

SENATE BILL REPORT

SB 5107

As Amended by House, April 12, 2019

Title: An act relating to trust institutions.

Brief Description: Addressing trust institutions.

Sponsors: Senators Das and Mullet; by request of Department of Financial Institutions.

Brief History:

Committee Activity: Financial Institutions, Economic Development & Trade: 1/15/19, 1/17/19 [DP].

Floor Activity:

Passed Senate: 3/04/19, 46-0.

Passed House: 4/12/19, 98-0.

Brief Summary of Bill

- Clarifies the definition of trust business and allows the Department of Financial Institutions (DFI) to expand the definition of trust business to accommodate activities that are closely akin to acting as a fiduciary through rulemaking.
- Defines doing business in Washington State to include out-of-state trust institutions that do not have a physical presence, but conduct trust business in the state.
- Provides a variety of enforcement actions that DFI may take against trust companies.
- Defines third-party service providers as they relate to trust business and provides rulemaking authority to DFI to initiate procedures to examine them under certain conditions.
- Provides specific guidance on certain life-cycles such as mergers and dissolutions that are specific to trusts.

SENATE COMMITTEE ON FINANCIAL INSTITUTIONS, ECONOMIC DEVELOPMENT & TRADE

This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.

Majority Report: Do pass.

Signed by Senators Mullet, Chair; Hasegawa, Vice Chair; Wilson, L., Ranking Member; Braun, Das and Hobbs.

Staff: Clint McCarthy (786-7319)

Background: A trust is a form of ownership of property that separates responsibility or control of the property from the benefits of ownership. Washington law defines a "trust company" as a corporation organized under the laws of the state engaged in trust business. In general terms, Washington law defines trust business as executing trusts of every description consistent with the law. Trust companies also have powers and privileges conferred on banks, but they are subject to the restriction that DFI may require that they have FDIC insurance and be otherwise capitalized as an FDIC insured bank before they may conduct themselves as a bank, that is, take deposits from the public. Non-depository trust companies serve a different function than banks. The exercise of trust powers is neither essential to being a bank nor automatically conferred upon a bank when receiving a charter.

In 2014, Title 30 RCW was divided into two separate acts: the Washington State Commercial Banking Act codified under Title 30A and the Washington Trust Institutions Act (WTIA), codified under Title 30B. The WTIA established a new statutory model for trust institutions. Numerous provisions in WTIA incorporate or reference the regulations and requirements under current law. Various provisions germane to trust institutions which are currently dispersed throughout Title 30 RCW were clarified within the new Title 30B.

In 2015, the Legislature amended Title 11 RCW to clarify how a trustee delegates power and acts as a fiduciary with respect to a trust. As part of this legislation, the Washington Directed Trust Act allows a trustor to direct specific functions to third parties—statutory trust advisors and directed trustees—rather than conferring all authority, duties, and liability upon the trustee.

Since the enactment of WTIA, DFI has chartered 11 trust companies. The majority of these trust companies are relatively small and incorporated as limited liability companies.

Trust business is defined in RCW 30B.08.080 to include a variety of custodial and non-fiduciary roles including bailee, escrow agent, registrar, recordkeeper, receiver, or transfer agent.

DFI is the regulator of state-chartered banks and trust companies. In order to legally engage in trust business in the state, a non-bank corporation or limited liability company must obtain a trust company charter. DFI, as the primary state regulator, is responsible for oversight of the safety and soundness of such state-chartered financial institutions. Under Title 30B, DFI may obtain a supervisory order related to economic conditions through issuing a temporary cease and desist order under adjudicative enforcement provisions. Prudential regulation is a type of financial regulation that requires financial firms to control risks and hold adequate capital as defined by capital requirements.

Trust companies are permitted under the statutory authority of RCW 30A to:

- merge into other entities;

- acquire trust companies;
- convert to or from a federal trust company charter;
- liquidate voluntarily; and
- liquidate involuntarily.

Summary of Bill: Organization of Trusts. *Organizational Governance Requirements of State Trust Companies.* A state trust company may operate either as a limited liability company or a corporation. Application requirements for a state trust company charter are amended to require background checks, including fingerprints for any officer, director, manager, or managing participant. An initial board of directors must include five persons, including two individuals who must be independent of the corporation or LLC. The statutory requirement for applicants to publish a notice of an application and for DFI to publish a written report of its investigation into the applicants is removed.

Statute is amended to provide state trust companies to have the same powers and authorities of a federally chartered trust company and of any out of state trust institution. The bill clarifies the make-up, duties, and fiduciary duties of a board. This includes compliance with federal regulations applicable to the fiduciary activities of a federally-insured state bank.

Clarifying the Definition of the Term Trust Business. The definition of the term trust business is clarified by defining what acts by a trustee are trust business, rather than defining what acts constitute trust business under current statute. DFI is provided rulemaking authority to expand the definition of trust business to accommodate certain kinds of non-fiduciary custodial arrangements and certain technology solutions. Significant activities of a trust business include:

- accepting or executing trusts;
- acting as an attorney-in-fact;
- acting pursuant to court order as executor, administrator, guardian, or conservator; and
- regularly engaging in any other activity that the director of DFI (director) determines by rule to be an essential function of a trust business in the state of Washington.

