised by state banking authorities are included in the definition of "bank."[9] Unregulated trust companies aren't subject to capital and examination requirements. In addition, unregulated trust companies typically have fewer operating costs than regulated trust companies.

Frequently Used States

Those states that practitioners often use to situs trusts are also some of the best states to form a trust company. Practitioners have traditionally looked to Nevada, South Dakota and Wyoming. In addition, Tennessee and New Hampshire have also recently enacted legislation to make their respective jurisdictions desirable. Delaware is often used by large institutions. As of Jan. 1, 2021, South Dakota leads the nation in the number of regulated public trust companies and PFTCs. Wyoming and Nevada are used frequently for unregulated PFTCs.

Unregulated/unlicensed PFTCs are difficult to access. Unlike regulated trust companies, state regulators don't publicly disclose the names of those that have chosen to be unregulated/unlicensed. Nevada unlicensed PFTCs aren't permitted to use the word "trust" or any direct derivative of that word as a part of its name.[10] Nevada unlicensed PFTCs must provide the Commissioner of the Nevada Financial Institutions Division with the name of the "designated relative" associated with the trust company.

Wyoming unregulated PFTCs are easier to identify through the Wyoming Secretary of State. To avoid confusion, Wyoming requires unregulated PFTCs to use "Single Family Private Trust Company" in the name of the trust company if the trust company wants to use "trust" in its name. Approximately 250 "active" status entities with the Wyoming Secretary of State used "Single Family Private Trust Company" in their name.[11]

State regulators typically examine trust companies through a review of the management, operations, earnings, compliance and asset management components.

Wyoming does require the directors or managers of unregulated PFTCs to execute an annual waiver to the state banking commissioner acknowledging that the PFTC isn't supervised by the commissioner and that the PFTC won't transact trust company business with the general public.[12]

See "Comparison of Requirements," pp. 20-21.

Examinations

State regulators typically examine regulated trust companies through a review of the management, operations, earnings, compliance and asset management (MOECA) components. A full review of the components can be found by reviewing the *FDIC Trust Examination Manual*.[13] Although state regulators aren't specifically bound by the *FDIC Trust Examination Manual*, it's a very helpful resource for those who are looking to understand examination criteria and fiduciary best practices. For public/retail trust companies, state regulators often will rate each of the MOECA components. Based on those individual component ratings, regulators will then assign a composite rating for the trust company, with "1" being the best and "5" being the worst.[14]

Comparison of Requirements

Trust company laws in five states

	South Dakota	Nevada
Regulated private family trust company (PFTC)	Yes; SDCL 51A-6A-7	Yes; NRS 669A
Number of regulated PFTCs (as of Jan. 1, 2021)	42	32
Minimum capital requirement—regulated PFTC	$200,000; SDCL 51A-6A-19	$300,000; NRS 669A.160
Regulated PFTC—board member requirements	Minimum 3 board members; maximum 12 board members; 1 South Dakota resident board member; at least half of the board must be U.S. citizens. SDCL 51A-6A-13	No specific requirement in statute
Exam frequency—regulated PFTC	Once every 36 months or more frequently if director considers it necessary to make full and careful examination and inquiry into condition of the affairs of the trust company. SDCL 51A-6A-31	Each licensed family trust company shall undergo an off-site examination or an independent review more than 1 year but not more than 2 years after the date on which its license was issued; subsequent exam within 1 year if report of exam rates the trust company as "unsatisfactory" or "needs improvement;" within 3 years if rated as "satisfactory." NAC 660A-200
Unregulated PFTC	No	Yes; NRS 669A.110
Regulated public/retail trust company	Yes; SDCL 51A-6A-7	Yes; NRS 669
Number of regulated public/retail trust companies (as of Jan. 1, 2021)	63	21
Minimum capital requirement—regulated public/retail trust company	Statutory minimum capital of a trust company is $200,000. Director may require that trust company have more capital than amount specified if director determines that the amount and character of the anticipated business of the trust company and the safety of the customers so require. SDCL 51A-6A-19. In application, minimum capital requirement for public trust companies starts at $400,000	$1 million; NRS 669.100
Exam frequency—regulated public/retail trust company	Once every 36 months or more frequently if director considers it necessary to make a full and careful examination and inquiry into the condition of the affairs of the trust company. SDCL 51A-6A-31	Annual examinations per Nevada Department of Financial Institutions. Commissioner shall examine as often as necessary. NRS 669.250
Board meetings	Quarterly; SDCL 51A-6A-15	Quarterly; NRS 669.115
Regulated public/retail trust company—board member requirements	Minimum 5 board members; 1 South Dakota resident board member; at least half of the board must be U.S. citizens. SDCL 51A-6A-13	Minimum 5 board members. However, commissioner may approve 3 member boards as appropriate. NRS 669.116
List of chartered/licensed trust companies	*https://dlr.sd.gov/banking/licensed_providers/state_chartered_trust_companies.pdf*	Nevada doesn't publish a list of licensed trust companies. Number of trust companies obtained through Public Information Officer; Nevada Department of Business and Industry

