

Rule 17i-2: Notice of Intention to be Supervised by the Commission as a Supervised Investment  
Bank Holding Company

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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 (“investment bank holding company” or “IBHC”) may voluntarily be supervised by the Commission as an supervised investment bank holding company (or “SIBHC”).<sup>2</sup> In 2004, the Commission promulgated rules, including Rule 17i-2, to create a framework for the Commission to supervise SIBHCs.<sup>3</sup> This framework includes qualification criteria for SIBHCs, as well as recordkeeping and reporting requirements. 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.

Section 17(i)(1)(B) of the Exchange Act states that in order to elect to become an SIBHC, an IBHC must file with the Commission a written notice of intention to become supervised by the Commission in such form and containing such information and documents concerning the IBHC as the Commission, by rule, may prescribe as necessary and appropriate in furtherance of the purposes of Section 17 of the Act (a “Notice of Intention”).<sup>7</sup> Rule 17i-2

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

provides the method by which an IBHC can elect to become an SIBHC. In addition, Rule 17i-2 indicates that the IBHC will automatically become an SIBHC 45 days after the Commission receives its completed Notice of Intention unless the Commission issues an order indicating either that it will begin its supervision sooner or that it does not believe it to be necessary or appropriate in furtherance of Section 17 of the Act for the IBHC to be so supervised. Finally, Rule 17i-2 sets forth the criteria the Commission would use to make this determination.

The collections of information included in Rule 17i-2 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. In addition, these collections are needed so that the Commission can adequately supervise the activities of these SIBHCs. Finally, these rules enhance 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 information and documents an IBHC is required to include in its Notice of Intention pursuant to Rule 17i-2 are necessary to enable the Commission to evaluate whether it is necessary and appropriate in the furtherance of Section 17 of the Exchange Act for the Commission to supervise an IBHC as an SIBHC. Without this information, the Commission would be unable to make this evaluation.

In addition, the updates to the Notice of Intention are needed so the Commission can adequately monitor the financial condition, risk management, and activities of SIBHCs on a group-wide basis. Without this information, the Commission could make an incorrect determination to supervise an IBHC as an SIBHC based on outdated, incorrect information, or the Commission may remain unaware of material changes to an SIBHC's mathematical model (which could significantly affect the financial or operational risks of the affiliate group).

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

Rule 17i-2 is not designed to collect information through electronic submission. The Commission designed Rule 17i-2 so an IBHC could compile and submit existing documents with its Notice of Intention (as opposed to requiring that an IBHC create additional documents) in order to decrease any costs or burdens involved with this rule. Further, those existing documents may be created and maintained by the IBHC in a diverse range of formats. Finally, the filing of a Notice of Intention is intended to be a one-time filing. Thus, improved technology would not reduce the burden.

## 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 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

If this information is not collected as frequently, the Commission will be unable to ascertain, on an ongoing basis, whether supervision of an IBHC as an SIBHC or continued supervision of an SIBHC is necessary and appropriate in furtherance of the purposes of Section 17 of the Exchange Act.

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-2 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

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].

10 See 17 CFR 240.0-10(c).

11 15 U.S.C. 78o(j).

12 5 U.S.C. 552(b)(3)(B).

pursuant to this section as confidential information for purposes of Exchange Act § 24(b)(2).”<sup>13</sup> In addition, paragraph 17i-2(d)(1) states that all Notices of Intention, amendments, and other documentation and information filed pursuant to Rule 17i-2 will be accorded confidential treatment to the extent permitted by law.

11. Sensitive Questions

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

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 cannot 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> When the SIBHC rule framework was finalized in 2004, the Commission estimated that three IBHCs would file notices of intent to be supervised by the Commission as SIBHCs. No IBHC has yet filed such a notice, however the Commission still believes that three IBHCs will file such Notices.

Each IBHC that files a Notice of Intention to become supervised by the Commission will require approximately 900 hours to draft a Notice of Intention, compile the various documents to be included with the Notice of Intention, and work with the Commission staff. Further, each IBHC likely will have an attorney review its Notice of Intention, and it will take the attorney approximately 100 hours to complete such a review. Consequently, we estimate the total burden

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13 15 U.S.C. 78x(b)(2).

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 *supra* note 8.

16 See *supra* 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.

for all three firms to be approximately 3,000 hours.<sup>18</sup> We believe this would be a one-time burden.

Rule 17i-2 also requires that an IBHC/SIBHC update its Notice of Intention on an ongoing basis.<sup>19</sup> Each IBHC/SIBHC will require approximately 2 hours each month to update its Notice of Intention, as necessary. Thus, we estimate that it will take the three IBHC/SIBHCs, in the aggregate, about 72 hours each year to update their Notices of Intention.<sup>20</sup>

Thus, the total burden relating to Rule 17i-2 for all SIBHCs is approximately 3,072 hours in the first year,<sup>21</sup> and approximately 72 hours each year thereafter.

We estimate that each IBHC that files a Notice of Intention to become supervised by the Commission as an SIBHC will incur a cost of approximately \$184,500 to have a Compliance Manager draft a Notice of Intention, compile the various documents to be included with the Notice of Intention, and work with the Commission staff.<sup>22</sup> We estimate that each such IBHC will incur a cost of approximately \$32,400 to have an Attorney review the Notice of Intention.<sup>23</sup> Consequently, we estimate that the total cost the three IBHCs that file Notices of Intention to become supervised by the Commission as SIBHCs will incur is about \$650,700.<sup>24</sup> We estimate that each SIBHC thereafter will incur a cost of approximately \$4,920 each year to make any

18 (900 hours + 100 hours) x 3 IBHCs/SIBHCs = 3,000 hours.

19 An IBHC would be required to review and update its Notice of Intention to the extent it becomes inaccurate prior to a Commission determination, and an SIBHC would be required to update its Notice of Intention if it changes a mathematical model used to calculate its risk allowances pursuant to Rule 17i-7 after a Commission determination was made.

20 (2 hours x 12 months each year) x 3 SIBHCs = 72.

21 ((900 hours + 100 hours) x 3 IBHCs/SIBHCs) + ((2 hours x 12 months each year) x 3 SIBHCs).

22 According to the Securities Industry Association (or "SIA"), the hourly cost of a Compliance Manager based in New York City is \$205, 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.) (\$205 x 900 hours) = \$184,500.

23 According to the SIA, the hourly cost of an Attorney based in New York City is \$324, 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. *See also* note 22. (\$324 x 100 hours) = \$32,400.

24 (\$184,500 + \$32,400) x 3 SIBHCs = \$650,700.

necessary updates to its Notice of Intention, or, in aggregate, about \$14,760 each year for all SIBHCs.<sup>25</sup> Therefore, we estimate the total dollar cost of the one-time and ongoing paperwork burden associated with Rule 17i-2 to be approximately \$665,460.<sup>26</sup>

13. Estimate of Total Annualized Cost Burden

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

14. Estimate of Cost to Federal Government

There will 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>27</sup> Second, the salary figures for the broker-dealer employees were updated.

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.

<sup>25</sup> We believe an SIBHC will have a Compliance Manager perform this task. According to the SIA, the hourly cost of a Compliance Manager based in New York City is \$205, 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. See also note 22. (24 hours x \$205) = \$4,920.  
((\$4,920 x 3 SIBHCs) = \$14,760.

<sup>26</sup> (\$650,700 + \$14,760) = \$665,460.

<sup>27</sup> See note 22.