a national bank has investment discretion, and each year thereafter, the bank promptly must conduct an individual account review of the account's assets to evaluate whether they are appropriate, individually and collectively, for the account. In addition to the individual account review, a bank must conduct an annual review of assets by issuer to determine the investment merit of the assets (or potential assets) in fiduciary accounts for which the bank has investment discretion, to the extent appropriate for that asset. The OCC anticipates that the scope of a bank's assets review will vary, depending on the nature of the particular asset.

To contrast the two types of review, a review of assets by issuer determines what investments, by issuer, (*e.g.*, common stock of Corporation X) are potentially appropriate investments for the bank's fiduciary accounts. In some banks, for example, the review of assets by issuer results in a list of permissible fiduciary investments for the bank's fiduciary accounts. The person or committee in charge of investing for a particular fiduciary account chooses investments from this list. An individual account review, on the other hand, determines whether the investments chosen for that particular account are appropriate, individually and collectively, given the objectives of the account.

The OCC invites comment on whether these specific standards are necessary or appropriate and, if not, what alternative approaches are preferable. For example, commenters may wish to discuss approaches that distinguish between large and small accounts or between large and small institutions.

Recordkeeping (Proposed § 9.8)

The proposal clarifies the recordkeeping requirements currently found at §§ 9.7(a)(2) and 9.8. In particular, a national bank must document the establishment and termination of fiduciary accounts, must maintain adequate records for fiduciary accounts, must retain records for a specified period of time, and must make sure its fiduciary records are distinguishable from other bank records.

Audit of Fiduciary Activities (Proposed § 9.9)

The proposal retains the current § 9.9 requirement that a national bank perform suitable audits of its fiduciary activities annually (specifically, at least once during each calendar year and not later than 15 months after the last audit), and that the bank report the results of the audit (including all actions taken as a result of the audit) in the minutes of the board. The proposal removes as redundant the requirement that the national bank ascertain compliance with ''law, this part, and sound fiduciary principles.''

The proposal clarifies that if a bank adopts a continuous audit system in lieu of performing annual audits, the bank may perform discrete audits of each fiduciary activity, on an activity-by-activity basis, at intervals appropriate for that activity. For example, a bank may determine that it is appropriate to audit certain low-risk fiduciary activities every 18 months. A bank that adopts a continuous audit system must report the results of any discrete audits performed since the last audit report (including all actions taken as a result of the audits) in the minutes of the board of directors at least once during each calendar year and not later than 15 months after the last audit report.

The proposal also clarifies that a national bank's audit committee may not include directors who are members of a fiduciary committee of the bank.[10] The proposal also modifies the current regulation's position that active officers of the bank may not serve on the audit committee. Under the proposal, only officers who participate significantly in the administration of the bank's fiduciary activities are barred from serving on the audit committee. This proposed position provides some degree of flexibility to smaller banks, which may have a limited number of outside directors.

Finally, the proposal permits an audit committee of an affiliate of the bank to conduct the required audit. This change allows a bank holding company to audit the fiduciary activities of its subsidiary national banks through a central audit committee. This approach facilitates consolidation of functions, and the accompanying efficiencies, within a bank holding company structure.

The OCC invites comment on these proposed changes and, in addition, on the relationship between the audit requirement and the OCC's fiduciary examination process (in particular, the extent to which OCC examiners should rely on a bank's internal or external fiduciary audits).

Fiduciary Funds Awaiting Investment or Distribution (Proposed § 9.10)

As mentioned earlier, the proposal relocates to proposed § 9.5 the current regulation's requirement that a national bank adopt policies and procedures regarding short-term investments. The proposal retains the current regulation's general prohibition against allowing fiduciary funds to remain uninvested and undistributed any longer than reasonable for proper account management. The OCC invites comment on whether reasonableness is a sufficiently clear standard and, if not, on what standard is appropriate.

The proposal continues to allow a national bank to deposit idle fiduciary funds (i.e., fiduciary funds awaiting investment or distribution) in its commercial, savings, or another department, provided that the bank secures the deposit with appropriate collateral. Additionally, the proposal explicitly allows a national bank to use, as collateral for self- deposits of idle fiduciary funds, assets (including surety bonds) that qualify under state law as appropriate security for deposits of fiduciary funds. The proposal also permits a national bank to deposit idle fiduciary funds with affiliates.

Surety bonds as collateral. Under 12 U.S.C. 92a(d), a national bank may deposit idle fiduciary funds with itself (*e.g.*, in its commercial or savings department) only if it pledges United States bonds or ''other securities'' approved by the OCC. Current § 9.10(b)(3) allows a bank to meet this requirement by pledging qualifying assets of the bank to secure a deposit in compliance with local law.

Under the OCC's interpretation of § 9.10(b)(3), a national bank may pledge, as a qualifying asset, a surety bond as collateral for a deposit of idle fiduciary funds if a surety bond is permissible collateral under state law, unless the instrument governing the fiduciary relationship prohibits the use of a surety bond. This interpretation recognizes that a surety bond provides protection that is functionally at least equivalent to the protection provided by other types of assets that the OCC has approved under section 92a(d). Moreover, this interpretation promotes Congress' policy objective of protecting the interests of beneficiaries and ensures that national banks are not disadvantaged in a state that permits its institutions to use surety bonds to secure deposits of idle fiduciary funds.

The proposal explicitly incorporates this interpretation into part 9 by allowing a national bank to secure deposits of idle fiduciary funds with assets, including surety bonds, that qualify under state law as appropriate security for deposits of fiduciary funds. The theory that a surety bond is comparable to other forms of security permitted by the OCC could have a broader application, however. In particular, the OCC invites comment on

[10] See Fiduciary Precedent 9.2505 (a member of a fiduciary committee may not serve on the trust audit committee).