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November 7, 2000

Ms. Catherine McGuire
Associate Director and Chief Counsel
Division of Market Regulation
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20036

RE: Title II of Gramm-Leach-Bliley Act, Pub. L. No. 106-102

Dear Caite:

On behalf of the American Bankers Association (“ABA”) and the ABA Securities Association (“ABASA”)¹, I would first like to thank you for taking the time from your busy schedule to meet with representatives from ABA/ABASA on October 12, 2000, to discuss the trust and asset management business conducted at banks and how that business could potentially be impacted by Title II of the Gramm-Leach-Bliley Act. Attendees at that meeting found the discussions most informative. I hope that you and your staff did as well. In fact, as you will read at the end of this letter, we would like to schedule another meeting to discuss further other issues that have surfaced as the industry moves toward implementation of this most significant piece of legislation.

During the meeting you offered to respond to certain questions posed by the industry. As you explained, these questions must not be fact specific but rather must be legal in nature or process-related. In that vein, the ABA and ABASA are writing to seek guidance from the staff of the Securities and Exchange Commission (“Commission”) on an issue that I have previously mentioned to you and certain members of your staff. That issue involves the application of the trust and fiduciary exception from broker registration to acquisitions by banks and trust companies (hereinafter referred to collectively as “banks”) of securities issued by registered open-end investment companies.²

¹ The ABA brings together all categories of banking institutions to best represent the interests of this rapidly changing industry. Its membership—which includes community, regional, and money center banks and holding companies, as well as savings associations, trust companies, and savings banks—makes ABA the largest banking trade association in the country.

ABASA is a separately chartered affiliate of the ABA representing those holding company members of the ABA that are the most actively engaged in securities underwriting and dealing activities, offering proprietary mutual funds, and derivatives activities.

² This issue also impacts the stock purchase plan and safekeeping and custody exceptions included in Title II. To the extent that securities activities conducted under these exceptions involve the purchase and redemption of shares of registered open-end investment companies, any guidance provided as a result of this request should apply equally to those exceptions.

There are over 2,200 banks authorized to exercise trust powers in the United States.¹ Many of those institutions have expressed concern that based on current industry practices, they will be unable to comply with all the applicable requirements of Title II. Specifically, banks, through their trust and custody departments, generally do not purchase and redeem shares of open-end investment companies through registered broker-dealers but, rather, purchase or redeem these securities through automated systems that do not always provide for an interface between the trust or custodial bank and the fund distributor.

Specifically, rather than phone or mail the fund companies themselves to effectuate a purchase or liquidation, many bank trust and custody departments use Fund/SERV to clear and settle mutual fund transactions automatically. The Fund/SERV system, operated through NSCC/DTCC, provides centralized, automated order entry, confirmation, registration, and settlement of mutual fund transactions for registered investment companies and various financial services firms, including banks. Fund/SERV gives users greater control over transaction processing; the benefits of standardized procedures, formats, and time frames across all funds in the system; and net settlement through a single payment.

The standard Fund/SERV agreements include the Trust Fund/SERV Agreement and the Trust Networking Agreement. The Trust Fund/SERV Agreement involves transmitting trade information between the trust or custodial bank and the registered investment company. The Trust Networking Agreement provides for transmission of non-trade shareholder information, including information involving dividends and registration records for new accounts. Generally, these agreements are entered into between a trust or custodial entity and a “Fund Agent.” Universally, the “Fund Agent” is defined as either: (i) an investment advisor to or the administrator for the Funds, (ii) the principal underwriter or distributor for the Funds, or (iii) the transfer agent for the Funds. Copies of the relevant agreements are attached.

As you know, Section 201 of Title II amends Section 3(a)(4) of the Securities Exchange Act of 1934 by adding, inter alia, new subsection (C).² That section requires trust, fiduciary and custody purchases and sales of U.S. publicly traded securities to be directed to a registered broker-dealer for execution. Obviously, when the Fund Agent is the principal underwriter or distributor for the Funds, the requirements of subparagraph (C) are satisfied as the underwriter/distributor is itself a registered broker or dealer.

This is not the case, however, if the bank’s trust or custody department interfaces with the fund’s investment advisor, the fund administrator or the transfer agent for the fund. Obvious, but highly disruptive, solutions could be to require either: (i) the banks to stop using Fund/SERV (or any other mutual fund where the bank’s trust and custody departments interact directly with fund’s

¹ Federal Financial Institutions Examination Council, Trust Assets of Financial Institutions –1998 at 8.

² Paragraph (C) provides:

“The exception to being considered a broker for a bank engaged in activities described in clauses (ii) [TRUST ACTIVITIES], (iv) [CERTAIN STOCK PURCHASE PLANS], and (viii) [SAFEKEEPING AND CUSTODY ACTIVITIES] shall not apply if the activities described in such provisions result in the trade ... of any security ... unless ... (i) the bank directs such trade to a registered broker or dealer for execution; ...; or (iii) the trade is conducted in some other manner permitted under rules, regulations, or orders as the Commission may prescribe or issue.”

investment advisor, administrator or transfer agent) or (ii) the funds participating in Fund /SERV (or any other mutual fund where the bank's trust and custody departments interact directly with the fund's investment advisor, administrator or transfer agent) to restructure the manner in which the banks and the funds interface with each other to assure that all transactions flow through the underwriter/distributor. The first alternative is not feasible while the latter would require many existing agreements to be amended. Importantly, neither alternative would benefit fund companies, or fiduciary or custodial customers of the banks.

Rather than require the implementation of either alternative, we would request that the staff interpret subparagraph (C) to permit bank trust and custody departments to interact with a fund's transfer agent, administrator or investment advisor without the need for a broker-dealer to be interposed between the current parties to the transaction. We believe that such a result is within the spirit, as well as the intent of subparagraph (C), especially subparagraph (C)(iii) which grants to the Commission the flexibility to permit trades to be conducted in some other manner.

Finally, we would note that the importance of this issue is not likely to diminish. It is anticipated that the trend toward using Fund/SERV is expected to continue with many more banks and funds opting to use the Fund/SERV system in the future.

In order to facilitate compliance with this and other provisions of Title II, the ABA would request an opportunity to meet informally with you and your staff to discuss several issues. Specifically, questions have surfaced among our membership regarding implementation of the "chiefly" concept contained in the trust and fiduciary exception's compensation provisions. Our members have several different views regarding how "chiefly" should best be calculated. The differences in views would appear to depend on the type of operational systems employed by the bank as well as the organizational structure of the institution itself. This is just one example where the ABA/ABASA would suggest that flexibility should be the watchword in interpreting Title II.

As the effective date for Title II is close upon us and many of the issues involving Title II are very important to an orderly implementation of that Title, we would suggest that any such meeting take place at your most earliest convenience.

Sincerely yours,

Sarah A. Miller

Attachments

cc: Lourdes Gonzalez

