1000 Wilson Boulevard
Suite 2500
Arlington, VA 22209-3912

March 26, 2007

Via Electronic Delivery

Jennifer J. Johnson
Secretary of the Board
Board of Governors of the
Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, D.C. 20051

Nancy M. Morris
Secretary
Securities and Exchange Commission
100n F Street, N.E.
Washington, D.C. 20549

Re: Federal Reserve Docket No. R-1274: Regulation R
SEC Release No. 34-54946: 17 C.F.R. Parts 240 and 247

Ladies and Gentlemen:

This letter is submitted by the Consumer Bankers Association ("CBA") in response to the joint proposal of the Board of Governors of the Federal Reserve System (the "Board") and the Securities and Exchange Commission (the "Commission") (together, the "Agencies") requesting comment on proposed rules that would implement certain exceptions for banks from the definition of the term "broker" under Section 3(a)(4) of the Securities Exchange Act of 1934 (the "Exchange Act") and amended by the Gramm-Leach-Bliley Act (the "GLB Act") (the "Proposed Rules").[1]

CBA is the recognized voice on retail banking issues in the nation's capital. Member institutions are the leaders in consumer financial services, including auto finance, home equity lending, card products, education loans, small business services,

[1] 71 *Fed. Reg.* 77522 (December 26, 2006).

community development, investments and deposits. CBA was founded in 1919 and provides leadership, education, research and federal representation on retail banking issues such as privacy, fair lending, and consumer protection legislation and regulation. CBA members include most of the nation's largest bank holding companies as well as regional and super community banks that collectively hold two-thirds of the industry's total assets. CBA appreciates the opportunity to offer its comments on the Proposed Rules.

CBA believes that the Proposed Rules represent a marked improvement from the Commission's previous proposals. CBA believes that the Proposed Rules more closely reflect the language of the GLB Act and Congressional intent when it revised the definition of the term "broker" in the Exchange Act. Although Congress narrowed the exception for banks, Congress believed it important to permit banks to continue to act as agents with respect to certain specific products and to engage in transactions that meet certain statutory conditions.[2] In order to accommodate existing business practices and avoid disrupting certain securities transaction services arising from the provision of trust, fiduciary, custodial and other banking services, the GLB Act provides eleven specific exceptions for banks from the definition of "broker."

The Proposed Rules address four of the eleven exceptions. In addition, the Proposed Rules include exemptions related to foreign securities transactions, securities lending transactions conducted in an agency capacity and execution of transactions involving mutual fund shares. The Agencies request comment on whether it would be useful or appropriate for them to propose rules relating to the remaining exceptions. CBA believes that the statutory language of the remaining exceptions are sufficiently clear such that no additional clarification is needed. Accordingly, CBA believes that there is no need at this time for the Agencies to propose any additional rules relating to the remaining exceptions.

The Agencies also indicate that the banking agencies will be developing recordkeeping rules for banks that operate under the broker exceptions. CBA looks forward to the opportunity to comment on these rules when they are proposed by the banking agencies.

CBA is pleased to provide the following comments on the Proposed Rules.

NETWORKING ARRANGEMENTS

The networking exception permits bank employees to receive a nominal one-time cash fee of a fixed dollar amount if the payment of the fee is not contingent on whether the referral results in a transaction. Exchange Act § 3(a)(4)(B)(i)(VI). However § __.700(a) of the Proposed Rules provides that the term "contingent on whether the referral results in a transaction" means <u>dependent</u> on whether the referral results in a purchase or sale of a security; whether an account is opened with a broker or dealer; . . ." (Emphasis added.) CBA believes that the Agencies should use the term "contingent"

[2] Exchange Act § 3(a)(4)(B) as amended by § 201 of the GLB Act. 15 U.S.C. § 78c(a)(4)(B).

rather the term “dependent.” The Exchange Act uses the term “contingent,” not “dependent.” Given the complexity of the Proposed Rules, CBA believes that it is undesirable to use different terminology to define the term “contingent,” a term that CBA believes is sufficiently precise. Accordingly, CBA requests that the Agencies employ the term used by Congress rather than resorting to different terminology that may be subject to different interpretations.