Wyoming	Tennessee	New Hampshire
Yes; WSA 13-5 Article 6	Yes; TCA 45-2-2001	Yes; Chapter 383-D
4	Not available	4
$500,000; WSA 13-5-208	$500,000; TCA 45-2-2107. However, Tennessee Department of Financial Institutions grants exemptions to capital requirement as appropriate	$200,000; 383-D:6-602
No specific requirement in statute	No specific requirement in statute	Minimum 3 board members. Board members need not be a resident of New Hampshire or a citizen of the United States unless required by the commissioner. 383-D:8-801
Once every 36 months or as often as deemed necessary. WSA 13-5-607	Once every 36 months per Tennessee Department of Financial Institutions	Commissioner shall examine a family trust company every 36 months. 383-D:11-1101
Yes; WSA 13-5 Article 7	No	No
Yes; WSA 13-5 Article 5	Yes; TCA 45-2-2102	Yes; Chapter 383-C
13	15	32
$1 million; WSA 13-5-511. In application, minimum capital requirement for public trust companies starts at $1.2 million. Per WSA 13-5-511, no public trust company shall organize without a paid-up surplus fund of at least 20% of its legally authorized capital stock or membership interest and undivided profits in sufficient amount for the first year expenses of operation as determined by commissioner	$500,000; or such greater amount as may be required by commissioner after considering factors in this section. TCA 45-2-2107	$500,000; commissioner may require a trust company to maintain required capital in excess of minimum required capital. 383-C:5-502
Once every 24 months or as often as deemed necessary. WSA 13-5-521	At least once in an 18-month period, except commissioner may extend the exam cycle up to an additional 18 months. TCA 45-2-1602	Commissioner shall examine condition and management of a trust company every 18 months, or more often when necessary in his or her judgment. 383-C:14-1401
Quarterly; WSA 13-5-520	Quarterly; TCA 45-2-2018(c)	Quarterly; 383-C:6-602
Minimum 5 board members. WSA 13-5-519	Minimum 5 board members. TCA 45-2-2108(a)	Minimum 5 board members. 383-C:6-601
http://wyomingbankingdivision.wyo.gov/regulated-financial-institutions/trust-companies	*www.tn.gov/content/dam/tn/financialinstitutions/bank-docs/2020-bank-division-updates/Listing%20of%20State%20Chartered%20Public%20Trust%20Companies%20-%2001.08.2020.pdf*	*www.nh.gov/banking/bank-cu-trust/documents/trusts.pdf*

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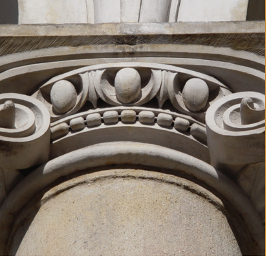


For chartered/licensed PTFCs, state regulators most often use a "satisfactory, needs improvement or unsatisfactory" rating system. Each state has its own areas in which examiners will focus. It's recommended that applicants learn examiner expectations and specific areas examiners will review. The frequency of examinations is often mandated via state law and examination results.

