March 26, 2007

Nancy M. Morris
Secretary
Securities and Exchange Commission
100 F. Street, NE
Washington, D.C. 20549-1090

Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, D.C. 20551

Re: Definitions of Terms and Exemptions Relating to the "Broker" Exemptions for Banks; SEC Regulation R; Federal Reserve Docket No. R-1274; SEC File Number S7-22-06

Dear Ms. Morris and Ms. Johnson:

The Independent Community Bankers of America (ICBA)[1] appreciates the opportunity to comment on proposed rules that will implement the exceptions that banks have from the definition of the term "broker" under Section 3(a)(4) of the Securities Exchange Act of 1934 (Exchange Act) as amended by the Gramm-Leach-Bliley Act ("GLBA"). The proposed rules, jointly issued by the Securities and Exchange Commission (SEC) and the Federal Reserve Board (Federal Reserve), would define terms used in these statutory exceptions and include certain related exemptions.

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[1]*The Independent Community Bankers of America represents the largest constituency of community banks of all sizes and charter types in the nation, and is dedicated exclusively to representing the interests of the community banking industry. ICBA aggregates the power of its members to provide a voice for community banking interests in Washington, resources to enhance community bank education and marketability, and profitability options to help community banks compete in an ever-changing marketplace.*

With nearly 5,000 members, representing more than 18,000 locations nationwide and employing over 265,000 Americans, ICBA members hold more than $876 billion in assets $692 billion in deposits, and more than $589 billion in loans to consumers, small businesses and the agricultural community. For more information, visit ICBA's website at www.icba.org.

Background

Prior to the passage of GLBA in 1999, banks were specifically excluded from the definition of "broker" contained in the Exchange Act and could engage in securities sales activities without registering as a broker with the SEC. With the enactment of GLBA, banks are excluded from the definition of 'broker" only to the extent that their securities sales activities fall into one or more of the eleven statutory functional exceptions. Each of these exceptions permits a bank to act as an agent with respect to specified securities products or in transactions that meet specific statutory conditions. The exceptions were adopted to allow banks to continue to conduct traditional banking activities that involve securities transactions without becoming subject to broker registration. In particular, the Exchange Act provides conditional exceptions for banks that engage in networking arrangements; trust and fiduciary activities; permissible securities transactions; certain stock purchase plans; sweep accounts; affiliate transactions; private securities offerings; safekeeping and custody activities; municipal securities; and de minimis transactions.

In 2001, the Commission adopted interim final rules (the "Interim Rules") to implement these exceptions.[2] The Interim Rules were suspended after the trade associations, members of the banking industry, and bank regulators expressed serious concerns about the compliance burdens of the new rules, including their impact on traditional bank activities. In 2004, the SEC proposed a new set of rules known as SEC Regulation B that were heavily criticized by ICBA and other industry groups for taking a narrow interpretation of the statutory "broker" exceptions. ICBA said that proposed Regulation B was so burdensome, unnecessarily complicated and restrictive, that it would force many banks—especially community banks—to discontinue existing services to the detriment of their customers.

In 2006, Congress passed the ICBA-endorsed Financial Services Regulatory Relief Act of 2006 which included a requirement that the Federal Reserve Board and the SEC jointly issue proposed rules to implement the broker exceptions within 180 days of the law's enactment. As a result, the SEC and the Federal Reserve have jointly issued proposed SEC Regulation R that implement the broker exceptions for banks relating to third-party networking arrangements, trust and fiduciary activities, sweep activities, and safekeeping and custody activities.

ICBA's Position Concerning Proposed Regulation R

ICBA commends the SEC and the Federal Reserve for issuing rules that are significantly more flexible, simple and accommodative than any of the previous proposals, including proposed Regulation B. The rules allow banks to continue conducting traditional banking activities that involve securities activities while including adequate safeguards to protect investors. Although we have several recommendations for improving the rules, in general, ICBA believes that the rules are flexible enough that most community banks will be able to comply with them without significantly altering

[2] Bank Broker-Dealer Interim Final Rules, Release No. 34-44291, 66 Fed. Reg. 27760 (May 18, 2001).

1615 L Street NW, Suite 900, Washington, DC 20036 ▪ (800)422·8439 ▪ FAX: (202)659·3604 ▪ Email: info@icba.org ▪ www.icba.org

any of their third party networking arrangements or any of their traditional banking activities involving securities activities.

Networking Arrangements

The statutory "networking" exception under GLBA permits bank employees to refer customers to a broker-dealer subject to several conditions that are designed, among other things, to help ensure customers receive adequate disclosures concerning the uninsured nature of securities products offered by the broker-dealer and to prevent unqualified bank personnel from providing investment advice or engaging in other inappropriate sales activities. One of these statutory conditions generally prohibits a bank employee that refers a customer to a securities broker from receiving "incentive compensation" for a securities brokerage transaction other than a "nominal" one-time fee for making the referral that is not contingent on whether the referral results in a securities transaction.

