

October 13, 2010

**VIA ELECTRONIC MAIL**

[rule-comments@sec.gov](mailto:rule-comments@sec.gov)

Elizabeth M. Murphy  
Secretary  
Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549-1090

**Re: Temporary Registration of Municipal Advisors; Release No. 34-62824; File No. S7-19-10; 17 CFR Parts 240 and 249; September 8, 2010**

Dear Ms. Murphy,

The American Bankers Association (ABA)<sup>1</sup> and the ABA Securities Association (ABASA)<sup>2</sup> appreciate the opportunity to comment on the Securities and Exchange Commission's (SEC or Commission) interim final temporary rule, Rule 15Ba2-6T, to implement the municipal advisor registration provisions of Section 15B of the Securities Exchange Act of 1934 (the Exchange Act), as amended by Section 975 of the Dodd-Frank Act.<sup>3</sup>

Thousands of banks and trust companies provide a variety of traditional banking services to municipal customers, or hold municipal and state bonds in their portfolios.<sup>4</sup> As a consequence, a great number of our members have raised questions and concerns about the interim final temporary rule. We make these comments to assist the Commission in understanding both the uncertainty that the interim final temporary rule has imposed on banks and the regulatory framework that exists in the context of banks' provision of traditional banking products and services to their customers—including municipal entities.

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<sup>1</sup> The American Bankers Association represents banks of all sizes and charters and is the voice for the nation's \$13 trillion banking industry and its 2 million employees. ABA's extensive resources enhance the success of the nation's banks and strengthen America's economy and communities. Learn more at [www.aba.com](http://www.aba.com).

<sup>2</sup> ABASA is a separately chartered affiliate of the ABA that represents those holding company members of the ABA that are actively engaged in capital markets, investment banking, and broker-dealer activities.

<sup>3</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub.L. 111-203 (2010).

<sup>4</sup> According to June 2010 call report data 6,448 banks hold municipal and state government deposits, and 5,217 banks hold municipal and state bonds.

## **The Rush to Registration**

There has been a very short time frame between the publication of the interim final temporary rule and the expiration of the comment period. The notice was published on the SEC's website on September 8, 2010. The Rule was made effective absent the ordinary Administrative Procedure Act protections of a 30 day comment period.<sup>5</sup> The SEC took this unusual action on the grounds that solicitation of comment before adopting the new rules was "impracticable, unnecessary, or contrary to the public interest."<sup>6</sup>

The banking industry is still in the midst of assessing the impact of this rule on core banking activities. Both large and small institutions are reviewing their interactions with municipal entities to determine if they need to register. The current regulatory uncertainty and short time table has caused some banks to register, some to register under protest, and some banks not to register at all because they are not aware of the rule or do not believe the rule applies to them.<sup>7</sup> At the same time, these banks must consider the consequences to the bank's business, if they do register.<sup>8</sup> Because of the broad language used in the Commission's final interim temporary rule, and the lack of guidance regarding the meaning of ambiguous terms, this review can be quite extensive, time consuming and ultimately inconclusive.

We recognize that the Commission felt it was necessary to act with haste in this matter.<sup>9</sup> However, because of the great uncertainty about what activity falls within the registration requirement, we believe the Commission should have provided sufficient opportunity for notice and comment to balance against the possibility that the SEC's actions could negatively impact the ability of municipal entities to access commercial bank products and fiduciary services.

## **Clarification is Needed to Determine Registration**

Banks and trust companies throughout the country currently provide a great variety of products and services to municipal entities. On the commercial side of the bank, these services and products include direct loans, checking accounts, and CDs. Banks of all sizes also frequently are asked to respond to RFP requests from municipal entities regarding investment products offered by the banking entity, such as interest-bearing bank deposits, money market mutual funds, or other exempt securities. Banks also are significant investors in the securities issued by municipalities and provide credit or, through their affiliates, underwriting services to municipalities when the city or township wants to buy a fire truck or build a new school or other similar facility. Furthermore, for over one hundred and fifty years, banks and trust companies have provided fiduciary services to municipal entities in the United States. In this capacity banks often manage investment accounts for local

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<sup>5</sup> See 5 U.S.C. 553 (b) and 5 U.S.C 553 (d).

<sup>6</sup> See Release No. 34-62824, 75 Federal Register at 54471.

<sup>7</sup> In this context we strongly urge the SEC to adopt provisions to ensure that banks that registered as a precaution and who ultimately deregister be deemed never to have registered.

