

SUPPORTING STATEMENT

A. Justification

1. Necessity For Information Collection

The Commission adopted, on July 16, 1992, Rules 17h-1T and 17h-2T (17 CFR 240.17h-1T and 17 CFR 240.17h-2T), or the risk assessment rules, pursuant to its authority under the risk assessment provisions of the Market Reform Act of 1990 (Pub. L. No. 101-432, 104 Stat. 963 (1990)). These Rules are intended to give the Commission access to information concerning the financial and securities activities of certain broker-dealer affiliates. A broker-dealer may be affected by the financial difficulties of an affiliate both directly, such as by the affiliate's withdrawal of capital to meet the affiliate's obligations, and indirectly, such as by the effect that the affiliate's difficulties may have on the broker-dealer's ability to obtain financing. This impact on a broker-dealer may be exacerbated in times of market stress. Accordingly, Rules 17h-1T and 17h-2T enable the Commission to monitor the activities of broker-dealer affiliates through its access to affiliate information and receipt of reports on a quarterly basis. In June of 2004 the Commission promulgated exemptions from Rules 17h-1T and 17h-2T broker-dealers that use Appendix E to Rule 15c3-1 and broker-dealers affiliated with a supervised investment bank holding company because their holding companies are required to make and retain documents and file reports that are substantially similar to, and contain the same information as, those the broker-dealer is required to make, retain, and file pursuant to Rules 17h-1T and 17h-2T.

Rule 17h-1T requires a broker-dealer to maintain and preserve records and other information concerning certain entities that are associated with the broker-dealer. This requirement extends to the financial and securities activities of the holding company, affiliates and subsidiaries of the broker-dealer that are reasonably likely to have a material impact on the financial or operational condition of the broker-dealer. Rule 17h-2T requires a broker-dealer to file with the Commission reports concerning the information required to be maintained and preserved under Rule 17h-1T within 60-calendar days after the end of each fiscal quarter. However Rule 17h-2T also allows a firm to file its year-end financial statements separately from the rest of its fiscal fourth quarter report, within 105 calendar days after the end of that quarter.¹

The Commission is statutorily authorized by Section 17(h) of the Securities Exchange Act of 1934 ("Exchange Act") (15 USC 78q(h)), to adopt rules that require a broker-dealer to maintain and preserve risk assessment information with respect to those entities that are associated with the broker-dealer whose "business activities are reasonably likely to have a material impact on the financial and operational condition" of the broker-dealer. In addition, Section 17(h) authorizes the Commission to adopt rules that require a broker-dealer to file, no more frequently than quarterly, summary reports of the information and records maintained pursuant to the risk assessment rules. Further statutory authority is found in Section 23(a) of the Exchange Act (15 USC 78w).

¹ Thus, the same information is filed with the Commission whether the broker-dealer files all the information within 60 calendar days after the end of the fiscal fourth quarter or some of the information within 60 calendar days and the rest within 105 calendar days after the end of the fiscal fourth quarter.

2. Purpose of, and Consequences of Not Requiring, the Information Collection

The information required by Rules 17h-1T and 17h-2T is necessary to enable the Commission to monitor the activities of a broker-dealer affiliate whose business activities is reasonably likely to have a material impact on the financial and operational condition of the broker-dealer. Without this information, the Commission would be unable to assess the potentially damaging impact of the affiliate's activities on the broker-dealer.

3. Role of Improved Information Technology and Obstacles to Reducing Burden

The collection of information is not yet collected through electronic submission. The staff is presently exploring possible ways to implement a system through which these reports could be collected electronically. However, issues remain with respect to data security and logistics.

4. Efforts To Identify Duplication

Not applicable; there is no duplicate of information.

5. Effects On Small Entities

The Rules generally do not apply to small entities because a broker-dealer that maintains less than \$20 million in capital and does not carry customer accounts is exempted under the Rules. Further, a broker-dealer that either restricts its business to certain mutual fund activities, certain direct participation programs or introduces accounts on a fully disclosed basis is also exempt under the Rules. In addition, a natural person is exempt from the Rules under Section 17(h) of the Exchange Act.

6. Consequences of Less Frequent Collection

The Rules enable the Commission to monitor the activities of a broker-dealer affiliate whose business activities is reasonably likely to have a material impact on the financial and operational condition of the broker-dealer. This information is collected quarterly. If the information were to be collected less frequently, the Commission would have to rely on stale and outdated information when assessing risks to the broker-dealer. As a result, the Commission would be unable to adequately assess the potentially damaging impact of more recent activities of certain broker-dealer affiliates on a broker-dealer.

7. Inconsistencies With Guidelines In 5 CFR 1320.5(d)(2)

The collection of information is not inconsistent with 5 CFR 1320.5(d)(2).

8. Consultations Outside the Agency

All Commission rule proposals are published in the Federal Register for public comment. This comment period is generally thirty days, which affords the public an opportunity to respond to any proposed rule changes.

