

TC11 Scope of Directors' Examinations [Section 11-109-402(2), C.R.S.]

A. Definitions

For the purposes of this Rule, the term "reviewer" shall mean such public accountant or other independent person(s) as determined by the Banking Board.

B. Examination Scope

For the purposes of Section 11-109-402(2), C.R.S., a trust company (institution), at a minimum, shall perform annually the procedures as set forth in Appendix A as the scope of a directors' examination. The recommended procedures are intended to address the high risk areas common to all financial institutions. However, each institution must review its own particular business and determine if additional procedures are required to cover other high risk areas. The reviewer shall be informed of, and permitted access to, all examination reports, administrative orders, and any additional communications between the institution and the Division of Banking, including the Colorado State Banking Board, as well as the appropriate federal regulatory agency. The reviewer shall obtain the institution management's written representation that he or she has been informed of, and granted access to, all such documents prior to completion of the field work.

C. Extent of Testing

Where the procedures set forth in Appendix A require testing or determinations to be made, sampling may be used. Both judgmental and statistical sampling may be acceptable methods of selecting samples to test. Sample sizes should be consistent with generally accepted auditing standards, or as agreed upon by the reviewer and the client institution. In any event, the sampling method and extent of testing, including the sample size(s) used, shall be disclosed in the directors' examination report.

D. Reports to be Filed with the Division of Banking

After the completion of the procedures, or agreed-upon procedures, set forth in Appendix A, the independent reviewer shall evaluate the results of his audit work and promptly prepare and submit a report addressed to the board of directors of the institution. The report shall detail the findings and suggestions resulting from performance of the auditing procedures. Independent reviewers shall include in the report, at a minimum:

1. Financial statements (balance sheet and statement of earnings as of the examination date).
2. The accounts or items on which the procedures were applied.
3. The sampling methods used.
4. The procedures and agreed-upon extent of testing performed.
5. The accounting basis, either generally accepted accounting principles (GAAP) or regulatory required accounting, on which the accounts or items being audited are reported.
6. The reviewer's findings.
7. ~~[Emergency rule expired 07/29/2020]~~[The as of date that the procedures were performed.](#)

[The reviewer shall sign and date the report. The report shall also disclose the reviewer's business address.](#)

[The institution must send a copy of the report, the engagement letter, and any management letter](#)

or similar letter of recommendation to the Division of Banking and, if applicable, to the appropriate federal regulators within thirty (30) days after its receipt, but no later than one hundred fifty (150) days after the date of examination. In addition, each institution shall promptly notify the Division of Banking when a reviewer is engaged to perform a directors' examination and when a change in its reviewer occurs.

E. References

Generally accepted accounting principles are issued by the Financial Accounting Standard Board which is an arm of the Financial Accounting Foundation, an independently chartered institution. Section 23A of the Federal Reserve Act, also known as 12 USC 371c, is a law enacted by the United States Congress and administered by the Board of Governors of the Federal Reserve System. Regulation O of the Board of Governors of the Federal Reserve System, also known as 12 CFR 215, is a regulation enacted by the Federal Reserve Board under the authority granted by the United States Congress and administered by the Board of Governors of the Federal Reserve System. This Rule does not include amendments to or editions of the referenced materials later than the effective date of the Rule, October 24, 1990.

For more detailed information pertaining to this Rule, please contact the secretary to the Colorado State Banking Board at 1560 Broadway, Suite 44975, Denver, CO 80202, 303-894-758475.

APPENDIX A - TC11

For the purpose of Section 11-109-402(2), C.R.S., a trust company (institution), at a minimum, shall have the following procedures performed annually.

A. Securities

1. Review the investment policies and procedures established by the institution's board of directors. Review the board of directors', or investment committee, minutes for evidence that the policies and procedures are periodically reviewed and approved. The policies and procedures should include, but not be limited to:
 - a. Investment objectives, including use of "available for sale," "held for sale" and trading activities;
 - b. Permissible types of investments;
 - c. Diversification guidelines to prevent undue concentration;
 - d. Maturity schedules;
 - e. Limitation on quality ratings;
 - f. Hedging activities and other uses of futures, forwards, options, and other financial instruments;
 - g. Handling exceptions to standard policies;
 - h. Valuation procedures and frequency;
 - i. Limitations on the investment authority of officers; AND
 - j. Frequency of periodic reports to the board of directors on securities holdings.
2. Test the investment procedures and ascertain whether information reported to the board of directors, or investment committee, for securities transactions is in agreement with the supporting data by comparing the following information on such reports to the trade tickets for a sample of items, including futures, forwards, and options:

- a. Descriptions;
 - b. Interest rate;
 - c. Maturity;
 - d. Par value, or number of shares;
 - e. Cost; and
 - f. Market value on date of transaction, if different than cost.
3. Using the same sample items, analyze the securities register for accuracy and confirm the existence of the sample items by examining securities physically held in the institution and confirming the safekeeping of those securities held by others.
 4. Balance investment subledger(s) or reconcile computer-generated trial balances with the general ledger control accounts for each type of security.
 5. Review policies and procedures for controls that are designed to ensure that unauthorized transactions do not occur. Ascertain through reading of policies, procedures, and board of directors' minutes whether investment officers and/or appropriate committee members have been properly authorized to purchase/sell investments and whether there are limitations or restrictions on delegated responsibilities.
 6. Obtain a schedule of the book, par, and market values of securities, as well as the rating classifications. Test the accuracy of the market values of a sample of securities and compare the ratings listed to see that they correspond with those of the rating agencies. Review the institution's documentation on any permanent declines in value that have occurred among the sample of securities to determine that any recorded declines in market value are appropriately computed. Examine the institution's computation of the allowance account for securities, if any, for proper presentation and adequacy.
 7. Test securities income and accrued interest by:
 - a. Determining the institution's method of calculating and recording interest accruals;
 - b. Obtaining trial balances of accrued interest;
 - c. Testing the reconciliation of the trial balances to the general ledger;
 - d. Determining that interest accruals are not made on defaulted issues;
 - e. Selecting items from each type of investment and money market holding:
 - (1) Determining the stated interest rate and most recent interest payment date of coupon instruments by reference to sources of such information that are independent of the institution;
 - (2) Testing timely receipt of interest payments and correctness of entries to applicable general ledger accounts;
 - (3) Calculating accrued interest and comparing it to the trial balance; and
 - (4) Reviewing recorded book value for appropriate accretion of discount and amortization of premium; and
 - f. Performing an analytical review of yields on each type of investment and money market holdings for reasonableness.

8. Review investment accounts for volume of purchases, sales activity and length of time securities have been held. Inquire as to the institution's intent and ability to hold securities until maturity. If there is frequent trading in an investment account, such activity may be inconsistent with the notion that the institution has the intent and ability to hold securities to maturity. Test gains and losses on disposal of investment securities by sampling sales transactions and:
 - a. Determining sales prices by examining invoices or brokers' advices;
 - b. Checking for the use of trade date accounting and the computation of book value on trade date;
 - c. Determining that the general ledger has been properly relieved on the investment, accrued interest, premium, discount and other related accounts;
 - d. Recomputing the gain or loss and compare to the amount recorded in the general ledger; and
 - e. Determining that the sales were approved by the board of directors or a designated committee or were in accordance with policies approved by the board of directors.
9. Determine that sufficient and adequate securities have been collateralized against uninsured deposits, if applicable.

B. Allowance for Fee Receivables

1. Review policies and procedures for ensuring the collectibility of fees due.
2. Test charge-offs and recoveries for proper authorization and/or reporting by reference to the board of directors' minutes.
3. Review the institution's computation of the amount needed in the allowance as of the end of the most recent quarter. Documentation should include consideration of the following matters:
 - a. Aging of delinquent fees;
 - b. Ability to offset fees to account assets;
 - c. Valuation and marketability of assets in fee delinquent accounts;
 - d. Trends in the level of delinquent fees as compared with previous loss and recovery experience;
 - e. Monitoring controls; and
 - f. Collection efforts, both internal and through outside sources.

C. Insider Transactions

NOTE: For purposes of this section of the procedures, insiders include all affiliates of the institution, including its parent holding company, and all subsidiaries of the institution, as those terms are defined in section 23A of the Federal Reserve Act, as well as the institution's executive officers, directors, principal shareholders, and their related interests, as those terms are defined in section 215.2 of Federal Reserve Regulation O.

1. Review the institution's policies and procedures to ensure that extensions of credit to, and other transactions with, insiders are addressed. Ascertain that the policies include

specific guidelines defining fair and reasonable transactions between the institution and insiders, and test insider transactions for compliance with the guidelines and statutory and regulatory requirements. Ascertain that the policies and procedures on extensions of credit comply with the requirements of Federal Reserve Regulation O.