CBA also believes that the term “contingent on whether the referral results in a transaction” should not include “whether an account is opened with a broker or dealer.” The usual and customary meaning of the term “transaction” is “an exchange of goods, services or funds.”[3] CBA believes that opening an account should not be regarded as a transaction under the Proposed Rules because it does not necessarily result in a purchase or sale of securities by the customer and will not encourage employees to engage in impermissible securities sales practices. CBA believes that additional support for this position is found in the Proposed Rules definition of the term “referral,” which means “action taken to direct a customer of the bank to a broker or dealer for the purchase or sale of securities for the customer’s account.” Under the Proposed Rules, therefore, an employee’s referral resulting in the customer’s simply opening an account with the broker-dealer is not a referral. CBA believes that opening an account is similar to, and should be regarded in the same manner as, situations in which the customer contacts or keeps an appointment with the broker-dealer, or otherwise meets certain criteria established by the broker-dealer for customer referrals.

The Proposed Rules also indicate that a referral fee may be contingent on whether a customer contacts or keeps an appointment with a broker-dealer as a result of the referral or meets any objective, base-line qualification criteria established for customer referrals. CBA agrees that referrals under such circumstances should be permitted. However, CBA believes that the Proposed Rules should make it clear that such referrals are not exclusive and are only examples of the circumstances under which referral fees may be contingent. The Proposed Rules should also indicate that referral fees may be contingent upon the customer satisfying other criteria so long as the contingency does not relate to a purchase or sale of a security.

Referral Fee Determination

The Proposed Rules provide that the term “nominal one-time cash fee of a fixed dollar amount” would be defined as cash payment for a referral in an amount that meets one of three alternative standards. The first alternative would permit a cash payment in the amount of up to (a) twice the average of the bank’s minimum and maximum hourly wage, or (b) 1/1000th of the average of the bank’s minimum and maximum annual base salary for the current or prior year for the employee’s job family. The second alternative permits a payment that does not exceed twice the employee’s actual base hourly wage. The third option permits the bank to pay a $25 fee, adjusted over time for inflation.

[3] Merriam Webster’s Online Dictionary at www.m-w.com/dictionary/transaction

CBA notes that in connection with the Commission's previous proposal, the Board and the other Federal banking agencies (the "Banking Agencies") urged the Commission not to establish a fixed definition of what constitutes a "nominal" referral fee.[4] The Banking Agencies' comment noted that whether a referral fee paid in a particular instance is nominal depends upon a wide variety of factors. Accordingly, the Banking Agencies advised that the determination of whether a referral fee is nominal is best made in the context of the supervision and examination process, in light of all relevant circumstances. This, the Banking Agencies noted, is the way the Commission and the SROs historically have monitored the "nominal" requirement embodied in Commission staff no-action letters, on which the networking exception is based. In addition, this is the approach relied upon by the Banking Agencies in monitoring the "nominal" fee element in the Interagency Statement on the Retail Sale of Nondeposit Investment Products.[5] In light of these precedents, CBA believes that what constitutes a "nominal, one time cash fee" should be left to the determination of the banking agencies rather than the fixed standard contained in the Proposed Rules.

In the event the Agencies determine to adopt the Proposed Rules, CBA requests that the Agencies clarify that use of the term "hourly wage" does not mean that the alternative may be used only for employees whose wages are computed on an hourly basis. Rather, a bank should be permitted to convert the annual base salary for a job family or for an employee to an hourly rate and use that rate to compute the applicable referral fee. CBA also requests that the Proposed Rules clarify that a bank is not required to choose one alternative, but may use all of the options during the course of the year as it sees fit. The Agencies should also clarify that the payment may be made to the employee by the bank or by the broker.

The Proposed Rules provide that the term "referral" means the action taken by an employee to direct a customer of the bank to a broker-dealer for the purchase or sale of securities for the customer's account. While CBA recognizes that the Exchange Act uses the term "customer" in connection with the networking exception, CBA believes that the term customer should be defined to include any person, regardless of whether the person maintains an account with the bank at the time of the referral. Frequently, a person who does not maintain an account may contact a bank employee to inquire about various products and services. CBA believes that an employee should be permitted to obtain a fee for referring such a person to the broker-dealer in accordance with the Proposed Rules.

