

PAPERWORK REDUCTION ACT SUBMISSION

Rule 301

Supporting Statement

A. Justification

1. Necessity for Information Collection.

The Securities Exchange Act of 1934, as amended (“Act”)¹, sets forth a scheme of self-regulation in which national securities exchanges have primary responsibility for regulating their members and enforcing compliance by members and their associated persons with the Act, the rules thereunder and exchange rules. Under the Act, the Commission is charged with the responsibility for supervising and assuring that exchanges comply with and advance the policies of the Act.

In the 1975 Amendments to the Act,² Congress specifically endorsed the development of a national market system (“NMS”) and sought to clarify and strengthen the Commission’s authority to promote the achievement of such a system. The growing use of technology has made it possible for commercial entities to centralize trading without the use of a floor, members or a non-profit structure.

The growing significance of alternative trading systems had far outstripped the Commission’s ability to effectively oversee such systems through existing broker-dealer regulation. Regulation ATS provides a regulatory structure that directly addresses issues related to alternative trading systems’ role in the marketplace. Regulation ATS allows alternative trading systems to choose between two regulatory structures. Alternative trading systems have the choice between registering as broker-dealers and complying with Regulation ATS or registering as national securities exchanges. Regulation ATS provides the regulatory framework for those alternative trading systems that choose to be regulated as broker-dealers.

Regulation ATS is composed of Rules 300, 301, 302, and 303. Rule 300 defines terms that provide the basis for alternative trading system regulation. Rule 301 sets forth the conditions that an alternative trading system must meet in order to be regulated as a broker-dealer. Rule 301 contains certain notice and reporting requirements, as well as additional obligations that only apply to alternative trading systems with significant volume. Rule 302 establishes a set of records relating to trading activity that the alternative trading system must make. Rule 303 establishes requirements for the preservation of certain records that alternative trading systems must make.

¹ 15 U.S.C. 78a et seq.

² Pub. L. No. 29, 89 Stat. 97 (1975).

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

Rule 301 describes the conditions with which an alternative trading system must comply to be registered as a broker-dealer. The Rule requires all alternative trading systems that wish to comply with Regulation ATS to file an initial operation report on Form ATS. The initial operation report requires information regarding operation of the system, including the method of operation, access criteria, and the types of securities traded. Alternative trading systems are also required to supply updates on Form ATS to the Commission, describing material changes to the system. In addition, Regulation ATS requires alternative trading systems to provide quarterly transaction reports on Form ATS-R. Alternative trading systems are also required to file cessation of operations reports on Form ATS. The gathering of such information permits the Commission to oversee the operation of such systems and track the growth of their role in the securities markets.

Alternative trading systems with significant volume are required to comply with requirements for fair access and systems capacity, integrity and security. Under Rule 301, such alternative trading systems are required to establish standards for granting access to trading on the system. In addition, upon a decision to deny or limit an investor's access to the system, an alternative trading system is required to provide notice to the investor of the denial or limitation and their right to an appeal to the Commission. Regulation ATS requires alternative trading systems to preserve any records made in the process of complying with the systems capacity, integrity and security requirements. In addition, such alternative trading systems are required to notify Commission staff of material systems outages and significant systems changes.

The Commission uses the information provided pursuant to the Rule to monitor the growth and development of alternative trading systems to confirm that investors effecting trades through the systems are adequately protected, and that the systems do not impede the maintenance of fair and orderly securities markets or otherwise operate in a manner that is inconsistent with the federal securities laws. In particular, the information collected and reported to the Commission by alternative trading systems enables the Commission to evaluate the operation of alternative trading systems with regard to national market system goals, and monitor the competitive effects of these systems to ascertain whether the regulatory framework remains appropriate to the operation of such systems.

