

Treasury Regulation 1.408-2

Individual retirement accounts

- (a) *In general.* An individual retirement account must be a trust or a custodial account (see paragraph (d) of this section). It must satisfy the requirements of paragraph (b) of this section in order to qualify as an individual retirement account. It may be established and maintained by an individual, by an employer for the benefit of his employees (see paragraph (c) of this section), or by an employee association for the benefit of its members (see paragraph (c) of this section).
- (b) *Requirements.* An individual retirement account must be a trust created or organized in the United States (as defined in section 7701(a)(9)) for the exclusive benefit of an individual or his beneficiaries. Such trust must be maintained at all times as a domestic trust in the United States. The instrument creating the trust must be in writing and the following requirements must be satisfied.
- (1) *Amount of acceptable contributions.* Except in the case of a contribution to a simplified employee pension described in section 408(k) and a rollover contribution described in section 408(d)(3), 402(a)(5), 402(a)(7), 403(a)(4), 403(b)(8) or 409(b)(3)(C), the trust instrument must provide that contributions may not be accepted by the trustee for the taxable year in excess of \$1,500 on behalf of any individual for whom the trust is maintained. An individual retirement account maintained as a simplified employee pension may provide for the receipt of up to \$7,500 for a calendar year.
- (2) *Trustee.*
- (i) The trustee must be a bank (as defined in section 408(n) and the regulations thereunder) or another person who demonstrates, in the manner described in paragraph (e) of this section, to the satisfaction of the Commissioner, that the manner in which the trust will be administered will be consistent with the requirements of section 408 and this section.
- (ii) Section 11.408(a)(2)–1 of the Temporary Income Tax Regulations under the Employee Retirement Income Security Act of 1974 is superseded by this subparagraph (2).
- (3) *Life insurance contracts.* No part of the trust funds may be invested in life insurance contracts. An individual retirement account may invest in annuity contracts which provide, in the case of death prior to the time distributions commence, for a payment equal to the sum of the premiums paid or, if greater, the cash value of the contract.

(4) *Nonforfeitability.* The interest of any individual on whose behalf the trust is maintained in the balance of his account must be nonforfeitable.

(5) *Prohibition against commingling.*

(i) The assets of the trust must not be commingled with other property except in a common trust fund or common investment fund.

(ii) For purposes of this subparagraph, the term “common investment fund” means a group trust created for the purpose of providing a satisfactory diversification or investments or a reduction of administrative expenses for the individual participating trusts, and which group trust satisfies the requirements of section 408(c) (except that it need not be established by an employer or an association of employees) and the requirements of section 401(a) in the case of a group trust in which one of the individual participating trusts is an employees' trust described in section 401(a) which is exempt from tax under section 501(a).

(iii) For purposes of this subparagraph, the term “individual participating trust” means an employees' trust described in section 401(a) which is exempt from tax under section 501(a) or a trust which satisfies the requirements of section 408(a) provided that in the case of such an employees' trust, such trust would be permitted to participate in such a group trust if all the other individual participating trusts were employees' trusts described in section 401(a) which are exempt from tax under section 501(a).

(6) *Distribution of interest.*

(i) The trust instrument must provide that the entire interest of the individual for whose benefit the trust is maintained must be distributed to him in accordance with paragraph (b)(6)(ii) or (iii) of this section.

(ii) Unless the provisions of paragraph (b)(6)(iii) of this section apply, the entire interest of the individual must be actually distributed to him not later than the close of his taxable year in which he attains age 70½.

(iii) In lieu of distributing the individual's entire interest as provided in paragraph (b)(6)(ii) of this section, the interest may be distributed commencing not later than the taxable year described in such paragraph (b)(6)(ii). In such case, the trust must expressly provide that the entire interest of the individual will be distributed to the individual and the individual's beneficiaries, in a manner which satisfies the requirements of paragraph (b)(6)(v) of this section, over any of the following periods (or any combination thereof)—

