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State insurance licensing standards with regard to the specific products being sold or recommended.

APPENDIX A TO SUBPART H OF PART 208—CONSUMER GRIEVANCE PROCESS

Any consumer who believes that any bank or any other person selling, soliciting, advertising, or offering insurance products or annuities to the consumer at an office of the bank or on behalf of the bank has violated the requirements of this subpart should contact the Consumer Complaints Section, Division of Consumer and Community Affairs, Board of Governors of the Federal Reserve System at the following address: 20th & C Streets, NW, Washington, D.C. 20551.

Subpart I—Interpretations

SOURCE: Reg. H, 63 FR 37658, July 13, 1998, unless otherwise noted. Redesignated at 65 FR 14814, Mar. 20, 2000. Redesignated further at 65 FR 75841, Dec. 4, 2000.

§ 208.100 Sale of bank's money orders off premises as establishment of branch office.

(a) The Board of Governors has been asked to consider whether the appointment by a member bank of an agent to sell the bank's money orders, at a location other than the premises of the bank, constitutes the establishment of a branch office.

(b) Section 5155 of the Revised Statutes (12 U.S.C. 36), which is also applicable to member banks, defines the term branch as including ''any branch bank, branch office, branch agency, additional office, or any branch place of business * * * at which deposits are received, or checks paid, or money lent.'' The basic question is whether the sale of a bank's money orders by an agent amounts to the receipt of deposits at a branch place of business within the meaning of this statute.

(c) Money orders are classified as deposits for certain purposes. However, they bear a strong resemblance to traveler's checks that are issued by banks and sold off premises. In both cases, the purchaser does not intend to establish a deposit account in the bank, although a liability on the bank's part is created. Even though they result in a deposit liability, the Board is of the opinion that the issuance of a bank's money orders by an authorized agent does not involve the receipt of deposits at a ''branch place of business'' and accordingly does not require the Board's permission to establish a branch.

§ 208.101 Obligations concerning institutional customers.

(a) As a result of broadened authority provided by the Government Securities Act Amendments of 1993 (15 U.S.C. 78o–3 and 78o–5), the Board is adopting sales practice rules for the government securities market, a market with a particularly broad institutional component. Accordingly, the Board believes it is appropriate to provide further guidance to banks on their suitability obligations when making recommendations to institutional customers.

(b) The Board's Suitability Rule, § 208.37(d), is fundamental to fair dealing and is intended to promote ethical sales practices and high standards of professional conduct. Banks' responsibilities include having a reasonable basis for recommending a particular security or strategy, as well as having reasonable grounds for believing the recommendation is suitable for the customer to whom it is made. Banks are expected to meet the same high standards of competence, professionalism, and good faith regardless of the financial circumstances of the customer.

(c) In recommending to a customer the purchase, sale, or exchange of any government security, the bank shall have reasonable grounds for believing that the recommendation is suitable for the customer upon the basis of the facts, if any, disclosed by the customer as to the customer's other security holdings and financial situation and needs.

(d) The interpretation in this section concerns only the manner in which a bank determines that a recommendation is suitable for a particular institutional customer. The manner in which a bank fulfills this suitability obligation will vary, depending on the nature of the customer and the specific transaction. Accordingly, the interpretation in this section deals only with guidance regarding how a bank may fulfill

customer-specific suitability obligations under § 208.37(d).[7]

(e) While it is difficult to define in advance the scope of a bank's suitability obligation with respect to a specific institutional customer transaction recommended by a bank, the Board has identified certain factors that may be relevant when considering compliance with § 208.37(d). These factors are not intended to be requirements or the only factors to be considered but are offered merely as guidance in determining the scope of a bank's suitability obligations.

(f) The two most important considerations in determining the scope of a bank's suitability obligations in making recommendations to an institutional customer are the customer's capability to evaluate investment risk independently and the extent to which the customer is exercising independent judgement in evaluating a bank's recommendation. A bank must determine, based on the information available to it, the customer's capability to evaluate investment risk. In some cases, the bank may conclude that the customer is not capable of making independent investment decisions in general. In other cases, the institutional customer may have general capability, but may not be able to understand a particular type of instrument or its risk. This is more likely to arise with relatively new types of instruments, or those with significantly different risk or volatility characteristics than other investments generally made by the institution. If a customer is either generally not capable of evaluating investment risk or lacks sufficient capability to evaluate the particular product, the scope of a bank's customer-specific obligations under § 208.37(d) would not be diminished by the fact that the bank was dealing with an institutional customer. On the other hand, the fact that a customer initially needed help understanding a potential investment need not necessarily imply that the customer did not ultimately develop an understanding and make an independent investment decision.