The Proposed Rules define "incentive compensation" to exclude compensation paid under a bonus or similar plan if it is paid on a discretionary basis, is based on multiple factors or variables and (a) includes significant factors or variables that are not related to securities transactions at the broker-dealer; (b) an employee referral is not a factor or variable; and (c) the employee's compensation is not determined by reference to

[4] See Letter of October 8, 2004 to Securities Exchange Commission from Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation and Office of the Comptroller of the Currency, Appendix at 29. ("Banking Agencies Comment")
[5] Federal Reserve Regulatory Service, ¶ 3-1579.51.

referrals by other persons. This provision clarifies that compensation may be based upon the overall profitability of the bank, an affiliate or the broker-dealer (subject to certain factors). CBA supports this clarification. Compensation plans based upon the factors and variables specified in the clarification would not provide inappropriate incentives for employees. In this regard, CBA asks that the Agencies indicate that in applying the profitability factor, institutions may use the performance of an operating unit of the institution as an alternative to the overall profit of the organization. CBA also requests the further clarification that the networking exception applies to payments made to the bank's officers and directors as well as employees who are not officers and directors. CBA believes that a bank should be permitted to pay referral fees to the bank's officers and directors. This clarification could be achieved by defining the term "employee" to include officers and directors.

Non-Cash Payments

In its June 2004 proposed rules, the Commission proposed to permit the payment of the "nominal one-time cash fee" in the form of non-cash payments, so long as the value of the non-cash payment was readily ascertainable.[6] The Proposed Rules however do not provide for the payment of a fee by means of non-cash payments such as point accruals. No explanation was provided in the Agencies' *Federal Register* notice as to why the option to use non-cash payments was eliminated. Many institutions find that non-cash payments are an important method for providing incentives to employees. Accordingly, CBA believes that the Agencies' should permit financial institutions to provide incentive compensation to employees through the use of non-cash payments such as points. The Agencies should also permit institutions to integrate incentive programs in the form of non-cash payments into other incentive programs that offer rewards for activities unrelated to securities.

High Net Worth and Institutional Customers

The Proposed Rules also permit a bank to pay a contingent referral fee of more than a nominal amount to an employee for referring a "high net worth" customer or "institutional" customer to a broker-dealer with which the bank has a written arrangement, subject to certain conditions. CBA believes that this additional exception is appropriate given the nature of the customers, and is consistent with Congressional intent.

<u>Definition of High Net Worth and Institutional Customers</u>

A high net worth customer would be defined as a person who, individually or with a spouse, has at least $5 million in net worth, excluding the person's primary residence and associated liabilities. Assets the person holds individually and 50 percent of assets held jointly with a spouse, as well as assets held as community property, may be included in the calculation. If the person and the spouse act jointly, each person's assets may be included in the calculation, regardless of whether the assets are held jointly.

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[6] 69 *Fed. Reg.* 39682, 39688 (June 30, 2004).

CBA believes that the proposed $5 million net worth level is too high. In private banking, a person is regarded as possessing high net worth if his or her net worth (excluding primary residence) is $1 million or more.[7] Moreover, the Commission's rules provide that for purposes of determining whether a person comes within the Regulation D safe harbor for non-public offering, an accredited investor is one whose individual net worth, or joint net worth with a spouse, exceeds $1 million.[8] If the Commission and the Board believe that the $1 million threshold is appropriate to determine who are high net worth individuals for other similar purposes, CBA believes that the same level should be established for purposes of the Proposed Rules.

The Proposed Rules also define an "institutional customer" as an organization that has at least $10 million in investments or $40 million in assets, or $25 million in assets if the referral is for investment banking services. Again, CBA believes that this level is set far too high. CBA recommends that the Agencies look to the Commission's Regulation D, which generally establishes a $5 million level for an organization to qualify as an accredited investor.[9]

<u>Determination</u>

The Proposed Rules also provide that a bank would be required to determine that an organization qualifies as an institutional investor before the referral fee is paid to the employee. However, a bank would be required to determine that an individual is a high net worth customer before or at the time of any referral. CBA believes that the standard applicable to institutional investors should be applied to high net worth individuals as well. There is no logical reason why a different standard should apply to individuals and institutional investors. Because the statutory networking exception permits an employee to refer a bank customer to a broker-dealer, the only issue is whether additional compensation in excess of a nominal fee is permitted to be paid to the employee. If it is determined that a customer is not a high net worth individual, then only a nominal fee may be paid to the employee for the referral. As a result, CBA sees no reason why the determination cannot be made prior to the payment of the referral fee to the employee. Moreover, it may be extremely difficult if not impossible in certain settings for a bank employee to provide prospective customers with the required disclosures prior to the time of referral. For example, if an employee encounters a prospect on a golf outing or at a social gathering, during which the conversation turns to a discussion of business, it would seem highly inappropriate and quite cumbersome for the bank employee to pull out a disclosure form and provide it to the prospect.