- (A) The life of the individual,
 - (B) The lives of the individual and spouse,
 - (C) A period certain not extending beyond the life expectancy of the individual, or
 - (D) A period certain not extending beyond the joint life and last survivor expectancy of the individual and spouse.
- (iv) The life expectancy of the individual or the joint life and last survivor expectancy of the individual and spouse cannot exceed the period computed by use of the expected return multiples in §1.72-9, or, in the case of payments under a contract issued by an insurance company, the period computed by use of the mortality tables of such company.
- (v) If an individual's entire interest is to be distributed over a period described in paragraph (b)(6)(iii) of this section, beginning in the year the individual attains 70½ the amount to be distributed each year must be not less than the lesser of the balance of the individual's entire interest or an amount equal to the quotient obtained by dividing the entire interest of the individual in the trust at the beginning of such year (including amounts not in the individual retirement account at the beginning of the year because they have been withdrawn for the purpose of making a rollover contribution to another individual retirement plan) by the life expectancy of the individual (or the joint life and last survivor expectancy of the individual and spouse (whichever is applicable)), determined in either case as of the date the individual attains age 70 in accordance with paragraph (b)(6)(iv) of this section, reduced by one for each taxable year commencing after the individual's attainment of age 70½. An annuity or endowment contract issued by an insurance company which provides for non-increasing payments over one of the periods described in paragraph (b)(6)(iii) of this section beginning not later than the close of the taxable year in which the individual attains age 70½ satisfies this provision. However, no distribution need be made in any year, or a lesser amount may be distributed, if beginning with the year the individual attains age 70½ the aggregate amounts distributed by the end of any year are at least equal to the aggregate of the minimum amounts required by this subdivision to have been distributed by the end of such year.
- (vi) If an individual's entire interest is distributed in the form of an annuity contract, then the requirements of section 408(a)(6) are satisfied if the distribution of such contract takes place before the close of the taxable year described in subdivision (ii) of this subparagraph, and if the individual's

interest will be paid over a period described in subdivision (iii) of this subparagraph and at a rate which satisfies the requirements of subdivision (v) of this subparagraph.

- (vii) In determining whether paragraph (b)(6)(v) of this section is satisfied, all individual retirement plans maintained for an individual's benefit (except those under which he is a beneficiary described in section 408(a)(7)) at the close of the taxable year in which he reaches age 70½ must be aggregated. Thus, the total payments which such individual receives in any taxable year must be at least equal to the amount he would have been required to receive had all the plans been one plan at the close of the taxable year in which he attained age 70½.

(7) Distribution upon death.

- (i) The trust instrument must provide that if the individual for whose benefit the trust is maintained dies before the entire interest in the trust has been distributed to him, or if distribution has been commenced as provided in paragraph (b)(6) of this section to the surviving spouse and such spouse dies before the entire interest has been distributed to such spouse, the entire interest (or the remaining part of such interest if distribution thereof has commenced) must, within 5 years after the individual's death (or the death of the surviving spouse) be distributed or applied to the purchase of an immediate annuity for this beneficiary or beneficiaries (or the beneficiary or beneficiaries of the surviving spouse) which will be payable for the life of such beneficiary or beneficiaries (or for a term certain not extending beyond the life expectancy of such beneficiary or beneficiaries) and which annuity contract will be immediately distributed to such beneficiary or beneficiaries. A contract described in the preceding sentence is not includible in gross income upon distribution. Section 1.408-4(e) provides rules applicable to the taxation of such contracts. The first sentence of this paragraph (b)(7) shall have no application if distributions over a term certain commenced before the death of the individual for whose benefit the trust was maintained and the term certain is for a period permitted under paragraph (b)(6)(iii) (C) or (D) of this section.
- (ii) Each such beneficiary (or beneficiary of a surviving spouse) may elect to treat the entire interest in the trust (or the remaining part of such interest if distribution thereof has commenced) as an account subject to the distribution requirements of section 408(a)(6) and paragraph (b)(6) of this section instead of those of section 408(a)(7) and paragraph (b)(7) of this section. Such an

election will be deemed to have been made if such beneficiary treats the account in accordance with the requirements of section 408(a)(6) and paragraph (b)(6) of this section. An election will be considered to have been made by such beneficiary if either of the following occurs: (A) any amounts in the account (including any amounts that have been rolled over, in accordance with the requirements of section 408(d)(3)(A)(i), into an individual retirement account, individual retirement annuity, or retirement bond for the benefit of such individual) have not been distributed within the appropriate time period required by section 408(a)(7) and paragraph (b)(7) of this section; or (B) any additional amounts are contributed to the account (or to the account, annuity, or bond to which the beneficiary has rolled such amounts over, as described in (1) above) which are subject, or deemed to be subject, to the distribution requirements of section 408(a)(6) and paragraph (b)(6) of this section.

(8) *Definition of beneficiaries.* The term “beneficiaries” on whose behalf an individual retirement account is established includes (except where the context indicates otherwise) the estate of the individual, dependents of the individual, and any person designated by the individual to share in the benefits of the account after the death of the individual.