State regulators are often willing to outline items that will be reviewed well in advance of the examination.

Some states complete an initial review that amounts to a "practice examination" of the trust company prior to the first full examination. Wyoming and Tennessee are among the states that will complete an initial review within the first 12 months of charter/licensing. The frequency of examinations varies from state to state. However, most states will assign an examination schedule of between one to three years. Although the examination process can create anxiety for those who aren't used to operating in a regulated environment, state regulators are often willing to outline items that will be reviewed well in advance of the examination.

Capital Requirements

Generally, regulated PFTCs should anticipate a minimum capital requirement of between $200,000 and $500,000. Regulated public/retail trust companies should generally anticipate a minimum capital requirement of between $400,000 and $2 million.

Capitalization will vary based on the proposed trust company's overall risk profile, pro forma income and expense projections and state jurisdiction selected. For example, South Dakota public trust companies serving as trustees of foreign trusts or as custodians of cryptocurrency have been required to contribute and maintain higher capital.

Expenses

In addition to capitalization requirements, prospective trust companies should consider the costs to establish and operate a trust company. Generally, the costs for a PFTC are less than for a public trust company. Most applicants hire legal counsel or consult with an expert who understands the requirements for trust company formation. There's also an application fee that's due to the state.[15]

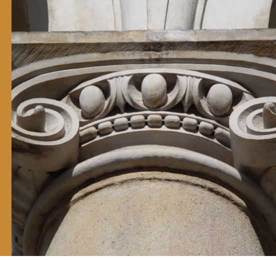
Annual operating costs will vary based on the state selected, trust company designation (private vs. public), business model and number of accounts. Traditional expenses include: directors' and officers' insurance; financial institution bond; annual fees due to the state of charter; board memberships; trust accounting software; and employees/third-party service providers for account administration.

Account administration is typically the largest variable expense. A public/retail trust company with several hundred accounts will have considerably more operational costs than a PFTC with a few accounts. As part of the application process, trust company applicants will need to prepare detailed pro forma financials that outline anticipated income and expenses.

Employees

Requirements for trust company employees vary from state to state. For example, Nevada requires each retail and licensed trust company to have an employee who's a resident of Nevada in the principal office who has experience that's deemed satisfactory to the commis-sioner in accepting and administering trusts.[16] South Dakota requires public trust companies to 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 and to facilitate examinations.[17] In addition, South Dakota public trust companies are required to perform trust administration in South Dakota.[18] It's important to have understanding of your state's requirements.

Practitioners should be aware that state regula-tors have become increasingly concerned with trust powers and trust administration being performed outside the state of charter/license without proper authorization. In most instances, these concerns can be overcome by either performing trust powers and administration in the state of charter or by seeking the appropriate designation with state banking regulators to perform trust company business or marketing out-



side the state of charter.

License/Charter Process

A regulated trust company can be formed through proper application to a state banking authority. The formation process will vary based on the type of application and state where the application is filed. After the application is filed with the state authorities, regulators will conduct a thorough review of the application and its corresponding business plan. In addition, regulators will conduct background checks on the proposed owners, board members, officers and employees.[19] An in-person or virtual meeting between the board members and regulators is typically required prior to approval.

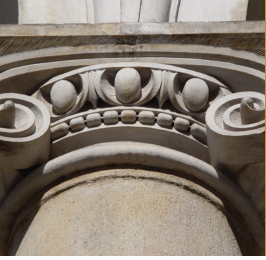
Approval Process

The approval process and the length of time needed to receive approval varies from state to state. Generally, it takes approximately five to nine months to receive a private or public trust company charter/license. Time frames will vary based on the trust company designation (private or public), the complexity of the business model, the quality of the application submitted and the number of applications currently pending in the state selected.

