

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 (g)(4), the term securities does not include government securities.

By order of the Board of Governors of the Federal Reserve System, February 27, 1997.

William W. Wiles,

Secretary of the Board.

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FEDERAL DEPOSIT INSURANCE CORPORATION

12 CFR Part 344

RIN 3064-AB74

Recordkeeping and Confirmation Requirements for Securities Transactions

AGENCY: Federal Deposit Insurance Corporation.

ACTION: Final rule.

SUMMARY: The Federal Deposit Insurance Corporation (FDIC) is amending its regulations governing the procedures for recordkeeping and confirmation requirements with respect to effecting securities transactions for customers of an insured state nonmember bank or a foreign bank having an insured branch (Bank). The final rule updates, clarifies and streamlines the FDIC regulations and reduces unnecessary regulatory costs and other burdens. The final rule also reorganizes and clarifies the regulation in areas where it previously was confusing. In addition, the FDIC has incorporated significant interpretive positions and updated various provisions to address market developments and regulatory changes by other regulators that affect requirements for recordkeeping and confirmation of securities transactions by Banks.

DATES: *Effective date.* The final rule is effective April 1, 1997. *Early compliance.* These revisions may be followed immediately by the affected party.

FOR FURTHER INFORMATION CONTACT:

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Legislation Section, Legal Division, (202) 898-8708.

SUPPLEMENTARY INFORMATION:

Background

In 1979, the FDIC adopted part 344 to require Banks under its jurisdiction to establish uniform procedures and recordkeeping and confirmation requirements with respect to effecting securities transactions for customers. The requirements reflected, in part, the recommendations of the Securities and Exchange Commission's (SEC) Final Report of the Securities and Exchange Commission on Bank Securities Activities (June 30, 1977). Part 344's recordkeeping and confirmation requirements were patterned after the SEC's rules applicable to broker/dealers and were intended to serve similar purposes for Banks involved in effecting customers' securities transactions. See 44 FR 43261 (July 24, 1979). The Board of Governors of the Federal Reserve System (FRB) and the Office of the Comptroller of the Currency (OCC) also adopted regulations substantially identical to part 344 in 1979.¹

The FDIC and the other federal banking agencies are required by section 303 of the Riegle Community Development and Regulatory Improvement Act of 1994 (CDRI) to review and streamline their regulations to improve efficiency, reduce unnecessary costs and eliminate unwarranted constraints on credit availability. 12 U.S.C. 4803(a). Section 303(a) also requires the federal banking agencies to work jointly to make uniform all regulations and guidelines implementing common statutory or supervisory policies.

On December 22, 1995, the OCC published a notice of proposed rulemaking (60 FR 66517) to revise 12 CFR part 12, the OCC's Recordkeeping and Confirmation Requirements for Securities Transactions regulation. The purpose of the proposal was to modernize part 12, address various market developments and regulatory changes, and reduce regulatory burden, where possible. The OCC published its final rule on December 2, 1996. See 61 FR 63958. The FRB published a substantially similar yet somewhat differently worded proposed rule on December 26, 1995. See 60 FR 66759.

The FDIC published an advance notice of proposed rulemaking on May 24, 1996, soliciting comment on issues similar to those raised in the OCC's and FRB's proposed rules, as well as issues

which the OCC and FRB proposals did not address. See 61 FR 26135. On December 24, 1996, the FDIC published a notice of proposed rulemaking (61 FR 67729) to amend part 344 to address various market developments and regulatory changes, and reduce regulatory burden, where possible. Consistent with Section 303 of CDRI, the FDIC reviewed the OCC rule and the FRB proposal in connection with the preparation of its notice of proposed rulemaking. The FDIC has endeavored to create a rule that is uniform with the other agencies. As part of that effort, the staff of the FDIC has been in contact with the staffs of the FRB and the OCC in connection with the drafting of the final rule. The FDIC's final rule is closer in structure, definitions, language and form to the FRB's proposal than the OCC's final rule, however, all of the agencies' rules are substantively very similar.

Comments Received and Changes Made

The FDIC received six comments on the proposal. One comment came from a bank, one from a bank holding company and four comments came from trade associations representing banks, investment companies and accountants. In general, the commenters strongly supported the proposal as promoting uniformity among the Federal bank regulatory agencies, reducing regulatory burdens as well as addressing recent developments in the securities market. Most commenters specifically supported the provision of the proposal that excluded from the scope of part 344 customer transactions conducted directly with a broker/dealer where the customer has a written account agreement with the broker-dealer and the broker-dealer is fully disclosed to the customer. This change would exclude from part 344's coverage commonly utilized contractual relationships between banks and broker/dealers whereby the broker/dealers conducts securities transactions on bank premises, known as networking arrangements.

In addition, certain of the commenters requested specific changes to the proposal. The FDIC has considered each of the comments carefully and has made a number of changes in response to the comments received. Overall, the final rule adopts most of the changes to part 344 as proposed by the FDIC although certain changes have been made in an attempt to increase uniformity with regard to recordkeeping and confirmation requirements among the federal banking regulatory agencies. The section-by-section discussion of this preamble describes the final regulation

¹ See 12 CFR 208.8(k), 44 FR 43258 (July 24, 1979) (FRB regulation); 12 CFR part 12, 44 FR 43254 (July 24, 1979) (OCC regulation).

and identifies and discusses the comments received and changes made to certain sections of the proposal.

Section-by-Section Discussion

Purpose and Scope. (Section 344.1)

The purpose of part 344 is twofold: to ensure that purchasers of securities from Banks are provided with certain necessary information about the transaction; and to ensure that Banks engaging in such transactions maintain adequate records and controls with respect to such transactions. In general, part 344 applies to securities transactions effected by Banks on behalf of customers unless the transaction is specifically exempted in § 344.2, such as, to a limited extent, transactions in government securities and transactions in municipal securities conducted by Banks that are not registered as municipal securities dealers with the SEC.