Without the information provided on Forms ATS and ATS-R, the Commission would not have readily available information on a regular basis in a format that will allow it to determine whether such systems have adequate safeguards. Further, in the absence of the Rule, the Commission would not regularly obtain uniform trading data to identify areas where surveillance by self-regulatory organizations may be more appropriately tailored to the detection of fraudulent, deceptive and manipulative practices that may be peculiar to an automated trading environment. In sum, without the data required by the proposed Rule, the Commission would be limited in its ability to comply

with its statutory obligations, provide for the protection of investors, and promote the maintenance of fair and orderly markets.

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

The SEC's electronic filing project, called EDGAR for Electronic Data Gathering, Analysis & Retrieval, is designed to automate the filing, processing and dissemination of full disclosure filings. Ultimately, all SEC filings, including Forms ATS and ATS-R, will be considered for electronic submission. Such automation will increase the speed, accuracy and availability of information, generating benefits to investors and financial markets.

4. Efforts to Identify Duplication

Most of the records required to be made under the Rule reflect practices that prudent alternative trading systems would establish. Because most alternative trading systems would maintain much of the information required by the proposed Rule, no duplication occurs with respect to such information. To the extent that the Rule establishes new collections of information, there is no similar information available that could replace the information required.

5. Effect on Small Entities

The Rule is one of general applicability that mostly does not depend on the size of the system. Fair access reporting requirements and system capacity, integrity and security requirements only apply to alternative trading systems that have significant volume. The filing requirements on Forms ATS and ATS-R, however, apply to all alternative trading systems regardless of size under Regulation ATS. Therefore, the Rule could apply to small businesses. Pursuant to 17 CFR 240.0-10(c), the term "small business" or "small organization" when used in reference to a broker-dealer means a broker-dealer that has total capital (net worth plus subordinated liabilities) of less than \$500,000 on the date in the prior fiscal year as of which its audited financial statements were prepared pursuant to 17 CFR 240.17a-5(d) or, if not required to file such statements, a broker-dealer that had total capital of less than \$500,000 on the last business day of the preceding fiscal year (or in the time that it has been in business); and is not affiliated with any person (other than a natural person) that is not a small business or small organization as defined in 17 CFR 240.0-10. The Commission staff estimates that 5 alternative trading systems that would register as broker-dealers are small entities as currently defined by the Act.

Because the risks that the Commission monitors in the operation of an alternative trading system occur in any size business, the Commission has determined that the Rule must apply in the same manner to small as well as large entities. Hence, the Rule does not contain an exemption for small entities. However, the Commission notes that alternative trading systems that transact significant volume, and thus, are subject to the requirements of fair access, market transparency and coordination and systems capacity, integrity and security, are not likely to be small entities as defined by the Act.

6. Consequences of Less Frequent Collection

Without the information provided on Forms ATS and ATS-R, the Commission would not have readily available information on a regular basis in a format that will allow it to determine whether such systems have adequate safeguards. Further, in the absence of the Rule, the Commission would not regularly obtain uniform trading data to identify areas where surveillance by self-regulatory organizations may be more appropriately tailored to the detection of fraudulent, deceptive and manipulative practices that may be peculiar to an automated trading environment. In sum, less frequent collection of the data required by the proposed Rule would limit the ability of the Commission to comply with its statutory obligations, provide for the protection of investors, and promote the maintenance of fair and orderly markets.

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

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

8. Consultations Outside the Agency

Not applicable.

9. Payment or Gift to Respondents

The respondents receive no payments or gifts.

10. Assurance of Confidentiality

The records required by the proposed amendments are available only to the examination of the Commission staff, state securities authorities and the SROs. Subject to the provisions of the Freedom of Information Act, 5 U.S.C. § 522 (“FOIA”), and the Commission’s rules thereunder (17 CFR 200.80(b)(4)(iii)), the Commission does not generally publish or make available information contained in any reports, summaries, analyses, letters, or memoranda arising out of, in anticipation of, or in connection with an examination or inspection of the books and records of any person or any other investigation.

11. Sensitive Questions

Not applicable. No information of a sensitive nature is required under the rule.

