



1120 Connecticut Avenue, NW
Washington, DC 20036

1-800-BANKERS
www.aba.com

*World-Class Solutions,
Leadership & Advocacy
Since 1875*

Sarah A. Miller
Director
Center for Securities, Trust
and Investments
202-663-5325
Smiller@aba.com

November 23, 2005

Jonathan G. Katz
Secretary
Securities and Exchange Commission
100 F. Street, N.E.
Washington, D.C. 20549-9303

Re: Commission Guidance Regarding Client Commission Practices Under Section 28(e) of the Securities Exchange Act of 1934; File No. S7-09-05, 70 Fed. Reg. 61700 (October 25, 2005).

Dear Mr. Katz:

The American Bankers Association ("ABA")¹ appreciates the opportunity to comment on the Securities and Exchange Commission's ("Commission") proposed interpretative release on client commission practices allowed under Section 28(e) of the Securities Exchange Act ("Exchange Act"). This issue is very important to our members. As of December 2004, 1,896 commercial banks and savings associations were authorized to exercise fiduciary powers. Collectively, these banks and savings associations managed \$4.7 trillion in assets on behalf of their fiduciary clients.

And as the Commission recognizes, banks acting in a fiduciary capacity are affected by Section 28(e) and the Commission's interpretation. The provision establishes a safe harbor that allows bank fiduciaries to use client funds to purchase "brokerage and research services" for their managed accounts under certain circumstances without breaching their fiduciary duties established under state and federal law, including ERISA and applicable banking regulations. Indeed, all of the federal banking regulators have confirmed the applicability of this safe harbor to bank trust activities.²

¹ The ABA, on behalf of the more than two million men and women who work in the nation's banks, represents all types of banking institutions in this rapidly changing industry. The ABA's membership includes community, regional and money center banks and holding companies, as well as savings associations, trust companies and savings banks (collectively referred to as "banks"), making it the largest banking trade association in the country.

² Comptroller of Currency, Trust Banking Circular 25: Use of Commission Payments by Fiduciaries (June 19, 1986); Federal Deposit Insurance Corporation, Trust Examination Manual, available at <http://www.fdic.gov/regulations/trust/index.html>; Federal Reserve Board, Guidelines for the Inspection of Investment Adviser Subsidiaries of Bank Holding Companies (Feb. 8, 1991);

Significance of Section 28(e)

At the outset, we applaud the Commission for its new Section 28(e) interpretative guidance that, for the most part, provides money managers a clear understanding of the safe harbor's scope and limitations. As the 1998 Office of Compliance, Inspections and Examinations Report³ ("OCIE Report") on client commissions indicated, some industry participants did not fully understand the boundaries of the safe harbor, especially with respect to complex technology and mixed-use products and services. Any additional guidance, if clearly and appropriately written, will provide money managers with a greater degree of legal certainty and increased fiduciary protections for their clients.

We also strongly support the Commission's determination that the safe harbor applies equally to arrangements involving client commissions paid to full service broker-dealers that provide brokerage and research services directly to money managers, and to third party research arrangements where the research services and products are developed by third parties and provided by a broker-dealer that participates in effecting the transaction. The Commission's position will assure that investors have access to quality and independent research.

Finally, we applaud the Commission's goal of providing greater cross-border compatibility between multiple regulatory regimes by taking the Financial Services Authority client commission rules into consideration in promulgating this interpretation.⁴ The need to achieve regulatory convergence is of great importance for those of our members that offer banking products and services, including fiduciary services, abroad. And it is for that reason, that ABA's affiliates, the ABA Securities Association and the Bankers' Association for Finance and Trade, sponsored, along with several other domestic and foreign trade associations, a study on the need to rationalize the various regulations governing cross-border wholesale dealings in equities and equity derivatives.⁵ We strongly encourage the Commission to continue these efforts.

