

Rule 17i-6: Reporting Requirements for Supervised Investment Bank Holding Companies

SUPPORTING STATEMENT

A. Justification

1. Necessity For Information Collection

Section 231 of the Gramm-Leach-Bliley Act of 1999<sup>1</sup> (the “GLBA”) amended Section 17 of the Securities Exchange Act of 1934 (the “Exchange Act” or the “Act”) to create a regulatory framework under which a holding company of a broker-dealer may voluntarily be supervised by the Commission as a supervised investment bank holding company (or “SIBHC”).<sup>2</sup> In 2004, the Commission promulgated rules, including Rule 17i-6, to create a framework for the Commission to supervise SIBHCs.<sup>3</sup> This framework includes qualification criteria for investment bank holding companies (“IBHCs”) that file notices of intention to be supervised by the Commission, as well as recordkeeping and reporting requirements for SIBHCs. Taken as a whole, the SIBHC framework permits the Commission to better monitor the financial condition, risk management, and activities of a broker-dealer’s parent and affiliates on a group-wide basis. In particular, it creates a formal process through which the Commission can access important information regarding activities of a broker-dealer’s affiliates that could impair the financial and operational stability of the broker-dealer or the SIBHC.

In addition, securities firms that do business in the European Union (“EU”) have indicated that they may need to demonstrate that they have consolidated supervision at the holding company level that is “equivalent” to EU consolidated supervision.<sup>4</sup> The enactment of Section 17(i) of the Exchange Act was also intended to address this concern.<sup>5</sup> This regulatory framework for SIBHCs is intended to provide a basis for non-U.S. financial regulators to treat the Commission as the principal U.S. consolidated, home-country supervisor for SIBHCs and their affiliated broker-dealers.<sup>6</sup> This would minimize duplicative regulatory burdens on broker-dealers that are active in the EU and in other jurisdictions that may have similar laws.

Pursuant to Section 17(i)(3)(A) of the Exchange Act, an SIBHC must make and keep records, furnish copies thereof, and make such reports as the Commission may require by rule.<sup>7</sup> Rule 17i-6 requires that an SIBHC file with the Commission certain monthly and quarterly reports and an annual audit report.

---

1 Pub. L. No. 106-102, 113 Stat. 1338 (1999).

2 See 15 U.S.C. 78q(i).

3 See Exchange Act Release No. 49831 (Jun. 8, 2004), 69 FR 34472 (Jun. 21, 2004).

4 See “Directive 2002/87/EC of the European Parliament and of the Council of 16 December 2002.”

5 See H.R. Conf. Rep. No. 106-434, 165 (1999).

6 See Exchange Act Release No. 49831, at 6 (Jun. 8, 2004), 69 FR 34472, at 34473 (Jun. 21, 2004).

7 15 U.S.C. 78q(i)(3)(A).

The collections of information required by Rule 17i-6 are necessary to allow the Commission to effectively determine whether supervision of an IBHC as an SIBHC is necessary or appropriate in furtherance of the purposes of § 17 of the Act and allow the Commission to supervise the activities of these SIBHCs. Rule 17i-6s also enhances the Commission's supervision of the SIBHCs' subsidiary broker-dealers through collection of additional information and inspections of affiliates of those broker-dealers.

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

The reporting requirements set forth in Rule 17i-6 are designed to inform the Commission about the activities of the SIBHC, as well as the financial condition, policies, systems for monitoring and controlling financial and operational risks, and transactions and relationships involving the affiliate group. In addition, these requirements are designed to keep the Commission informed of the extent to which the SIBHC or its affiliates have complied with the provisions of the Exchange Act, and regulations prescribed and orders issued under the Exchange Act.

Without these reports, the Commission would be unable to adequately supervise an SIBHC, nor would it be able to determine whether continued supervision of an IBHC as an SIBHC were necessary and appropriate in furtherance of the purposes of § 17 of the Act.

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

Rule 17i-6 was not designed to collect information through electronic submission.

The Commission designed Rule 17i-6 so an IBHC could compile and submit existing documents (as opposed to requiring that an IBHC create additional documents or fill out a new form or forms) in order to decrease any costs or burdens involved with the rule. Further, those existing documents may be created and maintained by the SIBHC in a diverse range of formats.

## 4. Efforts To Identify Duplication

No duplication is apparent.