(c) *Accounts established by employers and certain association of employees —*

(1) *In general.* A trust created or organized in the United States (as defined in section 7701(a)(9)) by an employer for the exclusive benefit of his employees or their beneficiaries, or by an association of employees for the exclusive benefit of its members or their beneficiaries, is treated as an individual retirement account if the requirements of paragraphs (c)(2) and (c)(3) of this section are satisfied under the written governing instrument creating the trust. A trust described in the preceding sentence is for the exclusive benefit of employees or members even though it may maintain an account for former employees or members and employees who are temporarily on leave.

(2) *General requirements.* The trust must satisfy the requirements of paragraphs (b) (1) through (7) of this section.

(3) *Special requirement.* There must be a separate accounting for the interest of each employee or member.

(4) *Definitions —*

(i) *Separate accounting.* For purposes of paragraph (c)(3) of this section, the term “separate accounting” means that separate records must be maintained with respect to the interest of each individual for whose benefit the trust is

maintained. The assets of the trust may be held in a common trust fund, common investment fund, or common fund for the account of all individuals who have an interest in the trust.

(ii) *Employee association.* For purposes of this paragraph and section 408(c), the term “employee association” means any organization composed of two or more employees, including but not limited to, an employee association described in section 501(c)(4). Such association may include employees within the meaning of section 401(c)(1). There must be, however, some nexus between the employees (e.g., employees of same employer, employees in the same industry, etc.) in order to qualify as an employee association described in this subdivision (ii).

(d) *Custodial accounts.* For purposes of this section and section 408(a), a custodial account is treated as a trust described in section 408(a) if such account satisfies the requirements of section 408(a) except that it is not a trust and if the assets of such account are held by a bank (as defined in section 401(d)(1) and the regulations thereunder) or such other person who satisfies the requirements of paragraph (b)(2)(ii) of this section. For purposes of this chapter, in the case of a custodial account treated as a trust by reason of the preceding sentence, the custodian of such account will be treated as the trustee thereof.

(e)

(1) *In general.* The trustee of a trust described in paragraph (b) of this section may be a person other than a bank if the person demonstrates to the satisfaction of the Commissioner that the manner in which the person will administer trusts will be consistent with the requirements of section 408. The person must demonstrate by written application that the requirements of paragraph (e)(2) to (e)(6) of this section will be met. The written application must be sent to address prescribed by the Commissioner in revenue rulings, notices, and other guidance published in the Internal Revenue Bulletin (see §601.601(d)(2)(ii)(b) of this chapter). For procedural and administrative rules, see paragraph (e)(7) of this section.

(2) *Fiduciary ability.* The applicant must demonstrate in detail its ability to act within the accepted rules of fiduciary conduct. Such demonstration must include the following elements of proof:

(i) *Continuity.*

(A) The applicant must assure the uninterrupted performance of its fiduciary duties notwithstanding the death or change of its owners.

Thus, for example, there must be sufficient diversity in the ownership of

the applicant to ensure that the death or change of its owners will not interrupt the conduct of its business. Therefore, the applicant cannot be an individual.

(B) Sufficient diversity in the ownership of an incorporated applicant is demonstrated in the following circumstances:

- (1) Individuals each of whom owns more than 20 percent of the voting stock in the applicant own, in the aggregate, no more than 50 percent of such stock;
- (2) The applicant has issued securities registered under section 12 (b) of the Securities Exchange Act of 1934 (15 U.S.C. 78l (b)) or required to be registered under section 12(g) (1) of that Act (15 U.S.C. 78l (g)(1)); or
- (3) The applicant has a parent corporation within the meaning of section 1563 (a) (1) that has issued securities registered under section 12 (b) of the Securities Exchange Act of 1934 (15 U.S.C. 78l (b)) or required to be registered under Section 12 (g) (1) of that Act (15 U.S.C. 78l (g)(1)).

(C) Sufficient diversity in the ownership of an applicant that is a partnership means that—

- (1) Individuals each of whom owns more than 20 percent of the profits interest in the partnership own, in the aggregate, no more than 50 percent of such profits interest, and
- (2) Individuals each of whom owns more than 20 percent of the capital interest in the partnership own, in the aggregate, no more than 50 percent of such capital interest.

(D) For purposes of this subdivision, the ownership of stock and of capital and profits interests shall be determined in accordance with the rules for constructive ownership of stock provided in section 1563 (e) and (f) (2). For this purpose, the rules for constructive ownership of stock provided in section 1563(e) and (f) (2) shall apply to a capital or profits interest in a partnership as if it were a stock interest.

(ii) *Established location.* The applicant must have an established place of business in the United States where it is accessible during every business day.

(iii) *Fiduciary experience.* The applicant must have fiduciary experience or expertise sufficient to ensure that it will be able to perform its fiduciary duties. Evidence of fiduciary experience must include proof that a significant part of the business of the applicant consists of exercising fiduciary powers similar to those it will exercise if its application is approved. Evidence of fiduciary

expertise must include proof that the applicant employs personnel experienced in the administration of fiduciary powers similar to those the applicant will exercise if its application is approved.