The Proposed Rules also indicate that the written agreement between the bank and the broker-dealer also must require the broker-dealer to determine whether a customer is a high net worth customer or an institutional customer. CBA believes that requiring both

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[7] Federal Reserve Commercial Bank Examination Manual ¶ 4128.1 at 2. ("Typically, private-banking customers are high net worth individuals or institutional investors who have minimum investible assets of $1 million or more.").
[8] 17 C.F.R. § 230.501(a)(5).
[9] 17 C.F.R. § 230.501(a)(3).

the bank and the broker-dealer to make such a determination is unnecessary, duplicative and serves no useful purpose. Moreover, such a duplicative requirement runs the risk of alienating customers who may be required to submit the same information again to the broker-dealer and may be subjected twice to the same inquiries. To avoid such a waste of resources, CBA believes that the Proposed Rules should provide that the bank and broker-dealer may rely upon the information received and conclusions reached by the other party as to whether the customer is a high net worth individual or institutional customer.

Ordinary Course of Assigned Duties

The Proposed Rules also require that the employee encounter the high net worth customer or institutional customer in the ordinary course of the employee's assigned duties for the bank. Given the nature of banking, it often may be difficult to draw a bright line in applying this standard. For example, a meeting with a customer on a golf course or at a sporting event which leads to a referral should be regarded as within the scope of the employee's assigned duties. Accordingly, CBA believes that the Proposed Rules should clarify that encountering such customers under circumstances that are not primarily intended to result in referrals to broker-dealers, such as social events, would be within the scope of the employee's assigned duties.

The Proposed Rules also require that before a referral fee may be paid to the employee, the bank must provide the broker-dealer with the employee's name in order for the broker-dealer to determine whether the employee is associated with a broker-dealer or is subject to a statutory disqualification. The Proposed Rules suggest that the broker-dealer must make such a determination each time the employee makes a referral. In order to conserve resources and prevent duplicative, unnecessary inquiries, CBA believes that the Proposed Rules should permit a broker-dealer to perform the required inquiry regarding the employee once a year, unless information regarding a change in the employee's status comes to the broker-dealer's attention before that time.

Suitability and Sophistication Analysis

The Proposed Rules also require that the agreement between the bank and the broker-dealer provide that the broker-dealer will make a suitability or sophistication determination depending upon whether the referral fee is contingent on the completion of a securities transaction. For contingent fees, a broker-dealer must conduct a suitability analysis of the securities transaction that triggers the contingent fee in accordance with the rules of the broker-dealer's SRO as if the broker dealer had recommended the securities transaction. This analysis must be performed before each securities transaction. For non-contingent referral fees, the broker-dealer must conduct either a sophistication analysis of the customer or a suitability analysis with respect to all securities transactions requested by the customer contemporaneously with the referral before a referral fee is paid to the employee. CBA sees no reason why these provisions should be required to be incorporated into the agreement between the bank and the broker-dealer, in particular because the bank does not have the ability to monitor the broker-dealer's compliance with such a requirement. If the Agencies believe that a broker-dealer should conduct a sophistication or suitability analysis of high net worth or institutional customers, CBA believes that the requirement should be established by the broker-dealer's SRO.

Referral Fee

The Proposed Rules provide that a referral fee may be a predetermined dollar amount or an amount determined in accordance with a predetermined formula (e.g., assets placed in the customer's account) that does not vary based upon the revenue generated by, or the profitability of the transactions conducted by the customer. However, the Proposed Rules permit the payment of a referral fee to be based upon a fixed percentage of the revenue received by the broker-dealer for providing investment banking services. CBA believes that a fee for referring customers to a broker-dealer should be based upon a fixed percentage of the revenue received by the broker-dealer regardless of the type of service provided. CBA believes that permitting a referral fee to be computed in such a manner will not result in the employee having a "salesman's stake" in the transaction because the employee is simply referring the customer to the broker-dealer and is not recommending that the customer purchase or sell any type or amount of securities.

TRUST AND FIDUCIARY ACTIVITIES

The Exchange Act provides that a bank is not considered to be a broker because it effects transactions in a trustee capacity, or effects transactions in a fiduciary capacity in its trust department (or other department regularly examined for compliance with fiduciary principles and standards) if the bank is "chiefly compensated" for such transactions on the basis of (a) an administration or annual fee; (b) a percentage of assets under management; (c) a flat or capped per-order processing fee equal to the bank's cost; or (d) or any combination of such fees.[10] These fees are referred to in the Proposed Rules as "relationship compensation."

CBA believes that the Proposed Rules relating to the trust and fiduciary activities exception substantially meet the provisions of the exception set forth in the Exchange Act and fulfill Congressional intent. However, CBA has the following comments on the Trust and Fiduciary Activities Exception.