Proposed SEC Regulation R defines "nominal" to mean a referral fee that meets one of three alternative standards. Under the first alternative, a referral fee is considered nominal if it does not exceed either twice the average of the minimum and maximum hourly wage established by the bank for the current or prior year for the job family (e.g., tellers, loans officers, etc.) that includes the relevant employee, or $1/1000^{th}$ of the average of the minimum and maximum annual base salary established by the bank for the current or prior year for the job family that includes the relevant employee. Under the second and third alternatives, a referral fee is considered "nominal" if it does not exceed twice the employee's actual base hourly wage or twenty-five dollars adjusted for inflation every five years.

ICBA commends the SEC and the Federal Reserve for including a specific dollar amount as one of the alternative standards. Most community banks will likely use the specific dollar standard since it is so simple and does not require any computation of employee wages. **However, as we stated in our comment letter regarding Regulation B, $25 is too low. We suggest $30 as the standard since this would accommodate most community bank third party referral programs.**

ICBA also commends the SEC and the Federal Reserve for excluding certain types of bonus compensation from the definition of "incentive compensation" so that community banks with third party referral programs will not have to significantly modify their bonus programs. Under the proposal, bonus programs are excluded as long the bonuses are paid on a discretionary basis and are based on multiple factors or variables including those not related to securities transactions. Banks can also pay employees on the basis of the overall profitability of the bank, any bank affiliate, or the broker or dealer provided that such profitability is only one of multiple factors or variables used to determine the compensation of the employee.

Proposed Regulation R also includes an exemption that would permit a bank to pay an employee a contingent referral fee of more than a nominal amount for referring to a broker or dealer an institutional customer or high net worth customer with which the bank has a contractual or other written networking arrangement. Even though most community banks will likely rely on the "nominal" fee exemption in lieu of this exemption, we support the proposed exemption for institutional or high net worth customers since these customers are clearly able to understand and evaluate the relationship between the bank and its broker-dealer.

Trust and Fiduciary Activities Exception

GLBA allows a bank to effect securities transactions for its trust and fiduciary customers so long as, among other things, the bank is "chiefly compensated" for these transactions by (i) administration fees, (ii) annual fees (iii) fees based on a percentage of assets under management, (iv) flat or capped per order processing fees that do not exceed the bank's cost for executing the transactions, or (v) any combination of these fees. These fees are referred to as "relationship compensation."

Proposed SEC Regulation R would provide banks two alternative methods for complying with the statute's "chiefly compensated" test:

(1) *Bank-wide test*. Under this test, a bank would meet the "chiefly compensated" test if the aggregate amount of relationship compensation the bank received from all of its trust and fiduciary accounts on a bank-wide basis during the preceding two years equals or exceeds 70% of the total compensation attributable to all of the bank's trust and fiduciary accounts during those years (after the annual ratio for both years are averaged together).
(2) *Account by account test*. The account-by-account test is structured similarly, except that a bank must separately compare the relationship compensation and total compensation attributable to each trust or fiduciary account individually rather than on a bank-wide basis. If a bank decides to follow this approach, the relationship compensation attributable to each trust or fiduciary account must represent 50% or more of the bank's total compensation from the account.

ICBA applauds the SEC and the Federal Reserve for incorporating our recommendations with regard to the "chiefly compensated" test. In our comment letter concerning proposed Regulation B, we suggested using a ratio of between 51% and 75% as a bank-wide test particularly since there is nothing in GLBA that indicates that relationship compensation needs to be higher than 51% of total compensation. We also thought that comparing relationship compensation to total compensation was much simpler than comparing sales compensation to relationship compensation.

ICBA also commends the SEC and the Federal Reserve for defining "relationship compensation" to include a wider range of fees customarily received by banks as compensation for trust or fiduciary services. For example, the term would include all Rule 12b-1, shareholder servicing and sub-accounting fees received from a mutual fund and attributable to the bank's trust or fiduciary accounts, as well as fees paid by trust and fiduciary accounts for personal services, tax preparation, real estate settlement and other administrative services. In our comment letter concerning Regulation B, we argued that 12b-1 fees do not create conflicts between banks and investors or create special incentives to distribute investment company securities. Banks receive 12b-1 fees from mutual funds to compensate them for the work involved in providing fund information to the customer and selling customer the fund. Furthermore, since a 12b-1 fee is a fee based on a percentage of assets, it should be considered "relationship compensation."

Sweep Accounts

The sweep accounts exception set out in the Exchange Act and GLBA permits a bank to participate in mixed product arrangements in which the bank offers a mutual fund "sweep" service linked to deposit accounts under certain conditions. Specifically, this section exempts a bank from the definition of "broker" to the extent it "effects transactions as part of a program for the investment or reinvestment of deposit funds into any no-load, open-end management investment company registered under the Investment Company Act that holds itself out as a money market fund."