- (iv) *Fiduciary responsibility.* The applicant must assure compliance with the rules of fiduciary conduct set out in paragraph (e)(5) of this section.
 - (v) *Financial responsibility.* The applicant must exhibit a high degree of solvency commensurate with the obligations imposed by this paragraph. Among the factors to be taken into account are the applicant's net worth, its liquidity, and its ability to pay its debts as they come due.
- (3) *Capacity to account.* The applicant must demonstrate in detail its experience and competence with respect to accounting for the interests of a large number of individuals (including calculating and allocating income earned and paying out distributions to payees). Examples of accounting for the interests of a large number of individuals include accounting for the interests of a large number of shareholders in a regulated investment company and accounting for the interests of a large number of variable annuity contract holders.
- (4) *Fitness to handle funds —*
- (i) *In general.* The applicant must demonstrate in detail its experience and competence with respect to other activities normally associated with the handling of retirement funds.
 - (ii) *Examples.* Examples of activities normally associated with the handling of retirement funds include:
 - (A) To Receive, issue receipts for, and safely keep securities;
 - (B) To collect income;
 - (C) To execute such ownership certificates, to keep such records, make such returns, and render such statements as are required for Federal tax purposes;
 - (D) To give proper notification regarding all collections;
 - (E) To collect matured or called principal and properly report all such collections;
 - (F) To exchange temporary for definitive securities;
 - (G) To give proper notification of calls, subscription rights, defaults in principal or interest, and the formation of protective committees;
 - (H) To buy, sell, receive, or deliver securities on specific directions.
- (5) *Rules of fiduciary conduct.* The applicant must demonstrate that under applicable regulatory requirements, corporate or other governing instruments, or its established operating procedures:

(i) *Administration of fiduciary powers.*

(A)

(1) The owners or directors of the applicant will be responsible for the proper exercise of fiduciary powers by the applicant. Thus, all matters pertinent thereto, including the determination of policies, the investment and disposition of property held in a fiduciary capacity, and the direction and review of the actions of all employees utilized by the applicant in the exercise of its fiduciary powers, will be the responsibility of the owners or directors. In discharging this responsibility, the owners or directors may assign to designated employees, by action duly recorded, the administration of such of the applicant's fiduciary powers as may be proper to assign.

(2) A written record will be made of the acceptance and of the relinquishment or closing out of all fiduciary accounts, and of the assets held for each account.

(3) If the applicant has the authority or the responsibility to render any investment advice with regard to the assets held in or for each fiduciary account, the advisability of retaining or disposing of the assets will be determined at least once during each period of 12 months.

(B) All employees taking part in the performance of the applicant's fiduciary duties will be adequately bonded. Nothing in this subdivision (i)(B) shall require any person to be bonded in contravention of section 412(d) of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1112(d)).

(C) The applicant will employ or retain legal counsel who will be readily available to pass upon fiduciary matters and to advise the applicant.

(D) In order to segregate the performance of its fiduciary duties from other business activities, the applicant will maintain a separate trust division under the immediate supervision of an individual designated for that purpose. The trust division may utilize the personnel and facilities of other divisions of the applicant, and other divisions of the applicant may utilize the personnel and facilities of the trust division, as long as the separate identity of the trust division is preserved.

(ii) *Adequacy of net worth —*

(A) *Initial net worth requirement.* In the case of applications received after January 5, 1995, no initial application will be accepted by the

Commissioner unless the applicant has a net worth of not less than \$250,000 (determined as of the end of the most recent taxable year).

Thereafter, the applicant must satisfy the adequacy of net worth requirements of paragraph (e)(5)(ii)(B) and (C) of this section.

(B) No fiduciary account will be accepted by the applicant unless the applicant's net worth (determined as of the end of the most recent taxable year) exceeds the greater of—

(1) \$100,000, or

(2) Four percent (or, in the case of a passive trustee described in paragraph (e)(6)(i)(A) of this section, two percent) of the value of all of the assets held by the applicant in fiduciary accounts (determined as of the most recent valuation date).

(C) The applicant will take whatever lawful steps are necessary (including the relinquishment of fiduciary accounts) to ensure that its net worth (determined as of the close of each taxable year) exceeds the greater of—

(1) \$50,000, or

(2) Two percent (or, in the case of a passive trustee described in paragraph (e)(6)(i)(A) of this section, one percent) of the value of all of the assets held by the applicant in fiduciary accounts (determined as of the most recent valuation date).

