

FEDERAL RESERVE BANK
OF NEW YORK

[Circular No. 8720]
January 8, 1980

UNIFORM RULES FOR BANK RECORDKEEPING AND PROCEDURES
REGARDING SECURITIES TRANSACTIONS
Amendments to Regulation H

To All State Member Banks in the Second
Federal Reserve District, and Others Concerned:

The Board of Governors of the Federal Reserve System has amended its rules, effective January 1, 1980, for bank recordkeeping, confirmation, and other procedures in making securities transactions for trust departments and other bank customers. The amendments, originally adopted in July 1979, have been modified with regard to transactions in U.S. government securities, as indicated in the following excerpt from the Board's announcement:

The Board's revised Regulation H, effective January 1, 1980, includes the following provisions (with revisions indicated by italics):

Recordkeeping:

The following records of securities transactions must be kept by banks for three years, in a manner forming an adequate record for audit:

Itemized daily records of purchases and sales; account records for customers and a separate record of each order to purchase or sell securities.

Alternative confirmation requirements:

—Where the bank uses a broker the bank may send customers the bank's confirmation, or a copy of the broker's confirmation, within five days from the time the bank executes the transaction or receives confirmation from the broker. Confirmation may not be required in certain cases where the customer and the bank agree to a different arrangement.

—Where the bank exercises investment discretion as agent for the customer, the bank must provide quarterly reports to the customer. In such cases the bank must identify separately its fees in transactions in government securities for customers. Dealer mark-ups need not be disclosed.

Policies and procedures:

Banks making securities transactions for customers must establish written policies and procedures, including:

—Policies and procedures relating to supervision of officers and employees, the equitable allocation of securities and equitable matching of buy and sell orders.

—Requirements for bank employees involved in securities transactions for customers to report their own securities transactions quarterly, *with the exception of their transactions in U.S. government securities.*

Exemptions:

A bank that is in compliance with the rules of the Municipal Securities Rulemaking Board with respect to transactions in municipal securities is deemed to be in compliance with the Board's recordkeeping and confirmation requirements. In addition, the Board's rules:

—Exempt the securities activities of foreign branches of banks, and

—Exempt banks that normally make 200 or fewer securities transactions a year for customers, *not counting transactions in U.S. government securities*, from certain recordkeeping requirements.

The Federal Deposit Insurance Corporation and the Comptroller of the Currency are considering similar revisions.

Enclosed is a copy of the changes in the January 1, 1980 amendments to Regulation H. Questions on this matter should be directed to our Consumer Affairs and Bank Regulations Department (Tel. No. 212-791-5914).

THOMAS M. TIMLEN,
First Vice President.

Board of Governors of the Federal Reserve System

MEMBERSHIP OF STATE BANKING INSTITUTIONS

IN THE FEDERAL RESERVE SYSTEM

CHANGES IN AMENDMENTS TO REGULATION H

(effective January 1, 1980)

FEDERAL RESERVE SYSTEM

12 CFR Part 208

[Docket No. R-0142; Reg. H]

Membership of State Banking Institutions in the Federal Reserve System; Recordkeeping and Confirmation Requirements for Certain Securities Transactions Effected by State Member Banks

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Final rule.

SUMMARY: On June 20, 1979, the Board of Governors of the Federal Reserve System adopted amendments to its Regulation H (12 CFR 208) to require that State member banks that effect certain securities transactions for customers provide confirmation of and maintain records with respect to such transactions. Similar regulations have been adopted by the Comptroller of the Currency and the Federal Deposit Insurance Corporation. The three banking regulatory agencies have also requested public comment on the confirmation requirements as they apply to transactions in U.S. government, federal agency and municipal securities and on the bank officers and employees reporting requirements as they apply to transactions in U.S. government or federal agency obligations. The comment period expired September 24, 1979; ten letters of comment were received. The Board has considered the comments and has amended its regulation in certain respects as set forth below.

EFFECTIVE DATE: January 1, 1980.

FOR FURTHER INFORMATION CONTACT: Robert A. Wallgren, Chief, Trust Activities Program, (202) 452-2717, or Walter R. McEwen, Attorney, (202) 452-2521, Division of Banking Supervision

and Regulation, Board of Governors of the Federal Reserve System, Washington, D.C. 20551.