12. Estimate of Respondent Reporting Burden

The Commission's estimated average reporting burden for each respondent to comply with Rule 301 of Regulation ATS is broken down as follows below. In each case, the estimated cost is derived from the Commission's estimate that the compensation paid to an employer of a broker-dealer or outside consultant to ensure compliance with Commission regulations is \$86.54/hour (equivalent to annual compensation of \$180,000 divided by 2080 payroll hours per years).

Also, in each case, the Commission estimates overhead costs (printing, supplies, copying and postage) to be approximately 35 percent of the value of labor costs. These estimates have been computed based on the GSA Guide to Estimating Reporting Costs (1973).

a. Form ATS - Initial Operation Report

Alternative trading systems that choose to register as broker-dealers and comply with Regulation ATS are required to file a Form ATS prior to commencing operations. The Commission estimates that the average burden for each respondent to file an initial operation report on Form ATS would be approximately 25 hours with an average cost of approximately \$2,244.64. This estimated cost is broken down as follows:

18 hours of in-house professional work at \$86.54/hr =	\$ 1,557.72
7 hours of clerical work at \$15/hr =	\$ 105.00
printing, supplies, copying and postage =	<u>\$ 581.95</u>
	\$ 2,244.64

b. Form ATS - Periodic Amendments to Update Information

Alternative trading systems that choose to register as broker-dealers and comply with Regulation ATS are required to file amendments to the initial operations report on Form ATS to provide notice of material systems changes and reflect other changes. The Commission estimates that the average burden for each respondent to file an amendment to Form ATS would be approximately 5 hours with an average total cost of approximately \$535.86. This estimated cost is broken down as follows:

4.5 hours of in-house professional work at \$86.54/hr =	\$389.43
0.5 hours of clerical work at \$15/hr =	\$ 7.50
printing, supplies, copying and postage =	<u>\$138.93</u>
	\$535.86

The Commission estimates that each respondent would file 2 amendments per year to report material systems changes for an estimated annual burden per respondent of 10 hours (2 amendments at 5 hours each per year) for an estimated total cost of \$1,071.72 (2 amendments at \$535.86 per filing).

c. Form ATS-R - Quarterly Reports

Alternative trading systems that choose to register as broker-dealers and comply with Regulation ATS are required to file quarterly reports on Form ATS-R. The Commission estimates that the average burden for each respondent to file an amendment to Form ATS would be approximately 4 hours with an average total cost of approximately \$370.74. This estimated cost is broken down as follows:

3 hours of in-house professional work at \$86.54/hr =	\$259.62
1 hour of clerical work at \$15/hr =	\$ 15.00
printing, supplies, copying and postage =	<u>\$ 96.12</u>
	\$370.74

Respondents would be required to file 4 quarterly reports on Form ATS-R each year. The Commission estimates that the average annual burden per respondent of 16 hours (4 quarterly reports at 4 hours per report) for an estimated total cost of \$1,482.96 (4 reports at \$370.74 per report).

d. Form ATS - Cessation of Operations Report

Alternative trading systems that choose to register as broker-dealers and comply with Regulation ATS are required to submit a notice on Form ATS when they are ceasing operations. The Commission estimates that the average burden for each respondent to file such a notice on Form ATS would be approximately 2 hours with an average total cost of approximately \$185.37. This estimated cost is broken down as follows:

1.5 hours of in-house professional work at \$86.54/hr =	\$ 129.81
0.5 hours of clerical work at \$15/hr =	\$ 7.50
printing, supplies, copying and postage =	<u>\$ 48.06</u>
	\$ 185.37

e. Fair Access Standards Recordkeeping

Alternative trading systems that choose to register as broker-dealers, comply with Regulation ATS and meet certain volume thresholds are required to establish standards for granting access on its trading system. Such alternative trading systems are required to make and keep such criteria, so such a requirement creates a recordkeeping burden for alternative trading systems. The Commission estimates that the average burden for each respondent to establish records relating to access standards would be approximately 5 hours with an average total cost of \$584.15. This estimated cost is broken down as follows:

5 hours of in-house professional work at \$86.54/hr =	\$432.70
printing, supplies, copying and postage =	<u>\$151.45</u>
	\$584.15

f. Fair Access Notices

Alternative trading systems that choose to register as broker-dealers, comply with Regulation ATS and meet certain volume thresholds are required to provide a notice to investors upon any decision to deny or limit their access to the system. The Commission estimates that the average burden for each respondent to provide such notices to such investors would be approximately 1 hour with an average total cost of approximately \$20.25. This estimated cost is broken down as follows:

1 hour of clerical work at \$15/hr =	\$15.00
printing, supplies, copying and postage =	<u>\$ 5.25</u>
	\$20.25

The Commission estimates that each respondent would provide approximately 27 notices per year for an average annual burden per respondent of 27 hours (27 notices at 1 hour per notice) and an estimated total cost of \$546.75 (27 notices at \$20.25 per report).

g. Systems Capacity, Integrity and Security Recordkeeping

Alternative trading systems that choose to register as broker-dealers, comply with Regulation ATS and meet certain volume thresholds are required to make records relating to any steps taken to comply with systems capacity, integrity and security requirements under Rule 301. The Commission estimates that the average burden for each respondent to make such records would be approximately 10 hours with an average total cost of approximately \$1168.29. This estimated cost is broken down as follows:

10 hours of in-house professional work at \$86.54/hr =	\$ 865.40
printing, supplies, copying and postage =	<u>\$ 302.89</u>
	\$1,168.29

h. Systems Outage Notices

Alternative trading systems that choose to register as broker-dealers, comply with Regulation ATS and meet certain volume thresholds are required to provide a notice to the Commission to report any systems' outages. The Commission estimates that the average burden for each respondent to provide such notices to the Commission would be approximately 0.25 hours with an average total cost of approximately \$29.21. This estimated cost is broken down as follows:

0.25 hours of in-house professional work at \$86.54/hr =	\$ 21.64
printing, supplies, copying and postage =	<u>\$ 7.57</u>
	\$29.21

The Commission estimates that each respondent would provide approximately 5 notices per year for an average annual burden per respondent of 1.25 hours (5 notices at 0.25 hours per notice) and an estimated total cost of \$146.05 (5 notices at \$29.21 per notice).

13. Estimates of Total Annualized Cost Burden

a. Form ATS - Initial Operation Report

The Commission estimates that there are approximately 65 alternative trading systems that have registered as broker-dealers and filed initial operation reports with the Commission. The Commission estimates that, over time, approximately 8 new alternative trading systems would file initial operation reports on Form ATS on an annual basis. Thus, the Commission estimates that the average aggregate annual burden for new alternative trading systems to file initial operation reports would be 200 hours (8 alternative trading systems at 25 hours per initial operation report on Form ATS). The Commission estimates the average annual aggregate burden would be \$17,957.36 (8 alternative trading systems at \$2,244.67 per initial operation report).

b. Form ATS - Periodic Amendments to Update Information

The Commission estimates that the average annual aggregate burden to file amendments to the initial operation report on Form ATS to report material systems changes and reflect other changes would be \$69,661.80 (65 alternative trading systems filing 2 amendments per year at \$535.86 per filing). The Commission estimates that the average annual aggregate burden of filing amendments to the initial operation report on Form ATS would be 650 hours (65 alternative trading systems filing 2 amendments per year at 5 hours per filing).

c. Form ATS-R - Quarterly Reports

The Commission estimates that the average annual aggregate burden to file quarterly reports on Form ATS-R would be \$96,392.40 (65 alternative trading systems filing 4 amendments per year at \$370.74 per filing). The Commission estimates that the average aggregate annual burden of filing quarterly reports on Form ATS-R would be 1040 hours (65 alternative trading systems filing 4 reports per year at 4 hours per filing).