(D) Assets held by members of SIPC —

(1) For purposes of satisfying the adequacy-of-net- worth requirement of this paragraph, a special rule is provided for nonbank trustees that are members of the Securities Investor Protection Corporation (SIPC) created under the Securities Investor Protection Act of 1970 (SIPA)(15 U.S.C. 78aaa et seq., as amended). The amount that the net worth of a nonbank trustee that is a member of SIPC must exceed is reduced by two percent for purposes of paragraph (e)(5)(ii)(B)(2), and one percent for purposes of paragraph (e)(5)(ii)(C)(2), of the value of assets (determined on an account-by-account basis) held for the benefit of customers (as defined in 15 U.S.C. 78fff–2(e)(4)) in fiduciary accounts by the nonbank trustee to the extent of the portion of each account that does not exceed the dollar limit on advances described in 15 U.S.C. 78fff–3(a), as amended, that would apply to the assets in that account in the event of a liquidation proceeding under the SIPA.

(2) The provisions of this special rule for assets held in fiduciary accounts by

members of SIPC are illustrated in the following example.

Example:

- (a) Trustee X is a broker-dealer and is a member of the Securities Investor Protection Corporation. Trustee X also has been approved as a nonbank trustee for individual retirement accounts (IRAs) by the Commissioner but not as a passive nonbank trustee. Trustee X is the trustee for four IRAs. The total assets of each IRA (for which Trustee X is the trustee) as of the most recent valuation date before the last day of Trustee X's taxable year ending in 1995 are as follows: the total assets for IRA-1 is \$3,000,000 (all of which is invested in securities); the value of the total assets for IRA-2 is \$500,000 (\$200,000 of which is cash and \$300,000 of which is invested in securities), the value of the total assets for IRA-3 is \$400,000 (all of which is invested in securities); and the value of the total assets of IRA-4 is \$200,000 (all of which is cash). The value of all assets held in fiduciary accounts, as defined in §1.408-2(e)(6)(viii)(A), is \$4,100,000.
- (b) The dollar limit on advances described in 15 U.S.C. §78fff-3(a) that would apply to the assets in each account in the event of a liquidation proceeding under the Securities Investor Protection Act of 1970 in effect as of the last day of Trustee X's taxable year ending in 1995 is \$500,000 per account (no more than \$100,000 of which is permitted to be cash). Thus, the dollar limit that would apply to IRA-1 is \$500,000; the dollar limit for IRA-2 is \$400,000 (\$100,000 of the cash and the \$300,000 of the value of the securities); the dollar limit for IRA-3 is \$400,000 (the full value of the account because the value of the account is less than \$500,000 and no portion of the account is cash); and the dollar limit for IRA-4 is \$100,000 (the entire account is cash and the dollar limit per account for cash is \$100,000). The aggregate dollar limits of the four IRAs is \$1,400,000.
- (c) For 1996, the amount determined under §1.408-2(e)(5)(ii)(B) is determined as follows for Trustee X: (1) four percent of \$4,100,000 equals \$164,000; (2) two percent of \$1,400,000 equals \$28,000; and (3) \$164,000 minus \$28,000 equals \$136,000. Thus, because \$136,000 exceeds \$100,000, the minimum net worth necessary for

Trustee X to accept new accounts for 1996 is \$136,000.

(d) For 1996, the amount determined under §1.408–2(e)(5)(ii)(C) for Trustee X is determined as follows: (1) two percent of \$4,100,000 equals \$82,000; (2) one percent of \$1,400,000 equals \$14,000; and (3) \$82,000 minus \$14,000 equals \$68,000. Thus, because \$68,000 exceeds \$50,000, the minimum net worth necessary for Trustee X to avoid a mandatory relinquishment of accounts for 1996 is \$68,000.

(E) The applicant will determine the value of the assets held by it in trust at least once in each calendar year and no more than 18 months after the preceding valuation. The assets will be valued at their fair market value, except that the assets of an employee pension benefit plan to which section 103(b)(3)(A) of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1023(b)(3)(A)) applies will be considered to have the value stated in the most recent annual report of the plan.

(iii) *Audits.*

(A) At least once during each period of 12 months, the applicant will cause detailed audits of the fiduciary books and records to be made by a qualified public accountant. At that time, the applicant will ascertain whether the fiduciary accounts have been administered in accordance with law, this paragraph, and sound fiduciary principles. The audits shall be conducted in accordance with generally accepted auditing standards, and shall involve whatever tests of the fiduciary books and records of the applicant are considered necessary by the qualified public accountant.