Chiefly Compensated

The Proposed Rules provide that a bank meets the "chiefly compensated" test if the "relationship-total compensation percentage" for each trust or fiduciary account is greater than 50 percent. The "relationship-total compensation percentage" is the arithmetic mean of the "yearly compensation percentage" for the account for the immediately preceding year and for the year immediately preceding that year. The "yearly compensation percentage" is the relationship compensation attributable to the

[10] Exchange Act, § 3(a)(4)(B)(ii).

trust or fiduciary account during the year divided by the total compensation attributable to the account during that year. CBA believes that banks should be granted a greater degree of flexibility in calculating the relationship-total compensation percentage. CBA believes that rather than requiring a bank to compute the average of two percentages, banks should have the flexibility to aggregate both years' relationship compensation and total compensation and compute one percentage based upon the aggregate amount of compensation. This approach would simplify the periodic calculation and ensure that a fluctuation in volume does not have an unusual effect on the average percentage.

The Proposed Rules define relationship compensation as (a) administration fees; (b) annual fees; (c) a fee based on a percentage of assets under management; (d) a flat or capped per-order processing fee, <u>paid by or on behalf of a customer or beneficiary</u>, that is equal to not more than the cost incurred by the bank in connection with executing securities transactions for trust or fiduciary accounts; or (e) a combination of the above. The Exchange Act exception for trust and fiduciary activities does not contain the phrase "paid by or on behalf of a customer or beneficiary." Adding such a requirement is potentially confusing. Accordingly, CBA sees no reason why such a condition should be added to the unambiguous statutory language.

CBA also requests that the Agencies clarify that the phrase "cost incurred by the bank in connection with executing securities transactions for trust and fiduciary accounts" includes fixed as well as marginal costs in developing and maintaining shared systems for handling securities transactions for trust and fiduciary and other customers. Permitting banks to recover fixed as well as marginal costs enables them to recover the actual costs incurred as permitted by the Exchange Act. CBA believes the Agencies should expressly indicate that banks will be permitted to include their average costs for effecting securities transactions for trust and fiduciary and other customers in a per-order processing fee.

The Proposed Rules provide an alternate test that permits a bank to calculate compensation it receives from all of its trust and fiduciary accounts on a bank-wide basis. However, the bank's aggregate relationship-total compensation percentage must be at least 70 percent. (The aggregate relationship-total compensation percentage is the mean of the bank's yearly bank-wide compensation percentage for the immediately preceding two years.) The yearly bank-wide compensation percentage is the relationship compensation attributable to the bank's trust and fiduciary business during the year divided by the total compensation attributable to the bank's trust and fiduciary business during the year.

CBA believes that requiring the bank's aggregate relationship-total compensation amount to be at least 70 percent is too high. If "greater than 50 percent" is established as the appropriate level for the "chiefly compensated" when a bank uses the account-by-account test, CBA believes that "greater than 50 percent" should be the test when using the bank-wide test. CBA believes there is no reason why a significantly higher number should be used simply because a bank chooses to aggregate its compensation and use the bank-wide test rather than use the account-by-account test. In their 2004 comment to the

Commission on its previous proposal, the Banking Agencies stated that the Exchange Act itself establishes a 49 percent limit on the maximum compensation percentage that a bank could receive from fees that do not qualify as relationship compensation. Accordingly, the Banking Agencies urged the Commission to adopt a limit of 49 percent. CBA believes that the arguments set forth in the Banking Agencies' Comment continue to apply. Banks need meaningful "headroom" so that their trust and fiduciary business is not adversely affected by normal economic fluctuations and developments. A 70 percent level for aggregate relationship-total compensation will simply not accommodate the diverse trust and fiduciary operations and business lines.

In addition, CBA believes that banks should also be permitted to aggregate the compensation over the prior two years rather than use the average of yearly numbers. Such an option would facilitate ease of calculation and would help smooth out unusual compensation that may have been received during one of the two years.

The Exchange Act provides that a bank may not publicly solicit brokerage business other than by advertising that it effects transactions in securities in conjunction with advertising its other trust activities. The term "advertising" is defined in the Proposed Rules as any material that is published or used in any electronic or public media including a website.[11] CBA requests that the Agencies clarify that the term "electronic media" does not include material that may appear in e-mails that a bank may send to its customers relating to customer transactions and accounts. Because e-mails sent to customers are typically related to specific transactions engaged in by the customer, CBA believes that use of such a communication does not, and should not, come within the definition of advertising.