Doing Business in Washington State. The term doing business in Washington State is expanded to cover out of state trust institutions doing business in Washington. It provides a standard DFI can use to determine whether an out-of-state trust institution regularly engages in trust business, and greater specificity for the requirements for an out-of-state trust institution to conduct trust business in Washington State. DFI is authorized to enter into cooperative agreements with out-of-state regulators and supervisory agreements with out-of-state trust institutions and their regulators. Washington State trust companies must receive approval from DFI to do business in other states.

Enforcement of Trusts. *DFI Examination Requirements and Standard.* Existing examination practices are codified to include the regular examinations of state trust companies, the authority to make cooperative agreements with regulators, and the use of the uniform interagency trust rating system. The director is given rulemaking authority to the extent that it is consistent with the uniform interagency trust rating system, except for emerging business models.

Enforcement. Each trust company that is subject to the authority of DFI must comply with specific statutes, rules, conditions, and directives. Specific procedures for the director to follow in issuing orders and notices, as well as the procedure for a hearing on the notice. The director is also given the authority to apply to the superior court of Washington to enforce final orders. Enforcement actions are expanded to include:

- supervisory directive—a directive in which a state trust company has not given its prior consent;
- non-adjudicative corrective action order—a cease and desist order, consent order, order compelling action, or order of conservatorship; and
- non-adjudicative order of conservatorship—an order specifically authorized for the appointment for a conservatory of a state trust company.

Adjudicative Enforcement. DFI is authorized to impose fines or restitution or both. DFI has a five-year statute of limitations on the commencement of adjudicative proceedings against state trust institutions.

Lifecycle Event Procedures of Trusts. *Standards and Procedures for Voluntary Dissolution and Liquidation and Asset Purchase Agreement.* Procedures for the voluntary dissolution and liquidation of a trust company are provided for both corporations and limited liability corporations. Approval is deemed granted by the director unless otherwise determined within 60 days. While a state trust company is in the process of voluntary liquidation, it is subject to examination by the director and the company must continue to furnish to the director the reports required of a state trust company. Certain unclaimed funds must be transmitted to the director and the funds may be used by the state for the benefit of state financial literacy and education programs. A state trust company may sell all of its assets with a two-thirds vote of its shareholders or upon its board's decision and director approval.

Standards and Procedures for Involuntary Dissolution and Liquidation of a State Trust Company. RCW 30B.44B.020 is repealed, which provides that a state trust company's involuntary dissolution or liquidation is treated like a bank going through similar proceedings. Specific procedures for state trust companies are provided, and the director's powers and required actions in such proceedings provide for judicial review of the director's right to take possession and allow objections by interested persons to claims against the state trust company. Superior court is prohibited from appointing a temporary receiver for a state trust company except in cases of imminent necessity. Superior court is required to notify the director whenever such temporary appointments occur. Any preferential transfer of assets by a state trust company is voided, and such a transfer is criminalized as a class B felony, which is consistent with the banks statutes in Title 30A.

Mergers and Changes in Control. The Director can approve or disapprove the acquisition of a state trust company. The Director must approve the merger of trust companies if one or more of the companies is a state trust company.

Emerging Technologies and Accommodating Business Process Innovation within Trusts. *Compliance with the Bank Secrecy Act.* State trust institutions, their affiliates and their third party providers must comply with the Bank Secrecy Act and associated federal regulations, including safeguarding customer information as required by the Gramm-Leach-Bliley Act.

Third-Party Service Providers. Third-party service providers are defined to include an independent contractor or other person in which a trust institution has engaged to perform services to facilitate the conduct of its business as a trust institution or affiliate, to perform functions such as data storage, Internet related services, data processing services, fiduciary activities, activities related to trading securities, bookkeeping, and data analytics. Rulemaking is authorized to examine standards for third-party servicers. DFI may also issue orders of prohibition against third-party servicers whenever such a provider commits unsafe or unsound practices, or a state trust institution or its affiliate has suffered or is likely to suffer substantial financial loss by reason of a violation or practice by a third-party service provider.

Appropriation: None.

Fiscal Note: Available.

Creates Committee/Commission/Task Force that includes Legislative members: No.

Effective Date: Ninety days after adjournment of session in which bill is passed.

Staff Summary of Public Testimony: PRO: This is the third and final step in trust institution modernization that started in 2014. This bill positions the state of Washington to become an alternative financial services hub that is ready, willing, and able to adapt to new developments in fintech and the globalization of financial markets moving forward. The bill provides a multi-varied approach in oversight by modernizing adjudicative enforcement. The state will now have statutes for how trusts deal with issues like mergers, voluntary liquidations, and involuntary liquidations that are specific to trusts, rather than use the current one size fits all approach that are geared more towards banks. It is now clear what the examination standards are for trust companies. Third-party service provider definitions are necessary because trust companies are becoming more reliant on them, and they need to have some level of oversight.

Persons Testifying: PRO: Senator Mona Das, Prime Sponsor; Roberta Hollinshead, Director, Division of Banks, Department of Financial Institutions.

Persons Signed In To Testify But Not Testifying: No one.

EFFECT OF HOUSE AMENDMENT(S): The Public Records Act is modified to include an exemption for the explanatory letter DFI issues stating the reasons for disapproval of an acquisition of control of a trust company.