Exceptions. (Section 344.2)

The final rule provides five exceptions from the requirements of certain provisions of part 344. The specific exceptions, which are unchanged from the proposal, are: (1) Banks conducting a small number of securities transactions; (2) certain government securities transactions; (3) certain municipal securities transactions; (4) securities transactions conducted by a foreign branch of a bank; and (5) certain securities transactions with a broker/dealer. The first four exceptions already exist in part 344. The proposal added the exemption covering certain securities transactions with a broker/dealer. In order for the exception to apply, the broker/dealer must be fully disclosed to the customer and the customer must have a direct contractual agreement with the broker/dealer, that is, a signed account agreement. This exception makes clear that under the circumstances described dual employee arrangements are not subject to part 344. This exemption is similar to that found in the OCC's rule. See 12 CFR § 12.1(c)(2)(v). The rule also clarifies that even though certain transactions are excepted from compliance with all, or certain sections, of part 344, the FDIC expects a Bank conducting securities transactions for its customers to maintain effective systems of records and controls to ensure safe and sound operations.

In connection with the broker/dealer networking exception, the FDIC requested comment on whether part 344 should apply to banks which impose surcharges or additional fees on customers in addition to the transaction

volume compensation they normally receive under a networking agreements. The only comment received on this issue indicated support for requiring banks to disclose to customers that such surcharges or additional fees were being imposed. It is the FDIC's understanding that these type of surcharges and additional fees are not common, however, the FDIC expects banks to disclose the imposition of these surcharges or fees to customers and will monitor this area to determine if further supervisory action is necessary.

The FDIC received comment on the small number of securities transactions exceptions. This exception applies to banks effecting an average of fewer than 200 securities transactions per year for customers over the prior three calendar year period and excepts the bank from certain record maintenance requirements as well as the need to establish most required written policies and procedures. One commenter proposed that this limited transactions exemption be expanded to allow a Bank to effect 500 rather than 200 transactions in securities that are neither municipal securities or government securities. In light of the FDIC's desire for uniformity of its recordkeeping and disclosure requirements with those of the other Federal banking regulators and the lack of a compelling basis by the commenter to make the suggested change, the FDIC has determined to maintain the exemption for limited transactions at an average of 200 of such transactions per year.

Definitions. (Section 344.3)

Section 344.3 sets forth the definitions of 13 terms used in the rule. The FDIC's advance notice of proposed rule making described six new definitions—"asset-backed security", "completion of the transaction", "crossing of buy and sell orders", "debt security", "government security" and "municipal security." The proposal added two additional new definitions: "bank" and "cash management sweep account". The proposed definitions are the similar to those proposed by the FRB. The OCC's final rule also uses the same terms, but the structure and language used are somewhat different. The final rule adopts the definitions as set forth in the proposal with the following minor modifications in response to comments received

As proposed, the term "cash management sweep account" would cover any prearranged, automatic transfer of funds above a certain dollar level from a deposit account to purchase a security or securities or any

prearranged, automatic redemption or sale of a security or securities when a deposit account drops below a certain dollar level with the proceeds being transferred into a deposit account. The term would only cover transactions involving the purchase or sale of securities. The FDIC received two comments on its proposed definition of a "cash management sweep account" found at § 344.3(c). One commenter expressed appreciation for the clarity provided by having a separately defined term; the other raised concern that while the FDIC proposes to treat cash management sweep accounts in a manner identical to the OCC, an additional definition may cause uncertainty. The OCC defined a cash management sweep account within its definition of "periodic plan". For the reasons stated in the proposed rulemaking², the FDIC believes that there are benefits to separately defining the term "cash management sweep account". Furthermore, we do not foresee confusion resulting from the distinction used in the OCC's regulation. With respect to cash management sweep accounts, both the OCC's and the FDIC's rules will require monthly statements to be furnished to a customer for each month in which a security is purchased or sold, but not less than quarterly.

The FDIC has amended the definition of the term "security" at § 344.3(m) so that it conforms to the definition used by the other federal banking regulatory agencies. The new definition more closely tracks the definition of "security" in the Securities Exchange Act of 1934. See 17 U.S.C. 78a et seq. No substantive change in the definition or meaning of the term "security" is intended from the definition of the term as published in the FDIC's proposal and the term as used in the existing regulation. The FDIC is conforming where possible the terms of part 344 with the rules of the other federal banking regulatory agencies so that any regulatory burden resulting from the use of different terminology can be minimized.

² Sweep accounts are different in kind from typical periodic plans such as dividend reinvestment plans (DRIPs) and automatic investment plans. Sweep accounts do not normally invest in securities at the regular intervals (i.e. monthly or quarterly) as do DRIPs and automatic investment plans. Second, sweep accounts are a significant product/service in their own right which account for several billions of dollars worth of transactions on a daily basis and probably exceed the dollar volume in traditional periodic plans. Due to these differences, the FDIC believes it is not appropriate to include sweep accounts in the definition of periodic plans.

Recordkeeping. (Section 344.4)

Section 344.4 sets forth the requirements for maintenance of records of securities transactions by Banks or a third party service provider for the Bank. The rule specifically permits the use of electronic or automated records as long as the records are easily retrievable and readily available for inspection and the Bank has the capability to reproduce the records in hard copy form. The FDIC received no comments on this section, and therefore it is being adopted as proposed.

Content and Timing of Customer Notification. (Section 344.5)

Section 344.5 of the regulation identifies the information that a Bank must provide to a customer at or before the completion of a securities transaction. When a broker/dealer is utilized in a transaction, Banks have the option of either having a broker/dealer that executes a transaction for the Bank send a confirmation directly to the Bank's customer or choosing to forward a copy of the broker/dealer confirmation to the Bank customer when it is received. Banks opting to have confirmations sent directly to their customers by the broker/dealer are ultimately responsible for the timely delivery of confirmations as well as accurate disclosure of all information required therein. The FDIC received several comments concerning this section of the proposal. One commenter supported the provision allowing notices to be furnished to customers via facsimile or other electronic means. The FDIC notes its intent that references—in § 344.5 as well as § 344.6—to the "give" or "send" notices includes notice provided via facsimile or other electronic transmission.