2. Obtain an institution-prepared list of insiders, including any business relationships the institution may have other than as a nominal customer. Also obtain a list of extensions of credit to, and other transactions that the institution, its affiliates, and its subsidiaries have had with, insiders that are outstanding as of the audit date or that have occurred since the prior year's external auditing procedures were performed. Compare the lists to those prepared for the prior year's external auditing program to test for completeness.
3. Review the institution's policies and procedures to ensure that expense accounts of individuals who are executive officers, directors, and principal shareholders are addressed and test a sample of the actual expense account records for compliance with the policies and procedures.

D. Internal Controls - General Accounting and Administrative Controls

1. Review the board of directors' minutes to verify that account reconciliation policies have been established and approved and are reviewed periodically by the board of directors. Determine that management has implemented appropriate procedures to ensure the timely completion of reconciliations of accounting records and the timely resolution of reconciling items.
2. Determine whether the institution's policies regarding segregation of duties and required vacations for employees, including those involved in the EDP function, have been approved by the board of directors and verify that the policies and the implementing procedures established by management are periodically reviewed, are adequate, and are followed.
3. Confirm a sample of deposits in each of the various types of deposit accounts maintained by the institution. Inquire about controls over dormant deposit accounts.
4. Test to determine that reconciliations are prepared for all significant asset and liability accounts, such as "due from" accounts; demand deposits; NOW accounts; money market deposit accounts; other savings deposits; certificates of deposit; and other time deposits and their related accrued interest accounts, if any. Review reconciliations for:
 - a. Timeliness and frequency;
 - b. Accuracy and completeness; and
 - c. Review by appropriate personnel with no conflicting duties.
5. Compare a sample of balances per reconciliations to the general ledger and supporting trial balances.
6. Examine detail and aging of a sample of reconciling items from the accounts whose reconciliations have been tested and reviewed and a sample of items in suspense, clearing, and work-in-process accounts by:
 - a. Testing aging;
 - b. Determining whether items are followed up on and appropriately resolved on a timely basis; and
 - c. Discussing items remaining on reconciliations and in the suspense account with appropriate personnel to ascertain whether any should be written off.

Review a sample of charged-off reconciling and suspense items for proper authorization.

7. Verify through inquiry and observation that the institution maintains adequate records of its off-balance sheet activities. Review the institution's procedures to determine whether probable or reasonably possible losses exist.

E. Internal Controls - Electronic Data Processing Controls

1. Read the board of directors' minutes to determine whether the board of directors has reviewed and approved the institution's electronic data processing (EDP) policies, including those regarding outside servicers, if any, and the in-house use of individual personal computers (PCs) and personalized programs for official institution records, at least annually, confirm that management has established appropriate implementing procedures, and verify the institution's compliance with these policies and procedures.
 - a. The policies and procedures for either in-house processing or use of an outside service center should include:
 - (1) A contingency plan for continuation of operations and recovery when power outages, natural disasters, or other threats could cause disruption and/or major damage to the institution's data processing support, including compatibility of the servicer's plan with that of the institution;
 - (2) Requirements for EDP-related insurance coverage that include the following provisions:
 - (a) Extended blanket bond fidelity coverage to employees of the institution or servicer;
 - (b) Insurance on documents in transit, including cash letters; and
 - (c) Verification of the insurance coverage of the institution or service bureau and the courier service;
 - (3) Review of exception reports and adjusting entries approved by supervisors and/or officers;
 - (4) Controls for input preparation and control and output verification and distribution;
 - (5) "Back-up" of all systems, including off-premises rotation of files and programs;
 - (6) Security to ensure integrity of data and system modifications; and
 - (7) Necessary detail to ensure an audit trail.
 - b. When an outside service center is employed, the policies and procedures should address the following additional items:
 - (1) The requirement for a written contract for each automated application detailing ownership and confidentiality of files and programs, fee structure, termination agreement, and liability for documents in transit;
 - (2) Review of each contract by legal counsel; and
 - (3) Review of each third party review of the service bureau, if any.
2. In the area of general EDP controls, determine through inquiry and observation that

policies and procedures have been established for:

- a. Management and user involvement and approval of new or modified application programs;
 - b. Authorization, approval, and testing of system software modifications;
 - c. The controls surrounding computer operations processing;
 - d. Restricted access to computer operations facilities and resources including:
 - (1) Off-premises storage of master disks and PC disks;
 - (2) Security of the data center and the institution's PCs; and
 - (3) Use and periodic changing of passwords.
3. With respect to EDP applications controls, inquire about and observe:
- a. The controls over:
 - (1) Input submitted for processing;
 - (2) Processing transactions;
 - (3) Output;
 - (4) Applications on PCs; and
 - (5) Telecommunications both between and within institution offices.
 - b. The security over unissued or blank supplies of potentially negotiable items; and
 - c. The control procedures on wire transfers including:
 - (1) Authorizations and agreements with customers, including who may initiate transactions;
 - (2) Limits on transactions; and
 - (3) Call back procedures.