Exemption for New and Transferred Accounts

The Proposed Rules permit a bank to exclude any trust or fiduciary account from its compensation calculation if the account had been open for less than three months, or if the account had been acquired from another person as part of a merger, consolidation, acquisition purchase of assets or similar transaction for 12 months after the date of the transaction. CBA supports this exemption, but recommends that the time frame for a new account be extended to 12 months. Banks find that it often takes one year to achieve an orderly administration of new accounts and fully integrate them into the operations of the trust department. Using 12 months for both new and acquired accounts will simplify compliance and facilitate a bank's operational needs without compromising the goals of the Exchange Act.

Trustee for Self-Directed IRAs

The trust and fiduciary exception permits a bank to effect securities transactions in a trustee capacity without being registered as a broker if the transactions are effected in the institution's trust department or other department that is regularly examined by bank

[11] §_.760(g)(2).

examiners for compliance with fiduciary principles and standards.[12] As the Agencies are aware, insured depository institutions are permitted to act as trustees of Individual Retirement Accounts ("IRAs") without being subjected to requirements that ordinarily will apply to depository institutions when exercising fiduciary powers.[13] When acting in an exempt fiduciary capacity, depository institutions generally may invest the funds of the fiduciary account only in the institutions' deposits, obligations or securities, or other assets as their customers may direct, provided the institutions do not provide investment advice for the accounts.[14] Such institutions, of course, will not have separate trust departments. It is unclear whether the Agencies would regard the examinations conducted by bank examiners of the institution's activities as trustee for self-directed IRAs as "a department that is regularly examined by bank examiners for compliance with fiduciary principles and standards."

CBA believes that the Agencies should expressly indicate that for institutions serving as trustee for self-directed IRAs and which do not maintain a trust department, the regular safety and soundness or compliance examination of the institution will meet the examination requirement of the trust and fiduciary exception. Agency examination procedures provide for a review of the institution's practices in connection with serving as trustee for self-directed IRAs.[15] Alternatively, the Agencies could determine that an institution acting as trustee for self-directed IRAs is virtually equivalent to the institution acting as a custodian. As a result, the Agencies could provide that the safekeeping and custody exception includes institutions that act as trustees for self-directed IRAs in accordance with the regulations of the Federal banking agencies. CBA is concerned that if the Agencies do not expressly address this issue, institutions acting as trustee for self-directed IRAs may be uncertain as to whether they may continue to provide IRA customers services Congress intended in the GLB Act.

SWEEP ACCOUNTS AND MONEY MARKET FUNDS

The Proposed Rules implement the Exchange Act exception that permits banks to invest deposits into no-load, money market funds. The term "no-load" is defined as securities, or a class or series of securities that are not subject to a sales load, or a deferred sales load, and total charges against net assets of that class or series of securities for sales or sales promotion expenses, for personal service, or for maintenance of shareholder accounts does not exceed 0.25 percent annually of the fund's average net assets. The Proposed Rules provide that seven types of charges are not included in the 0.25 percent calculation. CBA is concerned that the requirement that total charges against net assets for sales or sales promotion expenses, for personal service, or for maintenance of shareholder accounts not exceed 0.25 percent needlessly complicates the ability of banks to use this exception. For ease of compliance, CBA believes that the

[12] 15 U.S.C. § 78c(a)(4)(B)(ii).
[13] 12 U.S.C. § 1464(l) (Federal savings associations); 12 C.F.R. § 550.580 (state and Federal savings associations); 12 C.F.R. § 333.101(b) (state nonmember banks); Federal Reserve Regulatory Service ¶ 3-432 (S-2283, May 20, 1975) (state member banks).
[14] 12 C.F.R. § 550.600.
[15] FDIC Trust Examination Manual, Section 2.O; OTS Trust and Asset Management Handbook, § 300.23; Federal Reserve Board Commercial Bank Examination Manual § 4170.1.

Banking Agencies' Comment provided a better resolution of what constitutes a money market fund. In their comment letter, the banking agencies encouraged the Commission to define a no-load fund as a fund that does not charge a sales load or deferred sales load, and not include reference to 0.25 percent sales related expenses.[16] Such a definition of no-load would simplify bank compliance with the proposed exception and avoid providing additional needless paperwork.

In addition, CBA requests that the Agencies clarify that the exception permits a bank to provide sweep services for deposits held at other banks. Nothing in the Exchange Act indicates that the sweep exception applies only to sweeps involving deposits at the bank. Moreover, the Proposed Rules do not appear to preclude such a result. CBA believes that confirmation of this reading of the Exchange Act and the Proposed Rules would be helpful to banks.