Several commenters had concerns with the partial exemption to the customer notification requirement of the source and amount of remuneration received by a Bank from a third party. The source and amount of remuneration that the Bank receives, other than from its customer, must be disclosed to the extent required under paragraph (b)(6) of § 344.5. Paragraph 344.5(b)(6) describes three circumstances in which a Bank need only disclose to a customer that the Bank has received remuneration from a third party and that the Bank will provide such information upon the written request of the customer. If a transaction falls within one of the three enumerated exceptions in § 344.5(b)(6)(i), a simple disclosure that the Bank received remuneration from a third party and that the source and amount of such remuneration received

by the Bank from a third party is available upon written request of the customer will satisfy the disclosure requirements of § 344.5(a)(2). One commenter indicated that the rule could be read so that § 344.5(a)(2) would vitiate the exemption under § 344.5(b)(6)(ii). The FDIC does not agree. As discussed, § 344.5 (a)(2) is clear that notice need be provided only to the extent that such notice would be required under § 344.5(b)(6), including any notice based on the request of a customer as permitted in paragraph (b)(6)(ii).

Another commenter suggested that the § 344.5(b)(6)(ii) partial exemption to the customer notification requirement regarding remuneration to the Bank by a source other than the customer be extended to permit a Bank not to disclose this information to the customer at all. The commenter expressed the belief that the specific source of such remuneration would not be of interest to the majority of customers. After consideration, the FDIC has determined not to change the rule from its proposed form. The final rule will reduce regulatory burden because a Bank is required to provide amount and source of remuneration information only upon specific written request by the customer. It is also noted that the final rule is consistent with similar rules of the other federal banking regulatory agencies. Moreover, because the Bank will only need to provide such information to customers who affirmatively request it, the burden on the Bank should be minimal, particularly if—as the commenter suggests—third party remuneration to the Bank is not of interest to a majority of customers.

In addition, we note that the "source and amount of remuneration" issue which led to the FDIC issuing a partial waiver of part 344 in 1995³ has been resolved in the final rule. Previously, a literal reading of part 344 could have required a Bank to disclose the remuneration it obtained from a broker/dealer that dealt directly with the customer even if the Bank's remuneration was solely based on the broker/dealer's volume of transactions with Bank customers. Due to the impossibility of providing such disclosure to customers at the time of the transaction, the FDIC had granted a partial waiver of the requirements of part 344. Id. The FDIC now exempts for the scope of part 344 those securities

transactions where the customer has a direct contractual agreement with a fully disclosed broker/dealer. See 12 CFR § 344.2(a)(5). This exemption will remove from part 344's scope most, if not all, networking arrangements between registered broker/dealers and financial institutions. Banks will not be obligated to disclose the source and amount of remuneration since the customer is actually a customer of the broker/dealer, not the Bank, and will receive a confirmation from the broker/dealer as required by SEC regulations.

Notification by Agreement; Alternative Forms and Times of Notification. (Section 344.6)

In addition to the standard notification requirements in § 344.5, the final regulation, in § 344.6, generally authorizes a Bank, in cases in which it does not exercise investment discretion, to enter into a written agreement with its customer for an alternative arrangement as to the time and content of written notification. Section 344.6 also sets forth alternative forms and times of notification for certain specific types of accounts. These are: (1) accounts in which the bank exercises investment discretion in other than an agency capacity; (2) accounts in which the bank exercises investment discretion in an agency capacity; (3) cash management sweep accounts; (4) transactions for a collective investment fund account; and (5) transactions for a periodic plan account. The FDIC has added language to the final regulation amending the requirements for certain cash management sweep accounts set forth in § 344.6(d) in order to ensure that banks are aware that if they retain custody of securities that are the subject of a hold-in-custody repurchase agreement, they are subject to certain Treasury Department regulations governing confirmation requirements with respect to government securities transactions.

The FDIC received one comment regarding the financial disclosure required for collective investment fund accounts in § 344.6(e) suggesting that such disclosure be required to be made only by independent auditors in accordance with generally accepted auditing standards. The final rule allows either independent public accountants or internal auditors responsible only to the board of directors of the bank to prepare the financial information. The FDIC notes that § 344.6(e) is identical to language used in the OCC's rule and the FRB's proposal. Moreover, the potential benefits resulting from the mandated use of external auditors does not outweigh the costs associated with

³ See "Waiver of Burdensome Disclosures for Certain Securities Transactions for Bank Customers", FDIC Financial Institutions Letter 29-95 (April 7, 1995).

imposing such a regulatory burden upon the industry. Banks should be allowed the flexibility to effect the required disclosure through the use of external auditors as suggested by the commenter, or internal auditors that are responsible to only the board of directors. The final regulation adopts the language of the proposal.

Settlement of Securities Transactions. (Section 344.7)

The proposal provided for a settlement period of T+3 and requires Banks to send broker/dealer confirmations within one business day of receipt. These requirements are being adopted in the final rule without change. The requirements are identical to those of the SEC and the other federal banking regulatory agencies and were generally supported by the commenters. One commenter suggested cross-referencing the rules of the Securities and Exchange Commission governing the settlement period for securities transactions into part 344 so that regulatory amendments by the SEC would automatically amend the FDIC's regulations. The FDIC has determined not to incorporate citations to the SEC's settlement regulations. Rather, the FDIC will review any regulatory amendments by the SEC on a case-by-case basis to determine whether such changes would be appropriate for Banks. The FDIC received no other comments on this section, and therefore it is being adopted as proposed.

Securities Trading Policies and Procedures. (Section 344.8)

Section 344.8 of the final regulation requires Banks to establish written policies and procedures assigning supervisory responsibility for personnel engaged in different aspects of the trading process. Specifically, this section addresses orders and execution of trades, the equitable allocation of securities and prices for accounts and the crossing of buy and sell orders. In addition, § 344.8(a)(2) requires the separation of order and execution functions from the traditional back office clearing functions in order to ensure that Banks maintain adequate internal controls for securities trading. The FDIC received no comments on this section, and therefore it is being adopted as proposed.

Personal Securities Trading Reported by Bank Officers and Employees. (Section 344.9)

The proposal relocated to § 344.9 without substantive change the personal trading reporting requirements for certain officers and employees. The

notice of proposed rulemaking also included a new requirement that certain directors report their transactions in securities. As proposed, § 344.9(a) would have required Bank directors, under certain limited and specified circumstances, to report a limited number of transactions in securities. The OCC's rule and the FRB's proposal do not specifically address the issue of director reporting requirements in this area.

