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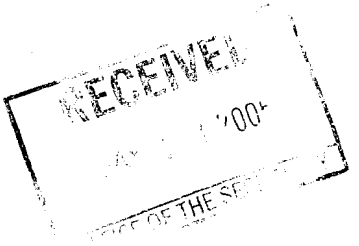

The Honorable William H. Donaldson
Chairman
Securities and Exchange Commission
450 5th Street, N.W.
Washington, D.C. 20549

Dear Chairman Donaldson:

Thank you for your leadership in the effort to bring regulatory relief to small businesses, including small financial institutions, as well as your concern for reducing unnecessary regulatory burden on all publicly held corporations. The Securities and Exchange Commission's Advisory Committee on Smaller Public Companies and the SEC's upcoming Roundtable on the Implementation of Sarbanes-Oxley Internal Controls Provisions are only two recent examples of your efforts.

We would like to present for your consideration two specific proposals that we believe together would provide important regulatory relief and reduced burden for public companies of all sizes. These proposals are fully consistent with the regulatory program of the Commission. The first would require a change in regulatory language, while the other may be achieved by regulatory and/or interpretative changes.

Your recent comments and those of Administration officials and congressional leaders echo pleas from the business community that now is the time to evaluate how recent reforms are doing. We believe that, working together, appropriate course adjustments can be made that will buttress the purposes of the reforms and eliminate unnecessary costs that are often clouding those purposes and inhibiting their effectiveness.

Proposal 1: Updating Shareholder Threshold for Registration

Generally, a company is deemed public for the purposes of the Securities Exchange Act of 1934 if it is listed on a national securities exchange, is traded on the NASDAQ, or has $10 million in assets and 500 shareholders. Companies are not considered to have a large enough market presence to be subject to reporting under the Act until both the asset and shareholder thresholds are met.

For the banking industry, the $10 million asset threshold is inconsequential. Almost 99% of all banks have assets in excess of $10 million. Thus, the 500

shareholder parameter is the critical criterion for determining which banking organizations are subject to the Exchange Act reporting requirements. This criterion has not been updated since it was initially legislated in 1964.

It is worth noting that some banking organizations today are required to report under the Exchange Act even though they may never have publicly issued any stock. Without effort or intention to offer shares publicly, many community banks have, over the years, seen their shareholder base grow as successive generations distributed their stock holdings among their descendants.

Recent activities by the Commission demonstrate a recognition that the cost of compliance with reporting requirements is relatively greater for smaller companies than for large issuers. Yet many new requirements have substantially increased the costs to small companies. To ameliorate the burdens associated with Exchange Act reporting, we propose that the 500-shareholder threshold be updated.

The asset size parameter has, for example, been incrementally increased by a factor of 10, from the $1 million level initially required when Section 12(g) was added to the Exchange Act in 1964, to $10 million in 1996, when the Commission concluded that the "increase in the asset threshold is not inconsistent with the public interest or the protection of investors . . ." The 500-shareholder threshold has never been adjusted, although the Commission noted in 1996 its intention to consider updating it.

In the intervening years, the size of the investing market has grown substantially, as has the number of corporations and the number of shareholders. A small corporation today with a small investor footprint is significantly different from what it was 40 years ago. The indicator of a public market (500 shareholders), given the population of investing shareholders in 1964, is now due for appropriate revision. Using change in the number of shareholders of New York Stock Exchange (NYSE) listed companies as a proxy for change in the number of shareholders in all publicly traded companies, we find that the number of shareholders of NYSE-listed companies has grown from approximately 20 million in 1965 to 65 million in 2005 – an increase of 223 percent. Correspondingly, the 500-shareholder criterion could also be raised 223 percent to about 1500 and still represent a similar level of public shareholder interest in a corporation as that which existed in 1964.

As another measure of change, we could contrast the market presence of 500 shareholders in 1964 with the market presence of comparable shareholders today. In 2005 dollars—that is, adjusting for inflation—the same market presence today that 500 shareholders would have occupied in 1964 would require six times the dollar investment, or six times the number of shareholders: $100 in 1964 would equal about $600 today. That is to say that it takes approximately 3000 shareholders today to equal the market presence of 500 shareholders in 1964 (if

the average number of shares held by each shareholder and the average price of each share have not changed).*

Accordingly, we recommend updating the 1934 Act registration shareholder threshold. We request that it be increased to a number somewhere within the range of 1500 to 3000 shareholders. This would appropriately establish a registration threshold comparable in effect to the level enacted in 1964.

The Exchange Act also provides that a company cannot seek to de-register until the number of shareholders of record is below 300. Sections 12(g)(4) and 15(d) should be similarly updated to place the threshold for de-registration at somewhere within the range of 900 to 1800 shareholders of record.

Proposal 2: More Valuable Auditing Practices

Many corporations—not just banks—advise that their most troubling regulatory challenge is justifying some of the costs connected with auditing practices in satisfaction of the Sarbanes-Oxley Act of 2002. In particular, concerns focus on the auditing costs imposed by implementation practices associated with Section 404 of the Act, costs for which they have difficulty identifying a corresponding benefit to them, to their customers, or to their shareholders. As a typical example, a mid-Atlantic community bank reports that its auditing costs have risen from $193,000 for 2003 to $600,000 for 2004.

Bankers single out for particular mention the recent practices of external auditors. We are familiar with the importance of the external audit, since significant federal auditing standards were applied to the industry under the 1991 Federal Deposit Insurance Corporation Improvement Act (FDICIA). Bankers question, however, the degree of expansion of the external audit: repeatedly, bankers report that external auditors are recreating 70% or more of the work of the internal auditor. Checking and verifying the work of the internal auditor is important and valuable to management and shareholders, but substantially duplicating that work seems excessive.

We propose working with the Commission and with the Public Company Accounting Oversight Board (PCAOB) in an effort to strengthen the value of Section 404 auditing practices and reduce unnecessary costs and activities. This would include improved public guidance with regard to not just what is required of auditors but also what is not required. Specifically, we would propose as an objective to reemphasize the role of the external audit as an effective testing and verification of internal audit work, not a substantial replication of it.

We believe that the focus of these efforts could begin with two areas:

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* In fact, this could understate the case, since the average NYSE share today trades for about $35 (the average share in 1964 cost $50), and the recent broadening of market participation suggests that today's shareholder owns fewer shares than the average, relatively wealthier shareholder of 1964.

--Clarifying what is the appropriate degree of reliance on the work of internal auditors; and
--Clearer guidance as to what is meant by the requirement that external auditors use principal evidence.

At the same time, this effort could encompass additional appropriate steps to be taken in the continuing effort to ensure that these rules and practices are most effectively meeting their important public purposes—purposes that bankers support—while minimizing unnecessary costs to public companies and to their customers and shareholders.

We appreciate both your public commitment to this effort and your dedication to seeing it carried through. The banking industry stands ready to join with you in these efforts to promote America as the best place in the world to save and invest.

Sincerely,

Wayne Abernathy
Executive Director
Financial Institutions Policy and Regulatory Affairs