<sup>8</sup> For example, the banks must consider whether registration makes the banking entity and its associated persons subject to the as yet undefined fiduciary duty imposed by Section 975(c)(2).

<sup>9</sup> See Release No. 34-62824, 75 Federal Register at 54472.

towns and act as trustees with respect to bond proceeds, escrow accounts, governmental pension plans and other similar capacities.

While we believe these activities do not fall within the definition of a municipal advisor and are not intended to be captured by the interim temporary rule, the hasty introduction of the rule without accompanying clarification or guidance has created unwelcome uncertainty. As a consequence there remain a significant number of issues outstanding before an institution can determine whether or not they need to register, and what it will mean if a bank determines it does need to register.

For example, banks are struggling with understanding what activities are meant to be covered by the term “investment strategies”. This term is defined as including “plans or programs for the investment of the proceeds of municipal securities”. As noted above, banks often manage investment accounts for local towns. A bank would not necessarily be aware of whether there are proceeds of municipal securities within those accounts. We assume that once the proceeds of a municipal securities offering are comingled with other operating funds or the general funds of the municipal entity that they lose their characteristic as “proceeds” under the statute, and the provision of advice by a bank to the municipal entity with respect to the investment of such operating or general funds would not make the bank a “municipal advisor” under the statute. Similarly, the proceeds of a municipal securities offering that are used to fund a municipal pension plan, once deposited in the plan and comingled with other funds, would likewise lose their characteristic as proceeds under the statute; and the provision of advice by a bank to the municipal entity with respect to the investment of plan assets would not make the bank a “municipal advisor” under the statute. Before a bank should be required to register, the SEC should provide guidance with regard to these ambiguous terms<sup>10</sup> to help institutions comply with the intent of the statute and the rule.

### **The SEC Should Exercise its Authority to Exempt Banks**

We believe that many of the products and services that banks offer to municipal customers will cause them not to register as municipal advisors because they do not involve the provision of “advice”. For example, when a bank responds to a municipal entity’s RFP with information about the types of CDs or other investment products that it offers, it is not providing advice to the entity, but simply providing information about the products that it offers. Similarly, in the trustee context, often times banks, serving as corporate trustees, escrow agents, fiscal agents and in other similar capacities, will identify and provide information with respect to investment products that are offered by the bank and are permitted investments under the municipalities’ investment guidelines governing the account. Banks functioning in such capacities may also be directed by the municipalities (in an agreement or other form of writing) to invest in specific investment products permitted by the municipalities’ investment guidelines. We would maintain that these services would not constitute advice.

Bank trustees also offer certain fiduciary services to municipal entities through a bank trust department that may include the provision of investment advice to, for example, state and local

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<sup>10</sup> In addition to questions that surround the term “investment strategies,” terms that are causing confusion within the banking industry at the registration stage include the use of the terms “municipal derivatives”, “advice”, and “swaps”.

government pension plans. This provision of advice does not fit the definition of being given in connection with municipal financial products because it is typically not in connection with the investment of the proceeds of municipal securities.

These traditional banking services should not be covered by this rule, because banks are currently well regulated and were not the intended subjects of this provision of the statute.<sup>11</sup> Banks that offer trustee services are subject to rigorous and frequent examination, as well as extensive regulation, by federal regulators such as the Office of the Comptroller of the Currency (OCC), the Federal Reserve Board, the Federal Deposit Insurance Corporation (FDIC), the Office of Thrift Supervision, or by state banking regulators. The extensive regulation and examination not only protect the interests of bank customers but also ensure the safety and soundness of the institution for the public good. With respect to fiduciary accounts, state and federal regulations address various aspects of these activities, including the fiduciary obligations of the bank, potential conflicts of interest, and the bank's management of transactional, strategic, compliance, and reputational risks. On-site examinations occur at least every eighteen months. Some large institutions have examiners onsite within the bank's premises throughout the year to examine fiduciary activities continuously.<sup>12</sup>

While the definition of municipal advisor exempts other categories of otherwise regulated investment advisors, namely investment advisors registered under the Investment Advisers Act of 1940 (Advisers Act), there is no statutory exemption for banks that provide the exact same investment advisory service as part of their regulated fiduciary duties. Congress long ago recognized that banks should be exempted from investment advisor registration because they are subject to extensive supervision and oversight. The SEC should follow Congress' lead and, pursuant to Section 15B (a)(4) of the Exchange Act provide an exemption for banks and trust companies from the definition of "municipal advisor" when the bank and trust company provides investment advisory services that are otherwise exempt from registration under the Advisers Act.