As proposed, the reporting requirements of § 344.9 would have applied equally to directors, officers, or employees who have access to information in such a fashion so as to enable the person to gain an improper advantage or abuse the information obtained. The reporting requirement would not extend to individuals who routinely obtain such information but are never in a position to abuse it.

The two comments received on the provision indicated uncertainty as to the scope and application of this provision of the proposed rule. One commenter indicated the rule could be interpreted more broadly than anticipated, and another comment indicated a reading more narrow than intended. Given the different interpretations of the proposed changes, it is clear that additional clarification is required if the FDIC were to retain the requirement. Upon review, the FDIC believes that additional revision to the proposed regulatory language would be necessary to accomplish the FDIC's intent. The FDIC recognizes that implementing the proposed amendatory language could result in reports being submitted by individual directors who are not intended to be subject to the reporting requirements. Other directors may innocently fail to report who are intended to be subject to the rule. Accordingly, in order to not unnecessarily increase the burden of regulatory reporting requirements, and in a continuing effort to maintain uniformity in the reporting requirements imposed by the federal banking regulators, the final rule does not contain specific reporting requirements for directors. The FDIC will, in consultation with the other federal banking regulators, study the issue of employee, officer, and director disclosures further and address the issue in a future rulemaking as appropriate. Any changes to the reporting requirements to be imposed upon bank directors, if proposed in the future, will be implemented following appropriate notice and comment.

Waivers. (Section 344.10)

This section maintains the current provision that enables the FDIC to waive any provision of part 344 for good cause. No comments were received on this provision and it is being adopted as proposed.

Effective Date

This regulation will become effective on April 1, 1997 in accordance with the requirements of the Paper Work Reduction and Regulatory Improvement Act (PWRRIA). Section 302(b) requires that the effectiveness of new rules be delayed until the beginning of the following calendar quarter in order to give depository institutions adequate time to adjust to new requirements, such as in this instance, the T+3 settlement requirement. Nevertheless, as permitted by Section 302 of the PWRRIA, 12 U.S.C. 4802, banks may comply with the final rule before the effective date. In particular, the FDIC would not object to a Bank immediately taking advantage of § 344.2(a)(5) of the final rule that exempts transactions in which a bank receives remuneration from a registered broker dealer so long as the broker/dealer is fully disclosed to the bank customer and the bank customer has a direct contractual agreement with the broker/dealer may be utilized.

Regulatory Flexibility Act

Under section 605(b) of the Regulatory Flexibility Act (RFA) (5 U.S.C. 605(b)), the final regulatory flexibility analysis otherwise required under section 604 of the RFA (5 U.S.C. 604) is not required if the head of the agency certifies that the rule will not have a significant economic impact on a substantial number of small entities and the agency publishes such certification in the Federal Register along with its general notice of proposed rulemaking or at the time of publication of the final rule.

The Board of Directors has concluded after reviewing the final regulation that it will not have a significant economic impact on a substantial number of small institutions. The Board of Directors therefore hereby certifies pursuant to section 605 of the RFA that the regulation will not have a significant economic impact on a substantial number of small entities within the meaning of the RFA. The FDIC anticipates that the final rule will result in a net benefit to all banks regardless of size due to the clarification provided by the rule. Small banks, in particular should be benefited by these changes. Most banks with total assets of under

\$100 million are not engaged in securities activities in a manner covered by this regulation. Rather, a small bank typically will use either a registered broker/dealer who has rented space on the bank's premises in what is commonly referred to as a "networking arrangement" or an "introducing broker" who will refer a customer to a dealer that can effect the desired transaction, both of which situations are outside the scope of part 344 as adopted.

Small Business Regulatory Enforcement Fairness Act

The Small Business Regulatory Enforcement Fairness Act of 1996 (SBREFA) (Public Law 104-121) provides generally for agencies to report rules to Congress and for Congress to review rules. The reporting requirement is triggered when agencies issue a final rule as defined by the Administrative Procedure Act (APA) at 5 U.S.C. 551. Because the FDIC is issuing a final rule as defined by the APA, the FDIC will file the reports required by SBREFA.

The Office of Management and Budget (OMB) has determined that this final revision to part 344 does not constitute a "major rule" as defined by SBREFA.

Paperwork Reduction Act

The collection of information contained in this final rule has been reviewed and approved by the OMB under control number 3064-0028 pursuant to section 3504(h) of the Paperwork Reduction Act of 1980 (44 U.S.C. 3501 *et seq.*). Comments on the collections of information should be directed to the OMB, Paperwork Reduction Project (3064-0028) Washington, D.C. 20503 Attention: Desk officer for the Federal Deposit Insurance Corporation, with copies of such comments to be sent to Steven F. Hanft, Office of the Executive Secretary, room F-400, Federal Deposit Insurance Corporation, 550 17th Street, NW, Washington, D.C. 20429.

The collection of information requirements in this final rule are found in 12 CFR 344.2(b), 344.4(a), 344.5 (a) and (b), 344.8, and 344.9. The collections consist of recordkeeping requirements, §§ 344.2(b) and 344.4(a); the provision of written confirmations, §§ 344.5 (a) and (b) and 344.6; the establishment of written policies and procedures for placing orders and executing trades as well as back office functions, § 344.8; the reporting of personal securities trading by certain bank officers and employees, § 344.9. The likely respondents/recordkeepers are state nonmember insured banks.

Estimated average annual burden hours per respondent/recordkeeper: 19.43 hours.

Estimated number of respondents and/or recordkeepers: 5,663 state nonmember insured banks.

Estimated total annual reporting and recordkeeping burden: 109,818 hours.

Start-up costs to respondents: None.

Records under this part are to be maintained for at least three years.

List of Subjects in 12 CFR Part 344

Banks, banking, Reporting and recordkeeping requirements, Securities.

For the reasons set forth above, the FDIC hereby revises 12 CFR part 344 to read as follows.

PART 344—RECORDKEEPING AND CONFIRMATION REQUIREMENTS FOR SECURITIES TRANSACTIONS

Sec.