9. Payment or Gift to Respondents

Not applicable.

10. Assurance of Confidentiality

The information required to be provided to the Commission pursuant to these Rules are deemed confidential, notwithstanding any other provision of law under Section 17(h)(5) of the Exchange Act and Section 552(b)(3)(B) of the Freedom of Information Act.

11. Sensitive Questions

Not applicable; questions of a sensitive nature are not asked.

12. Estimate of Respondent Reporting Burden

There are currently 200 respondents that must comply with Rules 17h-1T and 17h-2T. Each of these 200 respondents require approximately 10 hours per year, or 2.5 hours per quarter, to maintain the records required under Rule 17h-1T, for an aggregate annual burden of 2,000 hours (200 respondents X 10 hours). In addition, each of these 200 respondents must make five annual responses under Rule 17h-2T (for a total of 1,000 responses per year). These five responses require approximately 14 hours per respondent per year, or 3.5 hours per quarter, for an aggregate annual burden of 2,800 hours (200 respondents X 14 hours). In addition, there are approximately five new respondents per year² that must draft an organizational chart required under Rule 17h-1T and establish a system for complying with the Rules. The staff estimates that drafting the required organizational chart requires one hour and establishing a system for complying with the Rules requires three hours, thus requiring an aggregate of 20 hours (5 new respondents X 4 hours). Thus, the total compliance burden per year is approximately 4,820 burden hours (2,000 + 2,800 + 20).

The staff estimates that approximately 2/3 of the total compliance burden hours, or 3,213 hours, are performed by Compliance Clerks at \$68.00 per hour (based on the average annual salary for a Compliance Clerk based inside New York City of \$42,000, as reflected in the SIA Office Salaries in the Securities Industry for 2005, modified to account for an 1,800-hour work-year and multiplied by 2.92³ to account for bonuses, firm size, employee benefits and overhead),

² However, the staff further estimates that the number of respondents decreases by at least that many firms per year as a result of mergers and other business factors.

³ The SIA recently spoke with the Commission's Office of Economic Analysis to inform the Commission that the multiplier of 1.35 that the Commission has historically used was too low. The SIA informed the Commission that, with increasing health care costs, the fact that the largest firms that pay

for a cost of \$218,484. In addition, the staff estimates that approximately 1/3 of the total compliance burden hours, or 1,607 hours, are performed by Compliance Managers at \$205 per hour (based on the average annual salary for a Compliance Manager based inside New York City of about \$69,000, as reflected in SIA Management and Professional Earnings for 2005, modified to account for an 1,800-hour work-year and multiplied by 5.35⁴ to account for bonuses, firm size, employee benefits and overhead), for a cost of \$329,435. Thus, the estimated total compliance burden cost per year is \$547,919 (\$218,484 + \$329,435).

13. Estimate of Total Annualized Cost Burden

The estimated total annualized cost burden for Rules 17h-1T and 17h-2T is \$0. Other than provided for in item number 12 above, it is not anticipated that any of the respondents will incur additional operational or maintenance costs.

14. Estimate of Cost to Federal Government

The operational cost to the Federal Government and the related overhead to review the respondents' filings under Rule 17h-2T is approximately \$362,000. The staff estimates that reviewing these filings requires approximately 4,000 burden hours of staff time. About half of that time is professional staff time at approximately \$122 per hour (based on an annual salary of \$146,000 for professional labor, and adding average fringe benefits of 26% and average overhead of 25%), for a cost of \$244,000. The other half is para-professional staff time at approximately \$59 per hour (based on an annual salary of \$70,000 for para-professional labor, and adding average fringe benefits of 26% and average overhead of 25%), for a cost of \$118,000. There is no operational cost to the Federal Government or related overhead with respect to Rule 17h-1T. Thus, the total cost to the Federal Government is approximately \$362,000 (\$244,000 + \$118,000).

15. Explanation of Changes in Burden

The change in burden is a result of changes to four factors included in the calculation. First, there was an increase in the number of respondents from 148 to 200. Second, there was a change to the multiplier used to calculate the salary costs for broker-dealer employees.⁵ Third, there was a change to the manner in which the total annual burden hours for the Federal Government were divided between employees. Finally, both the salary figures for the broker-dealer employees and the Federal Government employees were updated.

higher salaries generally fail to respond to the SIA's salary survey, and other factors, the Commission should increase its multipliers. Consequently, the Commission and the SIA worked together to determine the level at which the multipliers should be set.

⁴ *Id.*

⁵ See explanation at footnote 3.

16. Information Collection Planned for Statistical Purposes

Not applicable.

17. Explanation as to Why Expiration Date Will Not Be Displayed

Not applicable.

18. Exceptions to Certification

Not applicable.

B. Collection of Information Employing Statistical Methods

The collection of information does not employ statistical methods, nor would the implementation of such methods reduce the burden or improve the accuracy of results.