Moreover, we would urge the SEC to act in a timely manner in exempting these institutions from municipal advisor registration. A timely issued exemption would eliminate a great deal of the uncertainty that the SEC's interim final rule has generated.

## **Conclusion**

ABA and ABASA support the goal in this instance of regulating previously unregulated market participants. However, we believe that the interim final temporary rule, absent clarification of several key terms and an exemption for banks that offer fiduciary services to municipal entities, is more far-reaching than what Congress intended or what is necessary to accomplish the laudable goals set out by Congress. In addition, the interim final temporary rule may possibly curtail the

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<sup>11</sup> The Senate Banking Committee Report discusses Congressional intent to cover previously unregulated market participants. S.Rep. No. 111-176, at 147 (2010), available at [http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=111\\_cong\\_reports&docid=frsr176.111.pdf](http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=111_cong_reports&docid=frsr176.111.pdf).

<sup>12</sup> For a more complete discussion of the duties, compensation, regulation and examination of corporate fiduciaries see [Appendix A](#).

availability of traditional bank products and services, including credit and cash management services, to municipal clients at a time when our economy can least afford it.

Sincerely,

A handwritten signature in black ink that reads "Carolyn Walsh". The signature is written in a cursive, flowing style.

Carolyn Walsh

Vice-President and Senior Counsel  
Center for Securities, Trust and Investments  
American Bankers Association

Deputy General Counsel  
ABA Securities Association

# Corporate Fiduciaries: Duties, Compensation, Regulation, and Examination

For over one hundred and fifty years, banks and trust companies have provided fiduciary services to trusts, individuals, families, charitable organizations, employee benefit plans, and government entities in the United States. The creation, obligations, and limitations of trusts, trustees, and the fiduciary standard are chiefly a matter of state statutes and common law. State law confers the authority to act as a corporate trustee exclusively to banks and trust companies.<sup>1</sup> State law also defines the highest fiduciary standard that applies to banks and trust companies when acting in a fiduciary capacity, including when offering investment advice for a fee.<sup>2</sup>

Before offering fiduciary services, a bank must apply for and be granted trust powers from its appropriate regulator. In its application, both national and state banks must show that they have the minimum capital and surplus that is required under state law. The bank must also demonstrate that it is in sound financial condition and that there is a need in the community for the fiduciary services. Lastly, the bank must submit the credentials and other background information about the trust management personnel so that the regulator can assess their qualifications and experience.

## Fiduciary Accounts

Fiduciary accounts are those accounts that are administered by a bank or trust company acting in a fiduciary capacity. Fiduciary capacity means acting as a trustee, executor, administrator, registrar of stocks and bonds, transfer agent, as well as assignee, receiver, or custodian under the uniform gifts to minors act. In addition, fiduciary capacity includes a bank acting as investment adviser for a fee, any other capacity in which the bank possesses investment discretion on behalf of another, or any other similar capacity that the banking regulators authorize.

## Fiduciary Duties

Corporate trustees are subject to fiduciary duties. In fulfilling these duties, corporate trustees provide investment management services, safekeeping of assets, management of real property, business interests

and mineral interests, as well as tax planning, preparation and tax payment services. These fiduciary duties include:

- *Duty of loyalty.* A trustee has a fundamental duty to administer a trust solely in the interests of the beneficiaries. A trustee must not engage in acts of self-dealing.
- *Duty of administration.* The trustee must administer the trust in accordance with its terms, purposes, and the interests of the beneficiaries. A trustee must act prudently in the administration of a trust and exercise reasonable care, skill, and caution, as well as properly account for receipts and disbursements between principal and income. A trustee can properly “incur and pay expenses that are reasonable in amount and appropriate to the purposes and circumstances of the trust.”<sup>3</sup>
- *Duty to control and protect trust property.* The trustee must take reasonable steps to take control of and protect the trust property.
- *Duty to keep property separate and maintain adequate records.* A trustee must keep trust property separate from the trustee’s property and keep and render clear and accurate records with respect to the administration of the trust.
- *Duty of impartiality.* If a trust has two or more beneficiaries, the trustee must act impartially in investing, managing, and distributing the trust property, giving due regard to the beneficiaries’ respective interests.
- *Duty to enforce and defend claims.* A trustee must take reasonable steps to enforce claims of the trust and to defend claims against the trust.
- *Duty to inform and report.* A trustee must keep qualified trust beneficiaries reasonably informed about the administration of the trust and of the material facts necessary for them to protect their interests.