- 344.1 Purpose and scope.
- 344.2 Exceptions.
- 344.3 Definitions.
- 344.4 Recordkeeping.
- 344.5 Content and time of notification.
- 344.6 Notification by agreement; alternative forms and times of notification.
- 344.7 Settlement of securities transactions.
- 344.8 Securities trading policies and procedures.
- 344.9 Personal securities trading reporting by bank officers and employees.
- 344.10 Waivers.

Authority: 12 U.S.C. 1817, 1818 and 1819.

§ 344.1 Purpose and scope.

(a) *Purpose.* The purpose of this part is to ensure that purchasers of securities in transactions effected by a state nonmember insured bank (except a District bank) or a foreign bank having an insured branch are provided adequate information regarding transactions. This part is also designed to ensure that banks subject to this part maintain adequate records and controls with respect to the securities transactions they effect.

(b) *Scope; general.* Any security transaction effected for a customer by a bank is subject to this part unless excepted by § 344.2. A bank effecting transactions in government securities is subject to the notification, recordkeeping, and policies and procedures requirements of this part. This part also applies to municipal securities transactions by a bank that is not registered as a "municipal securities dealer" with the Securities and Exchange Commission. See 15 U.S.C. 78c(a)(30) and 78o-4.

§ 344.2 Exceptions.

(a) A bank effecting securities transactions for customers is not subject to all or part of this part 344 to the

extent that they qualify for one or more of the following exceptions:

(1) *Small number of transactions.* The requirements of §§ 344.4(a) (2) through (4) and 344.8(a) (1) through (3) do not apply to a bank effecting an average of fewer than 200 securities transactions per year for customers over the prior three calendar year period. The calculation of this average does not include transactions in government securities.

(2) *Government securities.* The recordkeeping requirements of § 344.4 do not apply to banks effecting fewer than 500 government securities brokerage transactions per year. This exemption does not apply to government securities dealer transactions by banks.

(3) *Municipal securities.* This part does not apply to transactions in municipal securities effected by a bank registered with the Securities and Exchange Commission as a "municipal securities dealer" as defined in title 15 U.S.C. 78c(a)(30). See 15 U.S.C. 78o-4.

(4) *Foreign branches.* Activities of foreign branches of a bank shall not be subject to the requirements of this part.

(5) *Transactions effected by registered broker/dealers.* (i) This part does not apply to securities transactions effected for a bank customer by a registered broker/dealer if:

(A) The broker/dealer is fully disclosed to the bank customer; and

(B) The bank customer has a direct contractual agreement with the broker/dealer.

(ii) This exemption extends to bank arrangements with broker/dealers which involve bank employees when acting as employees of, and subject to the supervision of, the registered broker/dealer when soliciting, recommending, or effecting securities transactions.

(b) *Safe and sound operations.* Notwithstanding this section, every bank effecting securities transactions for customers shall maintain, directly or indirectly, effective systems of records and controls regarding their customer securities transactions to ensure safe and sound operations. The records and systems maintained must clearly and accurately reflect the information required under this part and provide an adequate basis for an audit.

§ 344.3 Definitions.

(a) *Asset-backed security* means a security that is serviced primarily by the cash flows of a discrete pool of receivables or other financial assets, either fixed or revolving, that by their terms convert into cash within a finite time period plus any rights or other assets designed to assure the servicing

or timely distribution of proceeds to the security holders.

(b) *Bank* means a state nonmember insured bank (except a District bank) or a foreign bank having an insured branch.

(c) *Cash management sweep account* means a prearranged, automatic transfer of funds above a certain dollar level from a deposit account to purchase a security or securities, or any prearranged, automatic redemption or sale of a security or securities when a deposit account drops below a certain level with the proceeds being transferred into a deposit account.

(d) *Collective investment fund* means funds held by a bank as fiduciary and, consistent with local law, invested collectively:

(1) In a common trust fund maintained by such bank exclusively for the collective investment and reinvestment of monies contributed thereto by the bank in its capacity as trustee, executor, administrator, guardian, or custodian under the Uniform Gifts to Minors Act; or

(2) In a fund consisting solely of assets of retirement, pension, profit sharing, stock bonus or similar trusts which are exempt from Federal income taxation under the Internal Revenue Code (26 U.S.C.).

(e) *Completion of the transaction* means:

(1) For purchase transactions, the time when the customer pays the bank any part of the purchase price (or the time when the bank makes the book-entry for any part of the purchase price, if applicable), however, if the customer pays for the security prior to the time payment is requested or becomes due, then the transaction shall be completed when the bank transfers the security into the account of the customer; and

(2) For sale transactions, the time when the bank transfers the security out of the account of the customer or, if the security is not in the bank's custody, then the time when the security is delivered to the bank, however, if the customer delivers the security to the bank prior to the time delivery is requested or becomes due then the transaction shall be completed when the bank makes payment into the account of the customer.

(f) *Crossing of buy and sell orders* means a security transaction in which the same bank acts as agent for both the buyer and the seller.

(g) *Customer* means any person or account, including any agency, trust, estate, guardianship, or other fiduciary account for which a bank effects or participates in effecting the purchase or sale of securities, but does not include

a broker, dealer, bank acting as a broker or a dealer, issuer of the securities that are the subject of the transaction or a person or account having a direct, contractual agreement with a fully disclosed broker/dealer.

(h) *Debt security* means any security, such as a bond, debenture, note, or any other similar instrument that evidences a liability of the issuer (including any security of this type that is convertible into stock or a similar security) and fractional or participation interests in one or more of any of the foregoing; provided, however, that securities issued by an investment company registered under the Investment Company Act of 1940, 15 U.S.C. 80a-1 et seq., shall not be included in this definition.

(i) *Government security* means:

(1) A security that is a direct obligation of, or obligation guaranteed as to principal and interest by, the United States;

(2) A security that is issued or guaranteed by a corporation in which the United States has a direct or indirect interest and which is designated by the Secretary of the Treasury for exemption as necessary or appropriate in the public interest or for the protection of investors;

(3) A security issued or guaranteed as to principal and interest by any corporation whose securities are designated, by statute specifically naming the corporation, to constitute exempt securities within the meaning of the laws administered by the Securities and Exchange Commission; or

(4) Any put, call, straddle, option, or privilege on a security described in paragraph (i) (1), (2), or (3) of this section other than a put, call, straddle, option, or privilege that is traded on one or more national securities exchanges, or for which quotations are disseminated through an automated quotation system operated by a registered securities association.