(B) In the case of an applicant which is regulated, supervised, and subject to periodic examination by a State or Federal agency, such applicant may adopt an adequate continuous audit system in lieu of the periodic audits required by paragraph (e)(5)(iii)(A) of this section.

(C) A report of the audits and examinations required under this subdivision, together with the action taken thereon, will be noted in the fiduciary records of the applicant.

(iv) *Funds awaiting investment or distribution.* Funds held in a fiduciary capacity by the applicant awaiting investment or distribution will not be held uninvested or undistributed any longer than is reasonable for the proper management of the account.

(v) *Custody of investments.*

(A) Except for investments pooled in a common investment fund in

accordance with the provisions of paragraph (e)(5)(vi) of this section and for investments of accounts established under section 408(q) on or after August 1, 2003, the investments of each account will not be commingled with any other property.

(B) Assets of accounts requiring safekeeping will be deposited in an adequate vault. A permanent record will be kept of assets deposited in or withdrawn from the vault.

(vi) *Common investment funds.* The assets of an account may be pooled in a common investment fund (as defined in paragraph (e)(5)(viii)(C) of this section) if the applicant is authorized under applicable law to administer a common investment fund and if pooling the assets in a common investment fund is not in contravention of the plan documents or applicable law. The common investment fund must be administered as follows:

(A) Each common investment fund must be established and maintained in accordance with a written agreement, containing appropriate provisions as to the manner in which the fund is to be operated, including provisions relating to the investment powers and a general statement of the investment policy of the applicant with respect to the fund; the allocation of income, profits and losses; the terms and conditions governing the admission or withdrawal of participations in the funds; the auditing of accounts of the applicant with respect to the fund; the basis and method of valuing assets held by the fund, setting forth specific criteria for each type of asset; the minimum frequency for valuation of assets of the fund; the period following each such valuation date during which the valuation may be made (which period in usual circumstances may not exceed 10 business days); the basis upon which the fund may be terminated; and such other matters as may be necessary to define clearly the rights of participants in the fund. A copy of the agreement must be available at the principal office of the applicant for inspection during all business hours, and upon request a copy of the agreement must be furnished to the employer, the plan administrator, any participant or beneficiary of an account, or the individual for whose benefit the account is established or that individual's beneficiary.

(B) All participations in the common investment fund must be on the basis of a proportionate interest in all of the investments.

(C) Not less frequently than once during each period of 3 months the applicant must determine the value of the assets in the fund as of the date set for the

valuation of assets. No participation may be admitted to or withdrawn from the fund except (1) on the basis of such valuation and (2) as of such valuation date. No participation may be admitted to or withdrawn from the fund unless a written request for or notice of intention of taking such action has been entered on or before the valuation date in the fiduciary records of the applicant. No request or notice may be canceled or countermanded after the valuation date.

(D)

- (1) The applicant must at least once during each period of 12 months cause an adequate audit to be made of the common investment fund by a qualified public accountant.
- (2) The applicant must at least once during each period of 12 months prepare a financial report of the fund which, based upon the above audit, must contain a list of investments in the fund showing the cost and current value of each investment; a statement for the period since the previous report showing purchases, with cost; sales, with profit or loss; any other investment changes; income and disbursements; and an appropriate notation as to any investments in default.
- (3) The applicant must transmit and certify the accuracy of the financial report to the administrator of each plan participating in the common investment fund within 120 days after the end of the plan year.

(E) When participations are withdrawn from a common investment fund, distributions may be made in cash or ratably in kind, or partly in cash and partly in kind: *Provided*, That all distributions as of any one valuation date must be made on the same basis.

(F) If for any reason an investment is withdrawn in kind from a common investment fund for the benefit of all participants in the fund at the time of such withdrawal and such investment is not distributed ratably in kind, it must be segregated and administered or realized upon for the benefit ratably of all participants in the common investment fund at the time of withdrawal.

(vii) *Books and records.*

(A) The applicant must keep its fiduciary records separate and distinct from other records. All fiduciary records must be so kept and retained for as long as the contents thereof may become material in the administration of any internal revenue law. The fiduciary records must contain full

information relative to each account.

(B) The applicant must keep an adequate record of all pending litigation to which it is a party in connection with the exercise of fiduciary powers.

(viii) *Definitions.* For purposes of this paragraph (e)(5), and paragraph (e)(2)(v), and paragraph (e)(7) of this section—

(A) The term “account” or “fiduciary account” means a trust described in section 401(a) (including a custodial account described in section 401(f)), a custodial account described in section 403(b)(7), or an individual retirement account described in section 408(a) (including a custodial account described in section 408(h)).

(B) The term “plan administrator” means an administrator as defined in §1.414(g)–1.