F. Trust Function

1. Supervisory Review
 - a. Determine the significant functions of the department, including areas of responsibility within the department and the financial institution.
 - b. Review the institution's written policies to determine that sufficient guidelines are established to meet fiduciary responsibilities and to comply with applicable laws. Policies should include:
 - (1) Account acceptance;
 - (2) Closed account review;
 - (3) Investments;

- (4) Account review;
 - (5) Discretionary distributions;
 - (6) Conflicts of interest; and
 - (7) Other as needed for scope of fiduciary activities.
 - c. Ascertain the qualifications of the staff and of the board of directors giving consideration to the nature of the fiduciary responsibilities accepted.
 - d. Determine if board policies are implemented and followed.
- 2. Accounting and Physical Controls
 - a. Verify account assets. Include a confirmation from holders of assets retained outside the department.
 - b. Determine that the assets are adequately safeguarded, and held separately from other assets of the institution.
 - c. Verify that a vault record of assets under joint custody is maintained.
 - d. Verify prompt ledger control of assets, including worthless assets, received as original and subsequent deposits of assets, including stock splits and dividends.
 - e. Verify that fiduciary cash accounts are regularly and appropriately reconciled to demand deposit or money market account statements.
 - f. Verify that internal balancing control procedures are performed each time account ledgers are posted.
 - g. Verify that suspense or operating accounts are reconciled at least monthly, contain only appropriate items, and are cleared in a timely manner.
 - h. Reconcile or verify the proper reconciliation of each of the following to the department's general ledger at least quarterly:
 - (1) Income cash;
 - (2) Principal cash;
 - (3) Invested income;
 - (4) Invested principal;
 - (5) Each type of investment, such as stock, bonds, real estate loans and real estate; and
 - (6) Investments by issuer.
 - i. If applicable, verify reconciliations or reconcile outstanding bonds for bond trusteeships, or paying agent activities.
 - j. Verify the accurate payment of dividends.
- 3. Activity Control
 - a. Verify fees paid to the trust company.

- b. Verify proceeds from sales of assets to brokers' invoices, sellers' receipts, or other evidence of sales price.
- c. Verify payment for purchases of assets to brokers' invoices, sellers' receipts, or other evidence of purchase price.
- d. Verify accuracy of amounts and receipt of income from investments.

4. Compliance

- a. Verify that transactions between fiduciary accounts and directors, officers, or employees of the institution, its holding company or other related entities do not constitute self-dealing. In general, self-dealing is considered to exist when the fiduciary uses or obtains the property held in a fiduciary capacity for his or her own benefit.
- b. Review fiduciary account holdings of the following items in light of self-dealing issues:
 - (1) Stock, obligations, repurchase agreements, or deposit accounts with the institution, its affiliates or other related organizations in which there exists such an interest that might affect the best judgment of the institution.
 - (2) Obligations of directors, officers and employees of the institution, its holding company or affiliates or other entities with whom there exists a connection that might affect the exercise of the best judgment of the institution.
- c. Verify that all accounts for which the institution has investment responsibilities are reviewed by the board of directors or a committee thereof.
- d. Verify that cash receipts are promptly invested or distributed.
- e. Verify and review the annual audit of each collective investment fund.

5. Administrative Review

- a. Complete administrative reviews of all major account types, including but not limited to, personal trusts, estates, corporate trusts, collective investment funds, pension trusts and profit sharing trusts. An acceptable administrative review would perform the following practices:
 - (1) Determine that the original or authenticated copy of the governing instrument is on file;
 - (2) Determine that synoptic and history records are current, reliable and comprehensive;
 - (3) Determine that accounts are administered and invested in conformance with management policies, governing instruments, laws, regulations and sound fiduciary principles;
 - (4) Determine that the minutes of the board of directors and committee meetings document the review of trust company activities; significant practices for the board of directors' review include the acceptance of new accounts, the closing of accounts and the review of discretionary payments of principal or income; and
 - (5) Test the accuracy of account statements submitted to beneficiaries.