Given the importance of this new guidance, we hope the Commission will allow a suitable level of flexibility in its use and implementation. If the safe harbor is interpreted too narrowly, for example, with respect to mixed-use items which we discuss below, trust departments, especially at smaller institutions, may

Office of Thrift Supervision, Trust Handbook: Asset Management, *available at* <http://www.ots.treas.gov/docs/4/427046.PDF>.

³ SEC, Inspection Report on the Soft Dollar Practices of Broker-Dealers, Investment Advisers and Mutual Funds (Sep. 22, 1998).

⁴ U.K. Financial Services Authority, Policy Statement 05/9, Bundled Brokerage and Soft Commission Arrangements: Feedback on CP 05/5 and Final Rules (July 2005).

⁵ The EU-US Coalition on Financial Regulation, *Report on The Transatlantic Dialogue in Financial Services: The Case for Regulatory Simplification and Trading Efficiency*, available at www.baft.org/jsps.

determine that providing customized money management services to trust clients using client commissions is fraught with limitations and not worth the effort to navigate. As a result, banks may be forced to pay hard dollars for research and brokerage services and fiduciary clients who do not need these services will be forced to subsidize those clients who do. In addition, we hope that the Commission will give money managers sufficient time to incorporate the final interpretive release into their policies, procedures, and most importantly contracts with third-party vendors.

Permissible Brokerage Services

With respect to brokerage services allowed under the safe harbor, the release's temporal test limits "brokerage" to those services performed between the transmission of the order to the broker and the crediting of the account. Despite the statute clearly permitting custodial services,⁶ it remains unclear whether these services performed by a broker would fall within this temporal standard. The Commission should affirm that those services are indeed appropriate and protected under the safe harbor.

In this connection, we note that our support for including custodial services within the definition of brokerage services protected under the safe harbor should not, in any way, suggest that order-taking, clearance and settlement and custodial services offered by banks are brokerage transactions subject to broker registration under Section 3(a)(4) of the Exchange Act. We believe that this is also the Commission's position in that its description of the temporal standard is expressly limited to the safe harbor.⁷

The second issue concerns the appropriateness of complex technology which performs more than one function. The interpretive release plainly states that order management systems ("OMS") are not eligible under the safe harbor. This inflexible conclusion ignores that fact that many OMS are integrated with order execution systems ("OES") in a complex and continuously evolving way. OES constitute "brokerage" under the release's temporal standard and the statutory definition of "effect[ing] securities transactions." Unfortunately, allocating the expense under a "mixed-use" approach would be extremely complicated given the rapidly changing industry. While the OCIE Report cited a number of examples of questionable allocation, the report did not explain what would be proper. Neither did the recent and 1986 interpretive releases explain in more than a vague fashion what was appropriate outside of keeping "adequate books and records."⁸ The ABA, therefore, asks the Commission for further

⁶ Section 28(e)(3)(C) states that brokerage services include "functions incidental thereto (such as clearance, settlement, and custody)."

⁷ The release states: "Specifically, *for purposes of the safe harbor*, we believe that brokerage begins when the money manager communicates with the broker-dealer for the purpose of transmitting an order for execution and ends when funds or securities are delivered or credited to the advised account or the account holder's agent." (emphasis added), 70 Fed. Reg. at 61708.

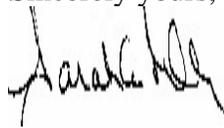
⁸ 70 FR 61700 at 61709.

explanation of what would constitute reasonable allocation for mixed-use services, especially for complex computer technology.

Conclusion

The ABA appreciates the opportunity to comment on the proposed interpretive release on Section 28(e) of the Exchange Act. We hope that our comments will assist the Commission's efforts to provide the appropriate guidance to money managers on this matter. Please do not hesitate to contact the undersigned or Phoebe Papageorgiou in this office should you wish to discuss these matters further.

Sincerely yours,

A handwritten signature in black ink, appearing to read "Sarah A. Miller". The signature is fluid and cursive, with the first name "Sarah" being the most prominent.

Sarah A. Miller