SUPPLEMENTARY INFORMATION: The final rule as adopted today is substantially similar to that adopted on June 20, 1979. Although comment was solicited only with respect to the confirmation requirements as they apply to transactions in U.S. government, federal agency and municipal securities and on the bank officers and employees reporting requirements as they apply to transactions in U.S. government or federal agency obligations, several commenters commented on sections of the regulation which had been adopted previously in final form. The Board found some of the comments to have merit and the Board has amended certain previously adopted sections in response to these comments. The following is a summary of the revisions which were made.

In response to a comment, subparagraph (k)(4)(iii) has been modified to state that a bank may charge accounts over which the bank exercises investment discretion in an agency capacity for confirmations made on a per transaction basis. This change merely reflects the Board's prior intent that banks could charge for furnishing individual confirmations in agency accounts where the bank exercises investment discretion.

One commenter stated its understanding that the intent of the banking agencies in drafting (k)(4)(i) was to permit a bank and a customer of a nondiscretionary agency account to agree on a suitable alternative reporting system. The commenter noted that the placement of this authority under the "Time of Notification" section, (k)(4), might be interpreted as a grant of authority for customer and bank to agree to a different time of notification, but not to a different form of

notification. This was not the Board's intent when adopting the regulation; however, the Board has determined that it does not object to a different form of notification. Accordingly, subparagraph (k)(4)(i) has been amended to clarify that a bank and its agency customers may mutually agree upon alternative forms of notification. The Board advises State member banks that any such alternative form of notification for non-discretionary agency accounts must be affirmatively approved by the customer. A State member bank will not be considered to be in compliance with this paragraph (k) if it interprets a customer's non-response to a bank communication as constituting customer approval.

Several commenters suggested changes to various parts of subparagraph (k)(5)(iv). Securities Trading Policies and Procedures. Many commenters suggested that bank officers and employees who purchase U.S. government and federal agency securities should not have to report transactions in those securities. One commenter noted that "Since the purpose of the disclosure is to detect misuse of inside information and manipulation of the market, and since such activity seems particularly unlikely in the marketplace for government securities, we feel that these securities should be excepted from the disclosure requirements." The Board has concluded that the benefit that would result from requiring disclosure of transactions in U.S. government and federal agency securities is outweighed by the increased reporting burden. The rule as adopted will exempt transactions in U.S. government and federal agency securities from the reporting requirements applicable to bank officers and employees, and will also exempt bank officers and employees whose duties do not involve knowledge of or

For this Regulation to be complete, retain:

- 1) Regulation H pamphlet, as amended effective March 18, 1969.
2) Amendments effective December 21, 1973; March 2, 1974; September 16, 1974; December 1, 1975; October 3, 1977; October 31, 1977; December 31, 1977; April 20, 1978; and January 1, 1980.
3) This slip sheet.

transactions in securities other than U.S. government and federal agency obligations.

The comment letters pointed out the importance of transactions in U.S. government and federal agency securities in determining the scope of the 200 securities transactions exemption of subparagraph (k)(6) which exempts banks effecting fewer than 200 securities transactions per year from some of the recordkeeping requirements. One commenter noted that the effect of the 200 securities transactions exemption has been rendered less generous now that transactions in U.S. government and federal agency securities are subject to the confirmation requirements. The Board has concluded that the intended purpose of the 200 securities transactions exemption can best be accomplished by excluding transactions in U.S. government and federal agency securities from the securities transactions which are to be counted for purposes of the 200 securities transactions exemption. A related comment noted that the requirements of subparagraphs (k)(5)(i) through (k)(5)(iii), which require written supervisory policies and procedures relating to supervision of officers and employees, fair and equitable allocation of securities and fair and equitable crossing of orders could be triggered by performance of a single customer accommodation transaction. The 200 securities transactions exemption set forth in subparagraph (k)(6)(i) has now been modified to exempt banks coming within the exemption from the policy and procedures requirements of subparagraphs (k)(5)(i) through (k)(5)(iii).

The Board received a few adverse comments concerning the burden imposed by extension of the confirmation requirements to transactions in U.S. government and federal agency securities. After due consideration of these comments, the Board has determined that application of the confirmation requirements to transactions in U.S. government and federal agency securities is appropriate in the public interest. Accordingly, no change has been made in these requirements as adopted previously.