SAFEKEEPING AND CUSTODY

The Proposed Rules provide an exception from the definition of the term "broker" for a bank that accepts orders for securities transactions for an employee benefit plan account or an IRA or similar account for which the bank acts as custodian, subject to certain conditions. CBA notes, however, that the Exchange Act exception for safekeeping and custody activities provides that a bank, as part of its customary banking activities, may serve as custodian or provider of other related administrative services to any IRA, pension, retirement, profit sharing, bonus, thrift savings incentive or other similar benefit plan.[17] The Proposed Rules carve out an exception for a bank that accepts orders for securities transactions only in its capacity as custodian for an employee benefit plan account or an IRA or similar account. CBA urges that the Agencies follow the language of the Exchange Act and include the bank in its capacity as the provider of other related administrative services. CBA believes that there may be instances in which the bank as provider of administrative services in connection with retirement or employee benefit plan accounts, may find it useful to accept orders for securities transactions from customers. Congress included the exception for provision of administrative services in the Exchange Act, and CBA believes that the same exception should be included in the Proposed Rules in the same manner as the exception is provided for a bank's role as custodian.

While CBA recognizes that the Proposed Rules provide a limited exception for a bank in its role as a provider of administrative services, such an exception does not include providing administrative services to IRAs.[18] In addition, the exception does not permit the bank to execute a cross-trade or net orders, other than orders for shares of open-end investment companies not traded on an exchange. CBA believes that a bank that is providing administrative services to IRA customers should be permitted to accept orders for securities transactions from such customers just as it may for other employee benefit plan accounts. In addition, CBA sees no reason why banks should not be

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[16] See Banking Agencies' Comment, Appendix at 31.
[17] Exchange Act § 3(a)(4)(B)(viii)(ee).
[18] Proposed Rules §__.760(e).

permitted to execute a cross-trade or net orders when it is providing administrative services, just as they are when providing custodial services. Cross-trades and netting orders facilitate the ability of the bank to provide administrative services for employee benefit plan accounts and IRAs. It is highly unlikely that securities transactions engaged in as an accommodation for such customers would result in the bank operating a securities broker out of this division of the bank.

Accommodation Transactions

The Proposed Rules also permit banks to accept orders to effect transactions in securities for custodial accounts other than employee benefit plan accounts or IRAs as an accommodation to customers. CBA believes that such an exception is appropriate. However, the exception provides that the bank may not advertise that it accepts orders for securities transactions for such accounts. CBA objects to such a restraint on advertising. It seems unusual to permit a bank to engage in the activity but not permit it to advertise that it offers the service. In connection with other exceptions, the Proposed Rules permit the service to be advertised but limit the scope and prominence with which the service may be promoted in advertisements.[19] In no instance is the bank flatly prohibited from advertising a service that it is legally permitted to offer. CBA believes that such a restriction would not be consistent with the principles established by the U.S. Supreme Court in *Central Hudson Gas & Electric Co. v. Public Service Comm'n*, 447 U.S. 557 (1980). In that case, the Court held that government restrictions affecting commercial speech do not violate the First Amendment if (a) the regulated speech concerns an illegal activity; (b) the speech is misleading; or (c) the government's interest in restricting the speech is substantial, the regulation in question directly advances the government's interest, and the regulation is no more extensive than necessary to serve the government's interest. 447 U.S. at 566. It seems difficult to conceive how a complete ban on advertising securities transactions conducted in accordance with the terms of the accommodation exception is needed to serve the government's interests. Indeed, the Agencies' *Federal Register* notice provides no reason for a total ban on advertising this service. Accordingly, CBA requests that the ban on advertising contained in §__.760(b)(4) be removed.

OTHER PROPOSED EXEMPTIONS

Regulation S Transactions

CBA supports the proposed exemption for Regulation S transactions with non-U.S. persons. Such an exemption is consistent with the safe harbor from securities registration requirements provided by Regulation S. If securities issued pursuant to Regulation S are exempt from registration requirements, CBA believes it makes sense that a bank be permitted to effect a sale or resale of such securities as agent to a purchaser who is outside the U.S. without the bank being deemed a broker.

[19] Proposed Rules §__.721(b).