To provide banks with guidance on the sweep accounts exception, proposed Regulation R defines various terms under the exception including the term "no-load." Under the proposal, a "no-load" mutual fund is a fund that (1) has no sales load or a deferred sales load; and (2) annually charges no more than 25 basis points against net assets to provide for sales-related expenses and service fees (including 12b-1 fees).

Recognizing that banks have long offered sweeps and other services that invest customer funds in money market funds that do not qualify as no-load, proposed Regulation R also provides a special exemption that would permit banks, without registering as a broker, to use loaded money market funds under certain conditions. **ICBA strongly endorses this exception for money market funds. As we stated in our letter concerning Regulation B, a 25 basis point restriction on what constitutes a "no-load" money market fund would cause community banks to discontinue current sweep arrangements and services they offer customers.** Administrative costs of implementation and servicing of sweep accounts is significant, especially for community banks that have lower aggregate account balances and fewer customers involved in the sweep function. An exception that would allow banks to use money market funds that charge over 25 basis points would allow many community banks to continue offering sweep arrangements.

Safekeeping and Custody Exception

The Exchange Act, as amended by GLBA, provides an exception from broker-dealer registration with respect to certain securities-related safekeeping and custody services that banks may perform for their customers. The exception explicitly allows a bank that holds funds and securities for its customers as part of "customary banking" activities to perform specified securities-related functions with respect to those securities without registering as a broker.

In particular, a bank may, among other things without registering as a broker, exercise warrants or other rights, facilitate the transfer of funds or securities in connection with clearing and settling customers' securities transactions, effect securities lending or borrowing transactions and invest cash collateral pledged in connection with such transactions, and hold securities pledged by a customer or facilitate the pledging or transfer of securities that involve the sale of those securities.

Proposed Regulation R includes an exemption that allows banks, subject to certain conditions, to accept orders for securities transactions from employee benefit plan accounts and individual retirement and similar accounts for which the bank acts as a custodian. In addition, the exemption allows banks, subject to certain conditions, to accept orders for securities transactions on an accommodation basis from other types of custodial accounts.

ICBA commends the SEC and the Federal Reserve for including an exemption for custody accounts and recognizing that accepting orders for the purchase or sale of securities has always been a core custody activity for banks. If a bank cannot accept orders from a customer on the disposition of securities the bank holds as custodian, including orders to purchase and sell, then there is little reason for a bank to serve as a custodian. ICBA also believes that the conditions on advertising and investment advice are reasonable requirements to prevent prohibited brokerage activity.

Proposed Exemptions for Contracts Entered Into by Banks; Proposed Regulation R Transition Period

ICBA strongly supports the proposed contract exemptions that are designed to protect banks from liability under the Exchange Act. Under these exemptions, (1) no contract entered into before eighteen months after the effective date of the proposed exemption would be voided by reason of Section 29 of the Exchange Act because any bank that is a party to the contract violated the registration requirements of the Exchange Act based solely on the bank's status as a broker when the contract was created, and (2) no contract would be voided by reason of Section 29(b) of the Exchange Act without a time limit if the bank acted in good faith when the contract was created and the violation of the registration requirements by the bank did not result in any significant harm, financial loss or cost to the person seeking to void the contract. We believe a bank acting in good faith which has reasonable policies and procedures in effect at the time a securities contract is created should not be subject to rescission claims as a result of an inadvertent failure to comply with the requirements under the Exchange Act.

ICBA also supports extending the effective date for banks to comply under the Exchange Act until the first day of the first fiscal year following June 30, 2008. Community banks will need that much time to change their policies and procedures and if necessary to revise their third party referral arrangements.

Conclusion

ICBA commends the SEC and the Federal Reserve for issuing rules that are significantly more flexible, simple and accommodative than any of the previous proposals, including proposed Regulation B. The rules allow banks to continue conducting traditional banking activities that involve securities activities while including adequate safeguards to protect investors. ICBA believes, in general, that the rules are flexible enough that most community banks will not have to significantly change their third party networking arrangements or how they conduct their securities activities. We support the proposed exemption for third party networking arrangements but recommend that $30 be used in lieu of $25 for purposes of defining a nominal referral fee.

With respect to the trust and fiduciary activities exemption, ICBA applauds the SEC and the Federal Reserve for incorporating our recommendations with regard to the "chiefly compensated" test and using a ratio of 75% for determining the bank-wide relationship between relationship compensation and total compensation and including Rule 12b-1 fees as part of relationship compensation. We strongly support the special sweep exemption for money market funds and allowing banks to sell securities as an accommodation to customers as part of the safekeeping and custody exemption. To help community banks comply with Regulation R, we support extending the effective date until the first day of the first fiscal year following June 30, 2008 for banks to come into compliance under the Exchange Act.

ICBA appreciates the opportunity to offer comments in connection with proposed SEC Regulation R to implement the bank exemptions under GLBA. If you have any questions about our letter, please do not hesitate to contact me at 202-659-8111 or Chris.Cole@icba.org.

Sincerely,

Christopher Cole

Christopher Cole

Regulatory Counsel