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Some jurisdictions also impose a duty to provide an accounting to qualified beneficiaries.

- *Duty of prudent investment.* A trustee who invests and manages trust property has a duty to “invest and manage trust property as a prudent investor would, by considering the purposes, terms, distribution requirements, and other circumstances of the trust.”<sup>4</sup> This duty is tied to the duty to use reasonable care and skill to make the trust property productive.

### Fiduciary Compensation

Whether set by state statute, custom, the courts, or the terms of the governing instrument, fiduciary fees are required to be reasonable. Generally, corporate fiduciaries use a graduated fee schedule of percentages of the assets in the account, which can be customized for the specific circumstances and needs of the trust or estate. A fiduciary may charge a minimum annual fee, as well as an additional fee for any extraordinary services provided to the trust or estate.

### Regulation of Corporate Fiduciaries

Banking institutions that offer these services are subject to rigorous and frequent examination, as well as extensive regulation, by federal regulators such as the Office of the Comptroller of the Currency (OCC), the Federal Reserve Board, the Federal Deposit Insurance Corporation (FDIC), the Office of Thrift Supervision, or by state banking regulators.

### Segregation of Fiduciary Assets

By law, assets held in fiduciary accounts must be segregated from all other bank assets. Likewise, the books and records of these accounts must also be kept separate from the books and records of other bank activities, such as routine deposit and withdrawal transactions. Many institutions use third-party entities, such as Federal Reserve banks or the Depository Trust & Clearing Corporation, to hold these assets. In all of these instances, the assets are not subject to the claims of a bank’s creditors.

All fiduciary cash held in insured deposit ac-

counts are entitled to FDIC insurance, generally up to \$250,000 per owner per ownership capacity. Through December 31, 2010, the FDIC provides unlimited coverage for noninterest-bearing transaction accounts at FDIC-insured institutions participating in the agency’s Transaction Account Guarantee Program. Beginning December 31, 2010 through December 31, 2012, pursuant to the Dodd-Frank Act, deposits held in noninterest-bearing transaction accounts will be fully insured, regardless of the amount in the account, at all FDIC-insured institutions.

Revocable and irrevocable trust accounts that are held in insured deposit accounts may receive additional coverage based on the number of owners of the account and the number of beneficiaries of the account. Here is the FDIC summary of coverage for these accounts (for more information go to <http://www.fdic.gov/deposit/deposits/dis/index.html>):

Revocable Trust Accounts	\$ 250,000 per owner per qualified beneficiary up to 5 beneficiaries (more coverage available with 6 or more beneficiaries subject to specific limitations and requirements)
Irrevocable Trust Accounts	\$ 250,000 for the non-contingent, ascertainable interest of each beneficiary

### Bank Regulations<sup>5</sup>

Bank trust departments are extensively regulated not only to protect the interests of bank customers, but also to ensure the safety and soundness of the institution for the public good. With respect to fiduciary accounts, state and federal regulations address various aspects of these activities, including the fiduciary obligations of the bank, potential conflicts of interest, and the bank’s management of transactional, strategic, compliance, and reputational risks. In addition, the Employee Retirement Income Security Act of

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1974 (ERISA) and the Internal Revenue Code, as well as implementing regulations, largely govern the operation, structure and administration of employee benefit plans.

### Segregation of Duties<sup>6</sup>

To safeguard fiduciary assets, bank trust departments segregate and often rotate the duties of their employees who work in fiduciary accounts. Under such a regime, no one individual is able to authorize, execute, and review the processing of assets, including securities, cash, income payments, and corporate actions. These dual control procedures ensure that one person, acting alone, cannot complete all phases of a transaction or transfer client assets.

### Strict Regulation of Self-Dealing and Conflicts of Interest<sup>7</sup>

Bank regulations significantly restrict self-dealing and other conflicts of interest. Unlike the obligations in an agency relationship (such as with a registered investment adviser), bank fiduciaries may not simply disclose conflicts of interest in order to engage in certain transactions. Self-dealing is prohibited unless the consent of all beneficiaries has been obtained, is specifically allowed under the terms of the trust or state law, or is authorized under court order. Even when the duty of loyalty is waived, trustees must still comply with their many other fiduciary duties, including the duty to invest prudently.

### Annual Reviews of Fiduciary Accounts<sup>8</sup>

In addition to reviewing a fiduciary account before acceptance to determine whether it can be properly administered, a bank must annually review *all* of the assets in each fiduciary account. This annual review must evaluate whether the investments are appropriate, individually and collectively, for the particular account.