Finally, the question has been raised regarding the applicability of this paragraph (k) to employee benefit accounts for which a State member bank acts as Investment Manager, as defined in section 3(38) of the Employee Retirement Income Security Act of 1974, with another entity acting as trustee and/or custodian of the assets. The Investment Manager concept permits one bank to be sole trustee of a pension plan ("Master Trustee"), rendering to the plan sponsor uniform accounting

reports including cash statements and valuation statements, while accepting investment direction as to specified parts of the pension plan assets from Investment Managers (another bank, an insurance company, or a registered investment advisor). In the case of a Master Trustee, the Board has determined that the requirements of this paragraph will be served if either the Master Trustee or the Investment Manager maintains the specified records and gives prescribed statements and confirmations in accordance with the requirements of the regulation. Any State member bank serving either as Master Trustee or Investment Manager should insure that the requirements of the regulation are being met, either through performing the functions required by the regulation itself or contracting with another party that that party should do so.

Pursuant to sections 9 and 11 of the Federal Reserve Act (12 U.S.C. 321, 248 (a) and (1) and 3(b)(1) *et seq.*), the Board amends Regulation H (12 CFR 208) by amending paragraph (k) to § 208.8 as set forth below:

PART 208—MEMBERSHIP OF STATE BANKING INSTITUTIONS IN THE FEDERAL RESERVE SYSTEM

§ 208.8 Banking practices.

Recordkeeping and confirmation of certain securities transactions effected by State member banks.

(4) *Time of Notification:* The time for mailing or otherwise furnishing the written notification described in paragraph (k)(3) of this section shall be 5 business days from the date of the transaction, or if a broker/dealer is utilized, within 5 business days from the receipt by the bank of the broker/dealer's confirmation, but the bank may elect to use the following alternative procedures if the transaction is effected for:

(i) Accounts (except periodic plans) where the bank does not exercise investment discretion and the bank and the customer agree in writing to a different arrangement as to the time and content of the notification; provided, however, that such agreement makes clear the customer's right to receive the written notification within the above prescribed time period at no additional cost to the customer;

(iii) Accounts, where the bank exercises investment discretion in an agency capacity, in which instance (A) the bank shall mail or otherwise furnish to each customer not less frequently than once every three months an itemized statement which shall specify the funds and securities in the custody

or possession of the bank at the end of such period and all debits, credits and transactions in the customer's accounts during such period, and (B) if requested by the customer, the bank shall mail or otherwise furnish to each such customer within a reasonable time the written notification described in paragraph (k)(3) of this section. The bank may charge a reasonable fee for providing the information described in paragraph (k)(3) of this section.

(5) *Securities Trading Policies and Procedures:* Every State member bank effecting securities transactions for customers shall establish written policies and procedures providing:

(iv) that bank officers and employees who make investment recommendations or decisions for the accounts of customers, who participate in the determination of such recommendations or decisions, or who, in connection with their duties, obtain information concerning which securities are being purchased or sold or recommended for such action, must report to the bank, within ten days after the end of the calendar quarter, all transactions in securities made by them or on their behalf, either at the bank or elsewhere in which they have a beneficial interest. The report shall identify the securities purchased or sold and indicate the dates of the transactions and whether the transactions were purchases or sales. Excluded from this requirement are transactions for the benefit of the officer or employee over which the officer or employee has no direct or indirect influence or control, transactions in mutual fund shares, and all transactions involving in the aggregate \$10,000 or less during the calendar quarter. For purposes of this paragraph (k)(iv) of this section, the term "securities" does not include U.S. government or federal agency obligations.

(6) *Exceptions:* The following exceptions to subparagraph (k) shall apply:

(i) The requirements of paragraph (k)(2)(ii) through (k)(2)(iv) and paragraph (k)(5)(i) through (k)(5)(iii) of this section shall not apply to banks having an average of less than 200 securities transactions per year for customers over the prior three calendar year period, exclusive of transactions in U.S. government and federal agency obligations;

Board of Governors of the Federal Reserve System, December 19, 1979.

Theodore E. Allison,
Secretary of the Board.

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