## 5. Effects On Small Entities

An IBHC can apply to become an SIBHC only if it is not affiliated with an insured bank or a savings association,<sup>8</sup> (ii) a foreign bank, foreign company, or a company that is described in section 8(a) of the International Banking Act of 1978, or (iii) a foreign bank that controls a corporation chartered under section 25A of the Federal Reserve Act.<sup>9</sup> In addition, pursuant to paragraph (d)(2)(i)(B) of Rule 17i-2, the Commission would not consider such supervision necessary or appropriate unless the investment bank holding company demonstrates that it owns or controls a broker or dealer that has a substantial presence in the securities business, which

---

8 Exchange Act § 17(i)(1)(A)(i) [15 U.S.C. 78q(i)(1)(A)(i)].

9 Federal Reserve Act § 25A [12 U.S.C. 611].

may be demonstrated by a showing that the broker or dealer maintains tentative net capital of \$100 million or more. Accordingly, neither an IBHC nor an SIBHC could be a small entity.<sup>10</sup>

6. Consequences of Less Frequent Collection

Pursuant to Rule 17i-6, the SIBHC must file monthly and quarterly reports and annual audits. These reports will allow the Commission to review and monitor the risk profile of the SIBHC. Further, they will alert the Commission to any deterioration in the SIBHC's financial or operational position and risk profile. To the extent they are filed less frequently, the financial condition of an SIBHC could seriously decline before the Commission became aware of it, which could jeopardize the financial and operational condition of the SIBHC's affiliated broker-dealers and could possibly pose a risk to the securities marketplace.

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 (but for Rule 17i-6 it was 90 days), which affords the public an opportunity to respond to the proposed rule changes.

9. Payment or Gift to Respondents

Not applicable.

10. Assurance of Confidentiality

Pursuant to Exchange Act § 17(j)<sup>11</sup> and Section 552(b)(3)(B) of the Freedom of Information Act,<sup>12</sup> notwithstanding any other provision of law, the Commission cannot be compelled to disclose any information required to be reported under §17(i). Section 17(j) states, [f]or purposes of section 522 of title 5 United States Code [commonly referred to as the Freedom of Information Act], this subsection shall be considered a statute described in subsection (b)(3) (B) of section 552," and "the Commission shall designate information described in or obtained pursuant to this section as confidential information for purposes of Exchange Act § 24(b)(2)."<sup>13</sup> In addition, paragraph 17i-6(h) specifies that all reports and statements filed by an SIBHC in accordance with Rule 17i-6 shall be accorded confidential treatment.

11. Sensitive Questions

Not applicable. Questions of a sensitive nature are not asked.

<sup>10</sup> See 17 CFR 240.0-10(c).

<sup>11</sup> 15 U.S.C. 78o(j).

<sup>12</sup> 5 U.S.C. 552(b)(3)(B).

<sup>13</sup> 15 U.S.C. 78x(b)(2).

## 12. Estimate of Respondent Reporting Burden

As of March 31, 2006, approximately 140 registered broker-dealers reported their tentative net capital as being over \$100 million.<sup>14</sup> Many of these broker-dealers are affiliated with another broker-dealer that reported its tentative net capital as being more than \$100 million. Approximately 35 could not be supervised by the Commission as an SIBHC due to the fact that each is either: (i) affiliated with an insured bank or a savings association,<sup>15</sup> (ii) a foreign bank, foreign company, or a company that is described in section 8(a) of the International Banking Act of 1978, or (iii) a foreign bank that controls a corporation chartered under section 25A of the Federal Reserve Act.<sup>16</sup> In addition, some broker-dealers may not be active in jurisdictions that require securities firms to demonstrate that they have consolidated supervision at the holding company level that is equivalent to EU consolidated supervision, or may not find it to be cost-effective to register as an SIBHC for other reasons.<sup>17</sup> Thus, the Commission estimates that three IBHCs will file notices of intent to be supervised by the Commission as SIBHCs.

An SIBHC will require about 8 hours each month to prepare and file the monthly reports required by this rule (or approximately 96 hours per year).<sup>18</sup> On average, it will take an SIBHC about 16 hours each quarter (or 64 hours each year)<sup>19</sup> to prepare and file the quarterly reports required by this rule. An SIBHC will require about 200 hours to prepare and file the annual audit reports required by this rule. Consequently, the total annual burden of Rule 17i-6 on all SIBHCs is approximately 1,080 hours.<sup>20</sup>

Rule 17i-6 requires that an SIBHC file certain monthly and quarterly reports with the Commission, as well as an annual audit report. The average cost for an SIBHC to prepare and file the monthly reports is about \$1,920 per month, and thus approximately \$23,040 per year.<sup>21</sup>

14 Per March 31, 2006, FOCUS Report filings. Broker-dealers are required to file monthly and/or quarterly reports on Form X-17A-5 pursuant to Rule 17a-5(a) (17 CFR 240.17a-5(a)), commonly referred to as FOCUS Reports.