### Record Keeping Requirements<sup>9</sup>

In addition to records for tax and accounting purposes, corporate fiduciaries must maintain detailed records to document and confirm securities transac-

tions. Banks must record securities transactions daily in chronological order. The records must include the account name, description of the securities, amount purchased or sold, trade date, and name of the broker/dealer purchaser or seller. A separate order ticket for each securities transaction, whether executed or canceled, must also be maintained. The order ticket includes such details as the time the trade was placed or received by the bank and the type of order used such as market order, limit order or an order subject to special instructions.

### Annual or Continuous Audits<sup>10</sup>

In addition to imposing rigorous record-keeping obligations, banking regulations require annual or continuous audits of all significant fiduciary activities conducted by an audit committee. The fiduciary audit committee's adoption of a thorough audit program allows the bank's board to identify practices that contravene policies or violate fiduciary laws and regulations. The audit committee of the board of directors may not contain any officer who participates significantly in the administration of the bank's fiduciary activities.

### External Audits

FDIC-insured institutions with more than \$500 million in assets must be audited each year by an independent public accountant (IPA) who is licensed to practice and in good standing under state law. To ensure the accountant's reliability and adherence to good accounting and auditing practices, IPAs must be peer-reviewed each year in a manner consistent with the standards of the American Institute of Certified Public Accountants.

IPAs must audit and report on the bank's internal controls on financial reporting directly to the bank's board of directors. Federal bank regulators prohibit banks from limiting an IPA's legal liability for their audits and require that the IPA's audit work papers, policies and procedures be made available to the bank's examiners upon request.

### Corporate Fiduciary Examination<sup>11</sup>

Federal and state banking regulators routinely



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examine trust departments for compliance with laws and regulations, as well as the bank's management of various risks. These thorough on-site examinations occur at least every eighteen months. Some large institutions have examiners on-site within the bank's premises throughout the year to examine fiduciary activities continuously.

During an examination, examiners obtain and review a number of important trust department documents, including: (1) most recent committee minutes and information packages; (2) asset management organizational chart; (3) most recent financial reports, including budget and variance reports; (4) policies and procedures if significant changes or additions have been made since first examined; (5) the bank's asset management risk assessment; and (6) audit and compliance reports. In addition, examiners take a risk-weighted sample of fiduciary accounts, weighted towards more complex accounts or accounts with unique assets, to determine whether the accounts were opened in compliance with applicable law and bank policy and whether the risks of the account comport with the bank's business plan and risk tolerance.

### Information on Corporate Fiduciaries

All FDIC-insured institutions, as well as OCC-chartered trust companies, must disclose extensive financial information in quarterly reports known as Call Reports. These publicly available reports (<https://cdr.ffiec.gov/public/>) provide timely and accurate data regarding a bank's financial condition and the results of its operations. Bank regulators use the information in the Call Reports to monitor the institutions when not engaged in an on-site examination. The information provided in these reports is extensive and covers everything from the income and expenses of the bank as a whole, to the number of fiduciary accounts and the amount held in those accounts.

### Notes

- <sup>1</sup> In 1913 under the Federal Reserve Act, national banks were given authority to provide fiduciary services to the extent to which state banks and trust companies are permitted to act.
- <sup>2</sup> In other words, banks that provide investment advice for a fee through their trust departments are held to a higher fiduciary standard than registered investment advisers providing the same services.
- <sup>3</sup> Restatement (Third) of Trusts § 88.
- <sup>4</sup> Uniform Prudent Investor Act § 2(a).
- <sup>5</sup> See generally 12 CFR Part 9. State banking regulators look to OCC Regulation 9 as a guide for state-chartered institutions.
- <sup>6</sup> 12 CFR §9.13.
- <sup>7</sup> 12 CFR §9.12.
- <sup>8</sup> 12 CFR § 9.6.
- <sup>9</sup> 12 CFR § 9.8.
- <sup>10</sup> 12 CFR §9.9.
- <sup>11</sup> See OCC Handbooks on Asset Management, FDIC Trust Examination Manual, and OTS Trust Examination Manual.

*This document is provided with the understanding that the American Bankers Association is not engaged in rendering legal, accounting, or other professional services. If legal advice or other expert assistance is required, the services of a competent professional should be sought.*

*The American Bankers Association represents banks of all sizes and charters and is the voice for the nation's \$13 trillion banking industry and its two million employees. Learn more at [aba.com](http://aba.com).*