(j) *Investment discretion* means that, with respect to an account, a bank directly or indirectly:

(1) Is authorized to determine what securities or other property shall be purchased or sold by or for the account; or

(2) Makes decisions as to what securities or other property shall be purchased or sold by or for the account even though some other person may have responsibility for these investment decisions.

(k) *Municipal security* means a security which is a direct obligation of, or an obligation guaranteed as to principal or interest by, a State or any political subdivision, or any agency or

instrumentality of a State or any political subdivision, or any municipal corporate instrumentality of one or more States or any security which is an industrial development bond (as defined in 26 U.S.C. 103(c)(2)) the interest on which is excludable from gross income under 26 U.S.C. 103(a)(1) if, by reason of the application of paragraph (4) or (6) of 26 U.S.C. 103(c) (determined as if paragraphs (4)(A), (5) and (7) were not included in 26 U.S.C. 103(c), paragraph (1) of 26 U.S.C. 103(c) does not apply to such security.

(l) *Periodic plan* means any written authorization for a bank to act as agent to purchase or sell for a customer a specific security or securities, in a specific amount (calculated in security units or dollars) or to the extent of dividends and funds available, at specific time intervals, and setting forth the commission or charges to be paid by the customer or the manner of calculating them. Periodic plans include dividend reinvestment plans, automatic investment plans, and employee stock purchase plans.

(m) *Security* means any note, stock, treasury stock, bond, debenture, certificate of interest or participation in any profit-sharing agreement or in any oil, gas, or other mineral royalty or lease, any collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, and any put, call, straddle, option, or privilege on any security or group or index of securities (including any interest therein or based on the value thereof), or, in general, any instrument commonly known as a "security"; or any certificate of interest or participation in, temporary or interim certificate for, receipt for, or warrant or right to subscribe to or purchase, any of the foregoing. The term security does not include:

(1) A deposit or share account in a federally or state insured depository institution;

(2) A loan participation;

(3) A letter of credit or other form of bank indebtedness incurred in the ordinary course of business;

(4) Currency;

(5) Any note, draft, bill of exchange, or bankers acceptance which has a maturity at the time of issuance of not exceeding nine months, exclusive of days of grace, or any renewal thereof the maturity of which is likewise limited;

(6) Units of a collective investment fund;

(7) Interests in a variable amount (master) note of a borrower of prime credit; or

(8) U.S. Savings Bonds.

§ 344.4 Recordkeeping.

(a) *General rule.* A bank effecting securities transactions for customers shall maintain the following records for at least three years:

(1) *Chronological records.* An itemized daily record of each purchase and sale of securities maintained in chronological order, and including:

(i) Account or customer name for which each transaction was effected;

(ii) Description of the securities;

(iii) Unit and aggregate purchase or sale price;

(iv) Trade date; and

(v) Name or other designation of the broker/dealer or other person from whom the securities were purchased or to whom the securities were sold;

(2) *Account records.* Account records for each customer, reflecting:

(i) Purchases and sales of securities;

(ii) Receipts and deliveries of securities;

(iii) Receipts and disbursements of cash; and

(iv) Other debits and credits pertaining to transactions in securities;

(3) *A separate memorandum (order ticket)* of each order to purchase or sell securities (whether executed or canceled), which shall include:

(i) The accounts for which the transaction was effected;

(ii) Whether the transaction was a market order, limit order, or subject to special instructions;

(iii) The time the order was received by the trader or other bank employee responsible for effecting the transaction;

(iv) The time the order was placed with the broker/dealer, or if there was no broker/dealer, time the order was executed or canceled;

(v) The price at which the order was executed; and

(vi) The broker/dealer utilized;

(4) *Record of broker/dealers.* A record of all broker/dealers selected by the bank to effect securities transactions and the amount of commissions paid or allocated to each broker during the calendar year; and

(5) *Notifications.* A copy of the written notification required by §§ 344.5 and 344.6.

(b) *Manner of maintenance.* Records may be maintained in whatever manner, form or format a bank deems appropriate, provided however, the records required by this section must clearly and accurately reflect the information required and provide an adequate basis for the audit of the information. Records may be maintained in hard copy, automated or electronic form provided the records are easily retrievable, readily available for inspection, and capable of being

reproduced in a hard copy. A bank may contract with third party service providers, including broker/dealers, to maintain records required under this part.

§ 344.5 Content and time of notification.

Every bank effecting a securities transaction for a customer shall give or send, by mail, facsimile or other means of electronic transmission, to the customer at or before completion of the transaction one of the types of written notification identified below:

(a) *Broker/dealer's confirmations.* (1) A copy of the confirmation of a broker/dealer relating to the securities transaction. A bank may either have the broker/dealer send the confirmation directly to the bank's customer or send a copy of the broker/dealer's confirmation to the customer upon receipt of the confirmation by the bank. If a bank chooses to send a copy of the broker/dealer's confirmation, it must be sent within one business day from the bank's receipt of the broker/dealer's confirmation; and

(2) If the bank is to receive remuneration from the customer or any other source in connection with the transaction, a statement of the source and amount of any remuneration to be received if such would be required under paragraph (b)(6) of this section; or

(b) *Written notification.* A written notification disclosing:

(1) Name of the bank;

(2) Name of the customer;

(3) Whether the bank is acting as agent for such customer, as agent for both such customer and some other person, as principal for its own account, or in any other capacity;

(4) The date and time of execution, or the fact that the time of execution will be furnished within a reasonable time upon written request of the customer, and the identity, price, and number of shares or units (or principal amount in the case of debt securities) of the security purchased or sold by the customer;

(5) The amount of any remuneration received or to be received, directly or indirectly, by any broker/dealer from such customer in connection with the transaction;

(6)(i) The amount of any remuneration received or to be received by the bank from the customer, and the source and amount of any other remuneration received or to be received by the bank in connection with the transaction, unless:

(A) Remuneration is determined pursuant to a prior written agreement between the bank and the customer; or

(B) In the case of government securities and municipal securities, the bank received the remuneration in other than an agency transaction; or

(C) In the case of open end investment company securities, the bank has provided the customer with a current prospectus which discloses all current fees, loads and expenses at or before completion of the transaction;

(ii) If the bank elects not to disclose the source and amount of remuneration it has or will receive from a party other than the customer pursuant to paragraph (b)(6)(i) (A), (B), or (C) of this section, the written notification must disclose whether the bank has received or will receive remuneration from a party other than the customer, and that the bank will furnish within a reasonable time the source and amount of this remuneration upon written request of the customer. This election is not available, however, if, with respect to a purchase, the bank was participating in a distribution of that security; or, with respect to a sale, the bank was participating in a tender offer for that security;

(7) Name of the broker/dealer utilized; or where there is no broker/dealer, the name of the person from whom the security was purchased or to whom the security was sold, or a statement that the bank will furnish this information within a reasonable time upon written request;

(8) In the case of a transaction in a debt security subject to redemption before maturity, a statement to the effect that the debt security may be redeemed in whole or in part before maturity, that the redemption could affect the yield represented and that additional information is available upon request;

(9) In the case of a transaction in a debt security effected exclusively on the basis of a dollar price:

(i) The dollar price at which the transaction was effected; and

(ii) The yield to maturity calculated from the dollar price, provided however, that this shall not apply to a transaction in a debt security that either has a maturity date that may be extended by the issuer thereof, with a variable interest payable thereon, or is an asset-backed security that represents an interest in or is secured by a pool of receivables or other financial assets that are subject continuously to prepayment;

(10) In the case of a transaction in a debt security effected on the basis of yield:

(i) The yield at which the transaction was effected, including the percentage amount and its characterization (e.g., current yield, yield to maturity, or yield to call) and if effected at yield to call,

the type of call, the call date and call price;

(ii) The dollar price calculated from the yield at which the transaction was effected; and

(iii) If effected on a basis other than yield to maturity and the yield to maturity is lower than the represented yield, the yield to maturity as well as the represented yield; provided however, that this paragraph (b)(10) shall not apply to a transaction in a debt security that either has a maturity date that may be extended by the issuer with a variable interest rate payable thereon, or is an asset-backed security that represents an interest in or is secured by a pool of receivables or other financial assets that are subject continuously to prepayment;

(11) In the case of a transaction in a debt security that is an asset-backed security, which represents an interest in or is secured by a pool of receivables or other financial assets that are subject continuously to prepayment, a statement indicating that the actual yield of the asset-backed security may vary according to the rate at which the underlying receivables or other financial assets are prepaid and a statement of the fact that information concerning the factors that affect yield (including at a minimum estimated yield, weighted average life, and the prepayment assumptions underlying yield) will be furnished upon written request of the customer; and

(12) In the case of a transaction in a debt security, other than a government security, that the security is unrated by a nationally recognized statistical rating organization, if that is the case.

§ 344.6 Notification by agreement; alternative forms and times of notification.

A bank may elect to use the following alternative notification procedures if the transaction is effected for:

(a) *Notification by agreement.* 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 written notification; provided however, that such agreement makes clear the customer's right to receive the written notification pursuant to § 344.5 (a) or (b) at no additional cost to the customer.

(b) *Trust accounts.* Accounts (except collective investment funds) where the bank exercises investment discretion in other than in an agency capacity, in which instance the bank shall, upon request of the person having the power to terminate the account or, if there is no such person, upon the request of any

person holding a vested beneficial interest in such account, give or send to such person the written notification within a reasonable time. The bank may charge such person a reasonable fee for providing this information.

(c) *Agency accounts.* Accounts where the bank exercises investment discretion in an agency capacity, in which instance:

(1) The bank shall give or send 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

(2) If requested by the customer, the bank shall give or send to each customer within a reasonable time the written notification described in § 344.5. The bank may charge a reasonable fee for providing the information described in § 344.5.

(d) *Cash management sweep accounts.* A bank effecting a securities transaction for a cash management sweep account shall give or send its customer a written statement, in the same form as required under paragraph (f) of this section, for each month in which a purchase or sale of a security takes place in the account and not less than once every three months if there are no securities transactions in the account. Notwithstanding the provisions of this paragraph (d), banks that retain custody of government securities that are the subject of a hold-in-custody repurchase agreement are subject to the requirements of 17 CFR 403.5(d).

(e) *Collective investment fund accounts.* The bank shall at least annually give or send to the customer a copy of a financial report of the fund, or provide notice that a copy of such report is available and will be furnished upon request to each person to whom a regular periodic accounting would ordinarily be rendered with respect to each participating account. This report shall be based upon an audit made by independent public accountants or internal auditors responsible only to the board of directors of the bank.

(f) *Periodic plan accounts.* The bank shall give or send to the customer not less than once every three months a written statement showing:

(1) The funds and securities in the custody or possession of the bank;

(2) All service charges and commissions paid by the customer in connection with the transaction; and

(3) All other debits and credits of the customer's account involved in the

transaction; provided that upon written request of the customer, the bank shall give or send the information described in § 344.5, except that any such information relating to remuneration paid in connection with the transaction need not be provided to the customer when the remuneration is paid by a source other than the customer. The bank may charge a reasonable fee for providing information described in § 344.5.

§ 344.7 Settlement of securities transactions.

(a) A bank shall not effect or enter into a contract for the purchase or sale of a security (other than an exempted security as defined in 15 U.S.C. 78c(a)(12), government security, municipal security, commercial paper, bankers' acceptances, or commercial bills) that provides for payment of funds and delivery of securities later than the third business day after the date of the contract unless otherwise expressly agreed to by the parties at the time of the transaction.

(b) Paragraphs (a) and (c) of this section shall not apply to contracts:

(1) For the purchase or sale of limited partnership interests that are not listed on an exchange or for which quotations are not disseminated through an automated quotation system of a registered securities association; or

(2) For the purchase or sale of securities that the Securities and Exchange Commission (SEC) may from time to time, taking into account then existing market practices, exempt by order from the requirements of paragraph (a) of SEC Rule 15c6-1, 17 CFR 240.15c6-1(a), either unconditionally or on specified terms and conditions, if the SEC determines that an exemption is consistent with the public interest and the protection of investors.