15 See note 8.

16 See note 9.

17 Broker-dealers that have more than \$1 billion in tentative net capital can elect to calculate market and credit risk capital charges using mathematical modeling techniques if their holding company volunteers to be subject to consolidated supervision by the Commission under an alternative supervisory framework (See Exchange Act Release 34-49830 (Jun. 8, 2004), 69 FR 34428 (Jun. 21, 2004)). Consequently, broker-dealers that are able to do so generally will elect that supervisory framework over the SIBHC framework. As of March 31, 2006 (See note 14), 33 broker-dealers reported having tentative net capital over \$1 billion.

18 (8 hours x 12 months in a year) = 96 hours/year.

19 (16 hours x 4 quarters in a year) = 64 hours/year.

20 (96 hours per year to prepare and file monthly reports + 64 hours each year to prepare and file quarterly reports + 200 hours each year to prepare and file annual audit reports) x 3 SIBHCs = 1,080 hours.

21 We believe that an SIBHC would have a Senior Accountant prepare and file these reports. According to the Securities Industry Association (or "SIA"), the hourly cost of a

On average, an SIBHC will incur a quarterly cost of \$3,840 to prepare and file the required quarterly reports, and thus will incur an annual cost of \$15,360 to file these reports.<sup>22</sup> Finally, an SIBHC, on average, will incur an annual cost of \$49,800 to prepare and file an annual audit.<sup>23</sup> Thus, the total dollar cost of the ongoing paperwork burden associated with Rule 17i-6 is approximately \$264,600.<sup>24</sup>

### 13. Estimate of Total Annualized Cost Burden

The information technology (“IT”) systems used by IBHCs to manage risk, make and retain records and reports, and calculate capital differ widely based on the types of business and the size of the IBHC. We believe that an IBHC will upgrade its IT systems with relation to four of the SIBHC framework Rules: Rule 17i-4 (requires an SIBHC to document its internal risk management control systems), Rule 17i-5 (requires an SIBHC to create and maintain records), Rule 17i-6 (requires an SIBHC to create and make reports to the Commission), and Rule 17i-7 (requires that an SIBHC compute allowable capital and allowances for market, credit, and operational risk). It is impossible to determine what percentage of these IT systems costs may be attributable to any particular SIBHC framework Rule, so we will allocate them equally (i.e., 25% of the total cost to each of these four Rules). We believe the costs to upgrade IT systems would be one-time costs.

These IBHCs’ IT systems may be in varying stages of readiness to meet the requirements of the rules. The staff estimated, when these rules were proposed, that it would cost an IBHC between \$1 million and \$10 million to upgrade its IT systems to comply with the SIBHC framework of rules, depending on the state of development of its IT systems. We believe this estimate to be fairly sound because no commenter disagreed with it. Thus, on average, it would

---

Senior Accountant in New York City is \$240, as reflected in the SIA’s *Report on Management and Professional Earnings for 2005*, and modified to account for an 1,800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead. (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 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.)  $(\$240 \times 8 \text{ hours}) = \$1,920$ .  $(\$1,920 \times 12 \text{ months}) = \$23,040$ .

22 We believe that an SIBHC would have a Senior Accountant prepare and file these reports. As stated above in note 21, the hourly cost of a Senior Accountant is \$240.  $(\$240 \times 16 \text{ hours}) = \$3,840$ .  $(\$3,840 \times 4 \text{ quarters}) = \$15,360$ .

23 We believe that an SIBHC would have a Senior Internal Auditor work with accountants to prepare and file these reports. According to the SIA, the hourly cost of a Senior Internal Auditor is \$249, as reflected in its *Report on Management and Professional Earnings for 2005*, and modified to account for an 1,800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead (see note 21).  $(\$249 \times 200 \text{ hours}) = \$49,800$ .

24  $((\$23,040 + \$15,360 + \$49,800) \times 3 \text{ SIBHCs}) = \$264,600$ .

cost each of the three SIBHCs about \$5.5 million to upgrade their IT systems, or approximately \$16.5 million in total. As described above, we allocate approximately 25% of this cost, or \$4,125,000, as attributable to Rule 17i-6.

14. Estimate of Cost to Federal Government

There would be no additional costs to the Federal Government.

15. Explanation of Changes in Burden

The changes in burden estimates are a result of changes to two factors included in the calculation. First, there was a change to the multiplier used to calculate the salary costs for broker-dealer employees.<sup>25</sup> Second, the salary figures for the broker-dealer employees were updated.

16. Information Collection Planned for Statistical Purposes

Not applicable. There is no intention to publish the information for any purpose.

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.

---

25 See note Error: Reference source not found.