

## SUPPORTING STATEMENT - RULE 17Ad-13

### A. Justification

#### (1) Necessity for Information Collection

As a result of the paperwork crisis that occurred in the late 1960's, during which the number of securities transactions exceeded the securities industry's capacity to process those transactions, Congress enacted the Securities Acts Amendments of 1975.<sup>1</sup> In order to establish a national system for the prompt and accurate clearance and settlement of securities transactions, Congress provided for a scheme of regulation with respect to the business of being a transfer agent. Those amendments to the Securities Exchange Act of 1934 (the "Exchange Act") require transfer agents to meet minimum standards as established by the Commission in furtherance of the purposes of the Exchange Act and generally to protect investors.

Transfer agents play an integral role in the national system for the clearance and settlement of securities transactions. Transfer agents cancel certificates presented for transfer, issue new certificates to the transferee and record the change of record ownership of securities on the issuers securityholder records. They also prepare, maintain and certify securityholder records, disburse dividend and interest payments and mail securityowner communications such as proxy materials and annual reports to shareholders.

To the extent transfer agents fail to perform their activities promptly, accurately, and safely, the entire clearance settlement and transfer process suffers. Substandard performance by transfer agents can effect the accuracy of an issuers securityowner records and, thus, interrupt the channels of communication between issuers and shareowners. Moreover, the absence of adequate internal accounting controls in the operation of transfer agents and procedures for the safeguarding of funds and securities in the possession or control of transfer agents can provide the opportunity for significant financial loss to securityholders, issuers, financial intermediaries and securities depositories.

Based on experience in the operation of the transfer agent regulatory program, the Commission adopted Rule 17Ad-13 which was designed to require certain registered transfer agents to obtain an annual report on the adequacy of internal accounting controls. Because the safe and accurate flow and recording of a large volume of securities transfers is dependent upon the adequacy, accuracy, and reliability of those controls and procedures, the Commission believed that an adequate system of internal accounting controls and procedures for safeguarding funds and securities was critical to the establishment of an accurate and safe clearance and settlement system for securities transactions.

Rule 17Ad-13 exempts issuers that perform transfer agent functions solely for their own securities and certain transfer agents that qualify under the rule as "small" transfer agents. The rule also permits the federal bank regulatory agencies to exempt bank transfer agents subject to their jurisdiction that are not otherwise exempt as small transfer agents or issuer-transfer agents,

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<sup>1</sup> <sup>?</sup> Pub. L. No. 94-29, 89 Stat. 97 (June 4, 1975).

provided that a report similar in scope to the report required by Rule 17Ad-13 is prepared by the bank's internal auditors for the bank's board of directors or an audit committee of the board of directors. The federal bank regulatory agencies have taken appropriate action and Rule 17Ad-13 applies primarily to professional independent transfer agents that perform transfer agent functions on behalf of other issuers, including affiliated issuers. The Commission believes that the benefits of Rule 17Ad-13 to the transfer agent community, public investors and the federal regulatory agencies far outweigh the compliance costs placed on the approximately 200 transfer agents subject to the audit requirement of the rule.

The report required by the rule must be prepared by an independent public accountant and filed with the appropriate regulatory agency. The report is required to be prepared on the basis of an annual examination of the internal accounting controls and procedures for safeguarding funds and securities used in the transfer agent's operations. The accountant must report and comment on any material weakness found to exist as of the date of the examination in the system of internal accounting controls and in the procedures for safeguarding funds and securities.

If the accountant's report specifies any "material weaknesses," the transfer agent receiving that report must indicate in writing to the appropriate regulatory agency and to the accountant, within thirty calendar days of receipt of the accountant's report, the corrective action taken, or planned to be taken, by the transfer agent. Sixty calendar days thereafter, the transfer agent must obtain from the accountant and forward to the appropriate regulatory agency a written statement regarding whether the corrective action has been implemented. If no corrective action has been taken, the transfer agent must give reasons for this.

Finally, the rule requires that the accountant's report and all other documents required by the rule be maintained for at least three years, and it must be maintained in the first year in an easily accessible place.