(c) Paragraph (a) of this section shall not apply to contracts for the sale for cash of securities that are priced after 4:30 p.m. Eastern time on the date the securities are priced and that are sold by an issuer to an underwriter pursuant to a firm commitment underwritten offering registered under the Securities Act of 1933, 15 U.S.C. 77a et seq., or sold to an initial purchaser by a bank participating in the offering. A bank shall not effect or enter into a contract for the purchase or sale of the securities that provides for payment of funds and delivery of securities later than the fourth business day after the date of the contract unless otherwise expressly agreed to by the parties at the time of the transaction.

(d) For purposes of paragraphs (a) and (c) of this section, the parties to a contract shall be deemed to have expressly agreed to an alternate date for payment of funds and delivery of securities at the time of the transaction for a contract for the sale for cash of securities pursuant to a firm commitment offering if the managing underwriter and the issuer have agreed to the date for all securities sold pursuant to the offering and the parties to the contract have not expressly agreed to another date for payment of funds and delivery of securities at the time of the transaction.

§ 344.8 Securities trading policies and procedures.

(a) *Policies and procedures.* Every bank effecting securities transactions for customers shall establish written policies and procedures providing:

(1) Assignment of responsibility for supervision of all officers or employees who:

(i) Transmit orders to or place orders with broker/dealers; or

(ii) Execute transactions in securities for customers;

(2) Assignment of responsibility for supervision and reporting, separate from those in paragraph (a)(1) of this section, with respect to all officers or employees who process orders for notification or settlement purposes, or perform other back office functions with respect to securities transactions effected for customers;

(3) For the fair and equitable allocation of securities and prices to accounts when orders for the same security are received at approximately the same time and are placed for execution either individually or in combination; and

(4) Where applicable, and where permissible under local law, for the crossing of buy and sell orders on a fair and equitable basis to the parties to the transaction.

§ 344.9 Personal securities trading reporting by bank officers and employees.

(a) *Officers and employees subject to reporting.* Bank officers and employees who:

(1) Make investment recommendations or decisions for the accounts of customers;

(2) Participate in the determination of such recommendations or decisions; or

(3) In connection with their duties, obtain information concerning which securities are being purchased or sold or recommend such action, must report to the bank, within ten business 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.

(b) *Exempt transactions.* Excluded from this reporting requirement are:

(1) Transactions for the benefit of the officer or employee over which the officer or employee has no direct or indirect influence or control;

(2) Transactions in registered investment company shares;

(3) Transactions in government securities; and

(4) All transactions involving in the aggregate \$10,000 or less during the calendar quarter.

(c) *Alternative report.* Where a bank acts as an investment adviser to an investment company registered under the Investment Company Act of 1940, the bank's officers and employees may fulfill their reporting requirement under paragraph (a) of this section by filing with the bank the "access persons" personal securities trading report required by (SEC) Rule 17j-1, 17 CFR 270.17j-1.

§ 344.10 Waivers.

The Board of Directors of the FDIC, in its discretion, may waive for good cause all or any part of this part 344.

By Order of the Board of Directors.

Dated at Washington, D.C., this 25th day of February, 1997.

Federal Deposit Insurance Corporation.

Robert E. Feldman,

Deputy Executive Secretary.

[FR Doc. 97-5425 Filed 3-4-97; 8:45 am]

BILLING CODE 6714-01-P

DEPARTMENT OF TRANSPORTATION

Federal Aviation Administration

14 CFR Part 21

[Docket No. AIR-100-9601]

Replacement and Modification Parts: "Standard" Parts; Interpretation

AGENCY: Federal Aviation Administration (FAA), DOT.

ACTION: Notice of interpretation.

SUMMARY: The FAA is notifying the public that the interpretation of an acceptable U.S. government or Industry accepted specification may include specifications that may be limited to detailed performance criteria, complete testing procedures, and uniform marking criteria. Manufacturers of parts

that conform to such specifications are excepted as "standard parts" from the requirement to obtain FAA Parts Manufacturer Approval. The FAA is aware that specifications meeting the above criteria exist for discrete electric or electrical component parts.

EFFECTIVE DATE: January 31, 1997.

FOR FURTHER INFORMATION CONTACT:

Bruce Kaplan, Aerospace Engineer, Aircraft Engineering Division, AIR-100, FAA, 800 Independence Avenue, SW., Washington, DC 20591, (202) 267-9588.

SUPPLEMENTARY INFORMATION: Section 21.303(a) of Title 14 of the Code of Federal Regulations (CFR), Replacement and Modification Parts, prohibits a person from producing a part for sale for installation on a type certificated product unless that person produces the part pursuant to an FAA Parts Manufacturer Approval (PMA). Section 21.303(b) provides four exceptions to the requirement in § 21.303(a). One of these exceptions is for "Standard parts (such as bolts and nuts) conforming to established industry or U.S. specifications." (14 CFR § 21.303(b)(4).)

"Standard part" is not otherwise defined in Title 14. Section 21.303(b)(4) has come to be understood by the aviation and manufacturing public as meaning a part, the specification for which has been published by a standard setting organization or by the U.S. government, and the FAA has traditionally regulated parts production with that understanding. Examples of such "traditional" standard part specifications include National Aerospace Standards (NAS), Air Force-Navy Aeronautical Standard (AN), Society of Automotive Engineers (SAE), SAE Aerospace Standard (AS), and Military Standard (MS). The FAA will continue to consider parts conforming to these specifications as standard parts.

Prior to this notice, for a specification to be acceptable, it had to include information on the design, materials, manufacture, and uniform identification requirements. The specification had to include all the information necessary to produce the part and ensure its conformity to the specification. Furthermore, the specification must be publicly available, so that any party is capable of manufacturing the part. The above examples of accepted specifications fulfill those criteria.

In the past the FAA has applied § 21.303(b)(4) to parts that have specifications where a determination of physical conformity to a design could be made. This application largely excluded classes of parts where the parts are conformed not on the basis of their physical configuration but by meeting