

# THE STA

## SECURITIES TRANSFER ASSOCIATION, INC.

Established 1911

June 15, 2004

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Jonathan G. Katz, Secretary  
United States Securities and Exchange Commission  
450 Fifth Street, NW  
Washington, DC 20549-0609

RE: RELEASE NO. 33-8398; 34-49405; 1C-26384; FILE NO. 57-13-04  
Concept Release: Securities Transactions Settlement

Dear Mr. Katz:

This letter is submitted on behalf of the Securities Transfer Association, Inc. ("STA") in response to the above-referenced concept releases. The STA represents more than 100 transfer agents nationwide who maintain in the aggregate more than 150,000,000 million registered shareholder accounts on behalf of more than 15,000 issuers.\* We very much appreciate the opportunity to present our views to the Commission.

With regard to the Commission's initial questions relative to the possible implementation of a settlement cycle shorter than T + 3, the STA supports industry initiatives to shorten the settlement cycle and believes there are a number of improvements that can be made to existing infrastructure to accomplish this. We believe efforts to achieve straight-through processing ("STP") between the participants in the clearance and settlement system should be increased, as this will lead to efficiencies and shortened settlement cycles, without mandating a shorter settlement cycle. We would recommend that the focus of the industry be on STP, rather than just on reducing the settlement cycle to T + 1. After making achievements in STP, we believe another review of the costs and benefits to transfer agents, broker-dealers, issuers and shareholders in mandating T + 1 for different types of transactions would be appropriate.

While there are, as noted by the Commission in its release, certain additional efficiencies which could enhance the T + 3 cycle, the STA believes that for certain transactions the current settlement cycle strikes the proper balance between risk and efficiency on the one side, and cost on the other.

With regard to the Commission's release pertaining to the immobilization and dematerialization of equity securities certificates, the STA endorses and supports the Commission's longstanding position that the securities markets should move toward increased dematerialization, while at the same time protecting the individual investor's rights to be directly registered on the books of the issuer, and to request a certificate if they so desire.

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\* These figures include shareholders of our members from the mutual fund industry.

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The STA agrees that utilization of certificates may not be the most efficient method for processing the vast majority of equity securities transactions, and that certificates generally result in increased costs for the brokerage industry, issuers and for custodians.\* Nevertheless, we feel constrained to note that there are certain instances where certificates, as an option, make sense:

1. Where the investor insists on physical custody of his holdings;
2. Where the investor holds restricted securities, and
3. Where the investor needs to pledge or otherwise hypothecate shares; e.g., place them in escrow in accordance with the prevailing laws in the 50 states and the Uniform Commercial Code (See, e.g., Sections 8-106, 8-301, 9-203 and 9-313(a) of the Uniform Commercial Code.)

While these examples represent a small fraction of securities processed, each is significant in its own right as a reason to allow certificate ownership as an investor option. While the STA agrees with dematerialization and believes that the vast majority of securities transactions can, are and should ultimately be processed in an uncertificated environment, we believe it would be impossible, under current legal constraints to eradicate certificates altogether.\* Having taken this position, the STA notes that it would support the notion of having the incremental costs involved with holding a physical certificate borne by those investors who choose to hold their securities in this manner.

Although we believe the brokerage community will also agree with eliminating the use of certificates, it may be more likely to prefer immobilization of securities in a depository, such as DTC, with beneficial owners holding in street name, as this would allow them to manage and control more investor accounts and assets. The STA would oppose complete immobilization, as it would serve as a mechanism to move away from direct ownership by investors on the issuer's books and prevent direct contact between the issuers and their shareholders. We do not believe this would be in the best interests of retail investors.

Unlike broker-dealers, transfer agents and custodians act as neutral intermediaries and as recordkeepers -- they *do not*, at the same time, make investment decisions or recommendations for the investor, as do broker-dealers.\*\* Investors should continue to have the choice to hold their assets with such a neutral party. We urge the Commission not to lose sight of this salient consideration.

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\* Although there are costs associated with lost certificates, those costs diminish dramatically each year as dematerialization increases, and it is the individual investor who pays this cost. Accordingly, the cost properly rests with the party who finds benefit in having possession of a certificate. We note there are also increased costs of dematerialization relating to the costs of sending statements to shareholders (annual rather than only upon issuance), unnecessary escheatment (increased risk due to address changes coupled with lack of a certificate) and identity theft (significantly more of a problem without certificates).

\*\* Moreover, when brokerage firms have failed or have been shut down by regulators, investors have been without access to their securities for prolonged periods, and have sustained losses. On the other hand, there have been virtually no investor losses associated with the failure or closure of registered transfer agents or custodians.