(g) A bank may conclude that a customer is exercising independent judgement if the customer's investment decision will be based on its own independent assessment of the opportunities and risks presented by a potential investment, market factors and other investment considerations. Where the bank has reasonable grounds for concluding that the institutional customer is making independent investment decisions and is capable of independently evaluating investment risk, then a bank's obligations under § 208.25(d) for a particular customer are fulfilled.[8] Where a customer has delegated decision-making authority to an agent, such as an investment advisor or a bank trust department, the interpretation in this section shall be applied to the agent.

(h) A determination of capability to evaluate investment risk independently will depend on an examination of the customer's capability to make its own investment decisions, including the resources available to the customer to make informed decisions. Relevant considerations could include:

(1) The use of one or more consultants, investment advisers, or bank trust departments;

(2) The general level of experience of the institutional customer in financial markets and specific experience with the type of instruments under consideration;

(3) The customer's ability to understand the economic features of the security involved;

(4) The customer's ability to independently evaluate how market developments would affect the security; and

(5) The complexity of the security or securities involved.

(i) A determination that a customer is making independent investment decisions will depend on the nature of the relationship that exists between the bank and the customer. Relevant considerations could include:

[7] The interpretation in this section does not address the obligation related to suitability that requires that a bank have''* * * a 'reasonable basis' to believe that the recommendation could be suitable for at least some customers.'' In the Matter of the Application of F.J. Kaufman and Company of Virginia and Frederick J. Kaufman, Jr., 50 SEC 164 (1989).

[8] *See* footnote 7 in paragraph (d) of this section.

(1) Any written or oral understanding that exists between the bank and the customer regarding the nature of the relationship between the bank and the customer and the services to be rendered by the bank;

(2) The presence or absence of a pattern of acceptance of the bank's recommendations;

(3) The use by the customer of ideas, suggestions, market views and information obtained from other government securities brokers or dealers or market professionals, particularly those relating to the same type of securities; and

(4) The extent to which the bank has received from the customer current comprehensive portfolio information in connection with discussing recommended transactions or has not been provided important information regarding its portfolio or investment objectives.

(j) Banks are reminded that these factors are merely guidelines that will be utilized to determine whether a bank has fulfilled its suitability obligation with respect to a specific institutional customer transaction and that the inclusion or absence of any of these factors is not dispositive of the determination of suitability. Such a determination can only be made on a case-by-case basis taking into consideration all the facts and circumstances of a particular bank/customer relationship, assessed in the context of a particular transaction.

(k) For purposes of the interpretation in this section, an institutional customer shall be any entity other than a natural person. In determining the applicability of the interpretation in this section to an institutional customer, the Board will consider the dollar value of the securities that the institutional customer has in its portfolio and/or under management. While the interpretation in this section is potentially applicable to any institutional customer, the guidance contained in this section is more appropriately applied to an institutional customer with at least $10 million invested in securities in the aggregate in its portfolio and/or under management.

APPENDIX A TO PART 208—CAPITAL ADEQUACY GUIDELINES FOR STATE MEMBER BANKS: RISK-BASED MEASURE

I. Overview

The Board of Governors of the Federal Reserve System has adopted a risk-based capital measure to assist in the assessment of the capital adequacy of state member banks.[1] The principal objectives of this measure are to: (i) Make regulatory capital requirements more sensitive to differences in risk profiles among banks; (ii) factor off-balance sheet exposures into the assessment of capital adequacy; (iii) minimize disincentives to holding liquid, low-risk assets; and (iv) achieve greater consistency in the evaluation of the capital adequacy of major banks throughout the world.[2]

The risk-based capital guidelines include both a definition of capital and a framework for calculating weighted risk assets by assigning assets and off-balance sheet items to broad risk categories. A bank's risk-based capital ratio is calculated by dividing its qualifying capital (the numerator of the ratio) by its weighted risk assets (the denominator).[3] The definition of qualifying capital is outlined below in section II, and the procedures for calculating weighted risk assets are discussed in Section III. Attachment I illustrates a sample calculation of weighted risk assets and the risk-based capital ratio.

In addition, when certain banks that engage in trading activities calculate their risk-based capital ratio under this appendix A, they must also refer to appendix E of this part, which incorporates capital charges for

[1] Supervisory ratios that relate capital to total assets for state member banks are outlined in appendix B of this part and in appendix B to part 225 of the Federal Reserve's Regulation Y, 12 CFR part 225.

[2] The risk-based capital measure is based upon a framework developed jointly by supervisory authorities from the countries represented on the Basle Committee on Banking Regulations and Supervisory Practices (Basle Supervisors' Committee) and endorsed by the Group of Ten Central Bank Governors. The framework is described in a paper prepared by the BSC entitled ''International Convergence of Capital Measurement,'' July 1988.

[3] Banks will initially be expected to utilize period-end amounts in calculating their risk-based capital ratios. When necessary and appropriate, ratios based on average balances may also be calculated on a case-by-case basis. Moreover, to the extent banks have data on average balances that can be used to calculate risk-based ratios, the Federal Reserve will take such data into account.