Securities Lending Transactions

CBA also supports the proposed exemption for certain securities lending activities conducted by banks as agent. Such an exemption would maintain the current exemption that would otherwise become void when the Agencies adopt final rules. CBA notes, however, that the securities lending exemption in the Proposed Rules does not include language contained in the Commission's current rule which also exempts banks acting as a conduit lender as well as an agent.[20] For the purposes of the Commission's exemption, the term "conduit lender" means a bank that borrows or loans securities, as principal, for its own account, and contemporaneously loans or borrows the same securities, as principal, for its own account.[21] In order to preserve the integrity of the current exception, CBA believes that it is important that the current exception in the Commission's rules for banks' engaging in securities lending transactions and securities lending services in connection therewith remain intact and unchanged. Accordingly, CBA requests that the Agencies adopt the language of the exemption that is currently set forth in the Commission's rules.

Transactions in Investment Company Securities

The Proposed Rules also provide an exception for the way banks may effect transactions in certain investment company securities if specified conditions are met. The exemption will enable banks to effect transactions in securities of an open-end investment company through the National Securities Clearing Corporation's Mutual Fund Services or directly with a transfer agent acting for the open-end company. CBA believes that the exemption is appropriate and supports its adoption.

Exemption for Contracts Entered Into By Banks

The Proposed Rules establish two additional exemptions that address inadvertent failures by banks that could trigger rescission of contracts between a bank and a customer. Under the first proposed exemption, no contract entered into before 18 months after the effective date of the proposed exemption would be void or considered voidable by reason of Section 29 of the Exchange Act because a bank that is a party to the contract violated the registration requirements of the Exchange Act, any other applicable provision, or rules of the Commission based solely on the bank's status as a broker when the contract was created.

Under the second proposed exemption, no contract entered into would be void or considered voidable by reason of Section 29(b) of the Exchange Act without a time limit. This would provide relief to a bank that violated certain provisions of the Exchange Act or Commission rules based solely on the bank's status as a broker when a contract was created if at the time the contract was entered into, the bank acted in good faith and had reasonable policies and procedures in place to comply with the Exchange Act and the Proposed Rules and the violation did not result in significant harm, financial loss or cost

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[20] 17 C.F.R. § 240.15a-11(a).
[21] 17 C.F.R. § 240.15a-11(d).

to the person seeking to void the contract. CBA agrees that a bank that is acting in good faith and has reasonable policies and procedures in effect should not be subject to rescission claims as a result of an inadvertent failure to comply with the Exchange Act's requirements if customers are not significantly harmed. Accordingly, CBA supports adoption of the two proposed exemptions.

EFFECTIVE DATE

The Proposed Rules will require banks to come into compliance with the Proposed Rules on the first day of its first fiscal year commencing after June 30, 2008. As a result, banks will have only approximately one year after the Proposed Rules are adopted to develop policies, procedures and systems that will be necessary to assure compliance with the rules. CBA believes that given the complexity of the rules, an effective date of the first fiscal year commencing after June 30, 2008 will not provide sufficient time to develop and implement the required changes. As the Agencies are well aware, developing and implementing programming changes, operational requirements, training and compliance programs require significant time. Given the numerous changes that are already in the queue, institutions will find themselves stretched to the limit to meet the proposed effective date. CBA suggests that a more realistic estimate is that it will take at least two years for banks to come into compliance. Accordingly, CBA requests that the Agencies extend the effective date until a bank's first fiscal year commencing after June 30, 2009.

NASD RULE 3040

In order to provide seamless financial services to customers, many depository institution employees are also registered representatives. NASD Rule 3040 ("Rule 3040") requires registered representatives involved in securities activities outside of member firms to comply with certain notice, approval, record retention and supervision requirements. Rule 3040 could be interpreted as applying to bank employees who are registered representatives when engaging in transactions that are exempt under the Proposed Rules and under the Exchange Act. If the rule is so applied, it would impose an undue burden on dual employees who engage in exempt transactions permitted by the Proposed Rules because such otherwise exempt transactions would nonetheless be subject to the requirements of Rule 3040. CBA believes that applying Rule 3040 to bank employees who are registered representatives engaging in exempt transactions under the Proposed Rules and under the Exchange Act conflicts with the GLB Act and undermines the purpose of the Congressionally mandated exemptions. Accordingly, CBA requests that the Commission expressly indicate that Rule 3040 does not apply to dual employees.

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CBA appreciates the opportunity to provide its comments on the Proposed Rules and anticipates that its comments will be taken into account by the Agencies when they adopt final rules. Should you have questions relating to this letter, please do not hesitate to contact the undersigned at (703) 276-1750.

Sincerely,

Joe Belew
President