(C) The term “common investment fund” means a trust that satisfies the following requirements:

(1) The trust consists of all or part of the assets of several accounts that have been established with the applicant, and

(2) The trust is described in section 401(a) and is exempt from tax under section 501(a), or is a trust that is created for the purpose of providing a satisfactory diversification of investments or a reduction of administrative expenses for the participating accounts and that satisfies the requirements of section 408(c).

(D) The term “fiduciary records” means all matters which are written, transcribed, recorded, received or otherwise come into the possession of the applicant and are necessary to preserve information concerning the acts and events relevant to the fiduciary activities of the applicant.

(E) The term “qualified public accountant” means a qualified public accountant, as defined in section 103(a)(3)(D) of the Employee Retirement Income Security Act of 1974, 29 U.S.C. 1023(a)(3)(D), who is independent of the applicant.

(F) The term “net worth” means the amount of the applicant's assets less the amount of its liabilities, as determined in accordance with generally accepted accounting principles.

(6) *Special rules* —

(i) *Passive trustee.*

(A) An applicant that undertakes to act only as a passive trustee may be relieved of one or more of the requirements of this paragraph upon clear

and convincing proof that such requirements are not germane, under all the facts and circumstances, to the manner in which the applicant will administer any trust. A trustee is a passive trustee only if under the written trust instrument the trustee has no discretion to direct the investment of the trust funds or any other aspect of the business administration of the trust, but is merely authorized to acquire and hold particular investments specified by the trust instrument. Thus, for example, in the case of an applicant that undertakes merely to acquire and hold the stock of regulated investment companies, the requirements of paragraph (e)(5)(i)(A)(3) in its place, and (i)(D), and (vi) of this section shall not apply and no negative inference shall be drawn from the applicant's failure to demonstrate its experience of competence with respect to the activities described in paragraph (e)(4)(ii)(E) to (H) of this section.

(B) The notice of approval issued to an applicant that is approved by reason of this subdivision shall state that the applicant is authorized to act only as a passive trustee.

(ii) *Federal or State regulation.* Evidence that an applicant is subject to Federal or State regulation with respect to one or more relevant factors shall be given weight in proportion to the extent that such regulatory standards are consonant with the requirements of section 401. Such evidence may be submitted in addition to, or in lieu of, the specific proofs required by this paragraph.

(iii) *Savings account.*

(A) An applicant will be approved to act as trustee under this subdivision if the following requirements are satisfied:

- (1) The applicant is a credit union, industrial loan company, or other financial institution designated by the Commissioner;
- (2) The investment of the trust assets will be solely in deposits in the applicant;
- (3) Deposits in the applicant are insured (up to the dollar limit prescribed by applicable law) by an agency or instrumentality of the United States, or by an organization established under a special statute the business of which is limited to insuring deposits in financial institutions and providing related services.

(B) Any applicant that satisfies the requirements of this subdivision is hereby approved, and (notwithstanding subparagraph (2) of this paragraph) is not

required to submit a written application. This approval takes effect on the first day after December 22, 1976, on which the applicant satisfies the requirements of this subdivision, and continues in effect for so long as the applicant continues to satisfy those requirements.

(C) If deposits are insured, but not in the manner provided in paragraph (e)(6)(iii)(A)(3) of this section, the applicant must submit an application. The application, notwithstanding subparagraph (2) of this paragraph, will be limited to a complete description of the insurance of applicant's deposits. The applicant will be approved if the Commissioner approves of the applicant's insurance.

(iv) *Notification of Commissioner.* The applicant must notify the Commissioner in writing of any change that affects the continuing accuracy of any representation made in the application required by this paragraph, whether the change occurs before or after the applicant receives a notice of approval. The notification must be addressed to address prescribed by the Commissioner in revenue rulings, notices, and other guidance published in the Internal Revenue Bulletin (see §601.601(d)(2)(ii)(b) of this chapter.

(v) *Substitution of trustee.* No applicant will be approved unless the applicant undertakes to act as trustee only under trust instruments which contain a provision to the effect that the grantor is to substitute another trustee upon notification by the Commissioner that such substitution is required because the applicant has failed to comply with the requirements of this paragraph or is not keeping such records, or making such returns, or rendering such statements as are required by forms or regulations.

(7) *Procedure and administration —*

(i) *Notice of approval.* If the applicant is approved, a written notice of approval will be issued to the applicant. The notice of approval will state the day on which it becomes effective, and (except as otherwise provided therein) will remain effective until revoked. This paragraph does not authorize the applicant to accept any fiduciary account before such notice of approval becomes effective.

