

Qualifications of an IRS Non-Bank Custodian

Qualification Requirements

No application form exists for an entity to request to become a nonbank trustee or custodian. The prospective trustee or custodian must file a written application with the IRS demonstrating its ability to act as trustee or custodian by complying with the requirements in Treasury Regulation Sections 1.408-2(e)(2) through 1.408-2(e)(8) on an item-by-item basis.

1. State and date of incorporation – showing how long the applicant has been in business.

2. Continuity – the applicant must assure its uninterrupted performance of fiduciary duties notwithstanding the death or change of owners. Diversity of ownership is a key factor in satisfying the continuity requirement. Treasury Regulation Section 1.408-2(e)(2)(i)(B)(1) provides three safe harbors for diversity of ownership.

For **corporate applicants**, the safe harbors are:

- Individuals each of whom owns more than 20% of the voting stock of the corporation own, in the aggregate, no more than 50% of such stock;
- The corporation has issued securities registered or required to be registered under Section 12(b) of the Securities Exchange Act of 1934; or
- The corporation has a parent corporation within the meaning of Internal Revenue Code Section 1563(a)(1) that has issued securities registered or required to be registered under Section 12(b) of the Securities Exchange Act of 1934.

For **partnership applicants**, the safe harbor is:

- Individuals each of whom owns more than 20% of the profits interest in a partnership own, in the aggregate, no more than 50% of such profits interest, and
- Individuals each of whom owns more than 20% of the capital interest in a partnership own, in the aggregate, no more than 50% of such capital interest.

If the applicant doesn't meet one of the corporate or partnership safe harbors, the following criteria are used in a facts and circumstances test:

- Concentration of Ownership
- Non-Owner Management
- Overall Financial Condition
- Substantial Business Operation
- Regulatory Supervision
- Number of Years of Operation, and
- Circumstances Unique to the Applicants

3. Established location – a business location, with a street address, that is accessible during every business day.

4. Fiduciary experience – the applicant must demonstrate that it has fiduciary experience or expertise with retirement plans.

5. Financial responsibility – the applicant must show a high degree of solvency that is demonstrated by a review of the applicant's financial statements focusing on net worth, liquidity and payment of debts as they come due.

6. Capacity to account – the applicant must demonstrate its experience and competence in accounting for a large number of individuals, including calculating and allocating earnings and making distributions to payees.

7. Fitness to handle funds – the applicant must demonstrate its experience and competence with respect to activities normally associated with the handling of retirement funds.

8. Rules of fiduciary conduct – the applicant must have a written document for the rules of conduct to be used in administering retirement plans. Rules of fiduciary conduct must meet the requirements found in Treasury Regulation Sections 1.408-2(e)(5)(i) through (viii). The rules of conduct must require:

- The owners or directors will be responsible for the proper exercise of fiduciary powers;
- A written record will be made of the acceptance or relinquishment of fiduciary accounts;
- If the applicant has the authority to render investment advice, the advisability of holding or selling assets will be determined once a year;
- All employees are adequately bonded;
- Legal counsel is retained and readily available to pass upon fiduciary matters;
- The applicant maintains a separate trust division;
- The applicant values trust assets once in a calendar year and at least every 18 months between valuation;
- No fiduciary accounts will be accepted unless the applicant's net worth is greater than a specified level;
- The applicant will maintain a minimum level of net worth;
- Once every 12 months, a qualified public accountant performs a detailed audit; and
- Fiduciary records are kept separate from all other records of the applicant.

9. Fidelity bond – all employees performing fiduciary duties are adequately bonded and the minimum bond amount must be at least \$250,000.

10. Net worth – the applicant's net worth, based on the most recent audited financial statements, must be at least \$250,000.