The Commission believes that the benefits of this rule to the transfer agent community, public investors, and the federal regulatory agencies far outweigh the compliance costs placed on transfer agents. Transfer agents are fully informed of the adequacy of their systems of internal accounting controls and their procedures for safeguarding funds and securities that come into their possession or custody. That information facilitates transfer agent efforts to establish and to maintain sufficient controls and procedures. In addition, public investors, who must use the services of transfer agents to become record owners of securities issues, also should experience fewer delays and inaccuracies in receiving their securities and related distributions from, and in the recording of ownership interests by transfer agents.

Further, while an independent audit will not replace examinations by the federal regulatory agencies charged with inspecting registered transfer agents, those agencies can enhance their ability to focus on those transfer agents that are experiencing serious difficulties. More importantly, the federal regulatory agencies can rely, in the first instance, on the efforts of

transfer agents and their accountants to remedy any problems without extensive government involvement.

The Commission adopted Rule 17Ad-13 pursuant to authority under Sections 17, 17A and 23(a) of the Act, 15 U.S.C. 78q, 78q-1 and 78w(a).

(2) Purposes of and Consequences of Not Requiring the Collection of Information

The report required under Rule 17Ad-13 is used by transfer agents to evaluate and, where necessary, improve the adequacy of their internal accounting controls and procedures for the safeguarding of funds and securities in their possession or control. The report also is used by the appropriate regulatory agency in examinations of transfer operations. The Commission believes that if the accountant reports were not prepared, serious transfer agent deficiencies in the safeguarding of securities and funds could go undetected and unremedied and result in substantial losses to public investors.

(3) Role of Improved Information Technology and Obstacles to Reducing Burden

There are no legal or technical obstacles which if removed would reduce burdens.

(4) Efforts to Identify Duplication

For transfer agents affected by Rule 17Ad-13, the information required by the rule is not otherwise available.

(5) Effects on Small Entities

Small transfer agents are exempt from Rule 17Ad-13.

(6) Consequences of Less Frequent Collection

The Commission believes that less frequent audits would greatly increase risks posed to public investors and the securities industry by transfer agent deficiencies in the safeguarding of securities and funds or operational difficulties.

(7) Inconsistencies with Guidelines in 5 CFR 1320.5(d)(2)

The collection is conducted in a manner consistent with the guidelines in 5 CFR 1320.5(d)(2).

(8) Consultations Outside the Agency

The Commission communicated with, and requested the views of, the Comptroller of the

Currency, the Board of Governors of the Federal Reserve System, and the Federal Deposit Insurance Corporation. The Commission communicates on a continuous basis with these organizations, and has not received any indication of major problems with Rule 17Ad-13. The Commission also communicates with many registered transfer agents on a continuous basis and has not discovered any major problems with Rule 17Ad-13.

(9) Payment of Gift to Respondents

Not applicable.

(10) Assurances of Confidentiality

This rule does not involve the collection of confidential information.

(11) Sensitive Questions

No questions of a sensitive nature are asked.

(12) Estimate of Respondent Reporting Burden

Approximately 200 independent, professional transfer agents must file the accountant's report annually. The Commission estimates that each report can be completed in 175 hours resulting in a total of 35,000 hours annually (175 hours x 200 reports). The burden was estimated using Commission review of filed Rule 17Ad-13 reports and Commission conversations with transfer agents and accountants.

(13) Estimate of Total Annualized Cost Burden

Not applicable; (a) it is not anticipated that respondents will have to incur any capital and start up cost to comply with the rule; (b) it is not anticipated that the respondents will have to incur any additional operational or maintenance cost (other than provided for in item no. 12) to comply with the rule.

(14) Estimated Cost to Federal Government

Cost to the Federal Government results from appropriate regulatory agency staff time, and related overhead devoted to review of Rule 17Ad-13 reports. Although staff time necessary for review will vary with each report, the Commission estimates that on average 1 hour of staff time is needed to review each of the approximate 200 reports received annually. Based on these estimates and the GSA Guide to Estimating Reporting Costs (1973), the cost to the Federal Government totals \$6,853.00.

(15) Explanation of Changes in Burden

There are no changes in burden.

(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

No statistical methods are employed in connection with the collections of information.