(ii) *Notice of disapproval.* If the applicant is not approved, a written notice will be furnished to the applicant containing a statement of the reasons why the applicant has not been approved.

(iii) *Copy to be furnished.* The applicant must not accept a fiduciary account until after the plan administrator or the person for whose benefit the account is to be established is furnished with a copy of the written notice of approval issued to

the applicant. This provision is effective six months after April 20, 1979 for new accounts accepted thereafter. For accounts accepted before that date, the administrator must be notified before the later of the effective date of this provision or six months after acceptance of the account.

- (iv) *Grounds for revocation.* The notice of approval issued to an applicant will be revoked if the Commissioner determines that the applicant is unwilling or unable to administer fiduciary accounts in a manner consistent with the requirements of this paragraph. Generally, the notice will not be revoked unless the Commissioner determines that the applicant has knowingly, willfully, or repeatedly failed to administer fiduciary accounts in a manner consistent with the requirements of this paragraph, or has administered a fiduciary account in a grossly negligent manner.
- (v) *Procedures for revocation.* The notice of approval issued to an applicant may be revoked in accordance with the following procedures:
 - (A) If the Commissioner proposes to revoke the notice of approval issued to an applicant, the Commissioner will advise the applicant in writing of the proposed revocation and of the reasons therefor.
 - (B) Within 60 days after the receipt of such written advice, the applicant may protest the proposed revocation by submitting a written statement of facts, law, and arguments opposing such revocation to address prescribed by the Commissioner in revenue rulings, notices, and other guidance published in the Internal Revenue Bulletin (see §601.601(d)(2)(ii)(b) of this chapter. In addition, the applicant may request a conference in the National Office.
 - (C) If the applicant consents to the proposed revocation, either before or after a National Office conference, or if the applicant fails to file a timely protest, the Commissioner will revoke the notice of approval that was issued to the applicant.
 - (D) If, after considering the applicant's protest and any information developed in conference, the Commissioner determines that the applicant is unwilling or unable to administer fiduciary accounts in a manner consistent with the requirements of this paragraph, the Commissioner will revoke the notice of approval that was issued to the applicant and will furnish the applicant with a written statement of findings on which the revocation is based.
 - (E) If at any time the Commissioner determines that immediate action is necessary to protect the interest of the Internal Revenue Service or of

any fiduciary account, the notice of approval issued to the applicant will be suspended at once, pending a final decision to be based on the applicant's protest and any information developed in conference.

(8) *Special rules for governmental units* —

- (i) *In general.* A governmental unit that seeks to qualify as a nonbank trustee of a deemed IRA that is part of its qualified employer plan must demonstrate to the satisfaction of the Commissioner that it is able to administer the trust in a manner that is consistent with the requirements of section 408. The demonstration must be made by written application to the Commissioner. Notwithstanding the requirement of paragraph (e)(1) of this section that a person must demonstrate by written application that the requirements of paragraphs (e)(2) through (e)(6) of this section will be met in order to qualify as a nonbank trustee, a governmental unit that maintains a plan qualified under section 401(a), 403(a), 403(b) or 457 need not demonstrate that all of these requirements will be met with respect to any individual retirement accounts maintained by that governmental unit pursuant to section 408(q). For example, a governmental unit need not demonstrate that it satisfies the net worth requirements of paragraph (e)(3)(ii) of this section if it demonstrates instead that it possesses taxing authority under applicable law. The Commissioner, in his discretion, may exempt a governmental unit from certain other requirements upon a showing that the governmental unit is able to administer the deemed IRAs in the best interest of the participants. Moreover, in determining whether a governmental unit satisfies the other requirements of paragraphs (e)(2) through (e)(6) of this section, the Commissioner may apply the requirements in a manner that is consistent with the applicant's status as a governmental unit.
- (ii) *Governmental unit.* For purposes of this special rule, the term *governmental unit* means a state, political subdivision of a state, and any agency or instrumentality of a state or political subdivision of a state.
- (iii) *Additional rules.* The Commissioner may in revenue rulings, notices, or other guidance of general applicability provide additional rules for governmental units seeking approval as nonbank trustees.
- (iv) *Effective/applicability date.* This section is applicable for written applications made on or after June 18, 2007. The rules in this section also may be relied on for applications submitted on or after August 1, 2003 (or such earlier application as the Commissioner deems appropriate) and before June 18, 2007.

[T.D. 7714, 45 FR 52791, Aug. 8, 1980, as amended by T.D. 8635, 60 FR 65549, Dec. 20, 1995; 61 FR 11307, Mar. 20, 1996; T.D. 9142, 69 FR 43739, July 22, 2004; T.D. 9331, 72 FR 33388, June 18, 2007]