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The STA firmly believes that there are benefits to be derived from dematerializing equity securities in the United States. Efficiency, portability, ease of negotiation, and certainty in execution of corporate actions, are among the many attributes a book-entry environment will support. However, the STA further believes that the concept of direct ownership of securities must continue to be fully supported in the proposed dematerialized environment, and that direct ownership need not be synonymous with holding securities in certificated form. Direct ownership must be preserved and "in the system" must include both holdings at brokerage firms and those at custodians, and the Commission should mandate that they be afforded equal weight and treatment.

In terms of moving forward with increased dematerialization, the STA believes that the Direct Registration System ("DRS") is a useful but incomplete model. The STA has been a proponent of DRS since its inception. Our members have participated in the joint industry committees that have charted the system's strategic evolution, and have directed the industry-wide forum that created its current operating guidelines. The STA favors expansion of DRS, but we note that DRS is an inefficient model for *total* dematerialization, because DRS is not constructed to deal with restricted securities and pledged securities. Under current states' laws and the UCC, physical certificates, not DRS, are mandated for such transactions. Moreover, as we have noted in our quarterly meetings with the Commission, while DRS is a usable model, its implementation has been underwhelming. In the first instance, we note that while the brokerage industry and the STA championed DRS, they have not been able to implement DRS by adequately educating primary brokers, clearing brokers or investors. In reality and in practice, the number of brokerage personnel who understand and can implement a DRS transaction is miniscule. Until this is changed drastically, talking about increased dematerialization is just talking.

We urge the Commission to require more DRS training and education for clearing brokers and primary brokers alike; and we urge the Commission to mandate that brokers distribute to their clients an education pamphlet cleared by the Commission which sets out in a neutral fashion the advantages and disadvantages in DRS of holding shares directly on the issuer's books or, in the alternative, in street name.

Additionally, we note that DRS implementation and expansion have been hamstrung by the fact that those issuers not presently participating in DRS have little or no incentive to subscribe to DRS in the absence of a split, stock dividend or other corporate action resulting in distribution of shares to a substantial percentage of the shareholder base. While issuers may agree in concept with dematerialization, our current DRS experience shows that the number of certificates issued in daily processing does not diminish after adoption of the system. In order to change this, securities exchanges need to make DRS a condition of listing and DTC's WT (withdrawal) transactions need to default to DRS shares where the security being withdrawn is DRS-eligible.

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The expansion and refinement of DRS might serve other purposes in addition to facilitating dematerialization. Given the communication mechanisms contemplated in our ongoing NFE\* discussions, DRS could be the vehicle that would allow transfer agents to hold in custody those directly registered positions currently under control of broker-dealers in physical form. Further, for those issuers seeking greater transparency of ownership and for those investors who hold securities in brokerage but who have a desire to stay directly connected to the issuer, a perfected DRS could be the vehicle that allows beneficially held positions to be placed on the issuer's register, while maintaining broker-dealer control. Similarly, DRS could support periodic transfers of broker-dealer stock records to the issuer for various and sundry purposes including, but not limited to, annual meeting related communication/solicitation.

The STA believes strongly that the current proxy voting and distribution rules totally obstruct effective communication between issuers and their shareholders. An effective DRS system and true transparency are, we believe, essential. The current distribution system is simply broken -- fostering a compromised voting structure where over-votes are frequent, and the costs to issuers are higher than what they otherwise could be in a more effective system.

In summary, the STA:

- is fully supportive of moving toward a more dematerialized securities market using DRS as the vehicle for delivery to directly registered shareholders;
- is strongly opposed to any dematerialization efforts which would hamper the ability of investors to hold securities in directly registered form or to request a certificate;
- recognizes that, in the present legal and regulatory environment, certificates cannot be completely eliminated;
- will continue to participate in industry efforts (e.g., NFE) to craft alternative solutions for those instances where certificates are still required;
- is supportive of, and continues to participate in, industry efforts to expand the usage of DRS, but recognizes that there must be substantial improvement in the industry's education efforts in order for such expansion to be realized. Further, it recommends that the securities exchanges make DRS a condition of listing, and that DTC be allowed to default its Withdrawal by Transfer (WT) transaction to DRS shares for those securities participating in DRS; and

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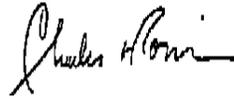
\* As we reported to the Commission, recent conversations between the STA and DTC relative to NFE have been very productive; and we believe that NFE, utilizing DRS, is, in all likelihood, the most effective vehicle for true, large scale dematerialization. However, the costs to transfer agents and custodians for implementing NFE are not yet quantified, and we need to explore together with DTC the economics of such a system.

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- recognizes that a 'perfected' DRS might serve as the mechanism for supporting other record-keeping opportunities beyond facilitating dematerialization.

Thank you for considering our position on these important issues. We look forward to discussing these and related issues in our next quarterly meeting with the Commission and would, of course, be happy to provide any additional assistance that the Commission or its staff might find helpful in considering these issues.

Very truly yours,  
The Securities Transfer Association, Inc.

A handwritten signature in cursive script, appearing to read "Charles V. Rossi".

Charles V. Rossi  
President