Ongoing Requirements

The requirements for regulated trust companies will vary based on the jurisdiction and designation as either a public/retail or PFTC. In addition to periodic examinations, regulated trust companies should plan to have a physical office in the jurisdiction of charter/license where original or trust copies, including electronic copies, of all material business records and accounts of the trust company may be accessed and readily available for examination by the commissioner.[20]

Public/retail trust companies typically are required



to have a minimum of five board members.[21] Some states require PFTCs to have a minimum of three board members.[22] Regulators will likely review the backgrounds and complete criminal background checks of prospective board members, officers, employees and principal owners. No individual who's been convicted of any felony or any crime involving fraud, dishonesty or a breach of trust may serve as a board member, officer or key employee of a trust company.[23] Trust companies that have non-U.S. citizens serving in a trust company capacity likely will be required to complete enhanced due diligence with state regulators. In addition, state regulators may also complete a background check with FINRA on those applicants who are registered with the SEC.

Regulated trust companies are also often required to hold quarterly board meetings.[24] In addition, regulated trust companies are often required to maintain a bank account with a state or nationally chartered bank having a principal branch in the state of charter/license.[25]

Valuable Tool

The U.S. trust company concept can be a valuable tool for firms and clients. Although many assume trust companies only benefit the ultra-wealthy, U.S. trust companies serve a diverse market for those who need financial services. The U.S. trust company designation continues to be extremely desirable both domestically and internationally. An understanding of key state requirements is an important step in the process.

Endnotes

1. South Dakota Codified Law (SDCL) 51A-6A-1 (14); Nevada Revised Statutes (NRS) 669.210; New Hampshire Revised Statutes Annotated (RSA) 383-C:3-302.
2. SDCL 51A-6A-1; Wyoming Statutes Annotated Statute (WSA) 13-5-10(b); NRS 669.210; Tennessee Code Annotated (TCA) 45-2-1002; New Hampshire RSA 383-C:3-301.
3. *See* SDCL 51A-6A-1(12A).
4. *See* South Dakota Administrative Rule 20:07:22:03.
5. New Hampshire RSA 383-D:4-402; NRS 669.042; WSA 13-5-204(a)(VI); TCA 45-2-2001.
6. *See supra* note 4; TCA 45-2-2002(b)(1); New Hampshire RSA 383-D:7-701; NRS 669.042.
7. WSA 13-5 Article 7; NRS 669A.110.
8. Investment Advisers Act of 1940 (Advisers Act), Section 202(a)(11)(A)–(E).
9. Advisers Act, Section 202(a)(2)(C).
10. NRS 669A.150.
11. *https://wyobiz.wyo.gov/Business/FilingSearch.aspx.*
12. WSA Section 13-5-701.
13. *www.fdic.gov/regulations/examinations/trustmanual/.*
14. *www.fdic.gov/regulations/examinations/trustmanual/appendix_b/appendix-_b.html.*
15. SDCL 51A-6A-6; NRS 669.150; NRS 669A.190; WSA 13-5-503; WSA 13-5-606; Tennessee Chapter 0180-07 of the Rules of the Department of Financial Institutions; TCA 45-2-2002(a)(1)(A) and Rule 0180-7.08(1)(m) of the Rules of the Department of Financial Institutions.
16. NRS 669.083.
17. SDCL 51A-6A-11.1.
18. SDCL 51A-6A-11.1; SDAR 20:07:22:04.
19. NRS 669.160; SDCL 51A-6A-17.
20. WSA 13-5-604; SDCL 51A-6A-11.2.
21. SDCL 51A-6A-13; NRS 669.116; WSA 13-5-519; New Hampshire RSA 383-C:6-601.
22. SDCL 51A-6A-13; New Hampshire RSA 383-D:8-801.
23. SDCL 51A-6A-17.
24. SDCL 51A-6A-15; NRS 669.115.
25. WSA 13-5-604; NRS 669A.110.

SPOT LIGHT

Roaming Around

A Bunch of Bison by Tucker Smith sold for $35,700 at Jackson Hole Art Auction's 2020 auction in Jackson Hole, Wyo. Wildlife and the mountains are the inspiration behind Smith's detail-oriented landscapes. He has an uncanny ability to convey the vastness of the sprawling fields and country in his work. Although his talent was readily apparent from a young age, Smith initially spent eight years as a computer programmer after college before making art his full-time career.