d. Form ATS - Cessation of Operations Report

The Commission estimates that 3 alternative trading systems that register as broker-dealers and choose to comply with Regulation ATS would be required to file cessation of operations reports on Form ATS each year. The Commission estimates that the average annual aggregate burden to file cessation of operations reports on Form ATS would be \$556.11 (3 alternative trading systems at \$185.37 per filing). The Commission estimates that the average aggregate annual burden of filing cessation of operations reports on Form ATS would be 6 hours (3 alternative trading systems at 2 hours per filing).

e. Fair Access Standards Recordkeeping

The Commission estimates that 2 alternative trading systems that register as broker-

dealers and comply with Regulation ATS would meet the volume thresholds that trigger fair access obligations. These obligations would require such alternative trading systems to establish and keep records relating to standards for granting access to trading on its system. The Commission estimates that the annual aggregate burden for 2 alternative trading systems to establish and keep standards for granting access to trading on their systems would be \$1,168.30 (2 alternative trading systems at \$584.15 each). The Commission estimates that the average annual aggregate burden for 2 alternative trading systems to establish and keep standards for granting access to their systems would be 10 hours (2 alternative trading systems at 5 hours each).

f. Fair Access Notices

The Commission estimates that 2 alternative trading systems that register as broker-dealers and comply with Regulation ATS would meet the volume thresholds that trigger fair access obligations. These obligations would require such alternative trading systems to provide notice to investors who have been denied or limited access to the system of such decision and their right of appeal to the Commission. The Commission estimates that the annual aggregate burden for 2 alternative trading systems to provide investors notice of a denial or limitation decision and their right of appeal to the Commission would be \$1,093.50 (2 alternative trading systems providing 27 notices per year at \$20.25 per notice). The Commission estimates that the average annual aggregate burden for 2 alternative trading systems to provide notice of a denial or limitation decision and their right of appeal to the Commission would be 54 hours (2 alternative trading systems providing 27 notices per year at 1 hour per notice).

g. Systems Capacity, Integrity and Security Recordkeeping

Alternative trading systems that choose to register as broker-dealers, comply with Regulation ATS and meet certain volume thresholds are required to make records relating to any steps taken to comply with systems capacity, integrity and security requirements under Rule 301. The Commission estimates that the annual aggregate burden for 2 alternative trading systems to make records regarding systems capacity, integrity and security requirements would be \$2,336.58 (2 alternative trading systems at \$1,168.29 each). The Commission estimates that the average annual aggregate burden for 2 alternative trading systems to make records regarding systems capacity, integrity and security requirements would be 20 hours (2 alternative trading systems at 10 hours each).

h. Systems Outage Notices

The Commission estimates that 2 alternative trading systems that register as broker-dealers and comply with Regulation ATS would meet the volume thresholds that trigger systems' outage notice obligations. These obligations require such alternative trading systems to provide prompt notice to Commission staff of system outages. The Commission estimates that the annual aggregate burden for 2 alternative trading systems to provide prompt notice of systems' outages would be \$292.10 (2 alternative trading systems providing 5 notices per year at \$29.21 per notice). The Commission estimates that the

average annual aggregate burden for 2 alternative trading systems to provide prompt notice of a systems' outages would be 2.5 hours (2 alternative trading systems providing 5 notices per year at 0.25 hours per notice).

i. Aggregate Burdens

The estimated average annual aggregate burden for alternative trading systems to comply with Rule 301 would be 1,982.5 hours. This estimate is broken down as follows:

Initial operation report filing on Form ATS =	200 hours
Amendments to Form ATS =	650 hours
Quarterly reports on Form ATS-R =	1040 hours
Cessation of operations report on Form ATS =	6 hours
Fair access standards =	10 hours
Fair access notices =	54 hours
Systems capacity, integrity and security records =	20 hours
Systems outage notices =	<u>2.5 hours</u>
	1,982.5 hours

The estimated number of annual responses for alternative trading systems under Rule 301 would be 465. This estimate is broken down as follows:

Initial operation report filing on Form ATS =	8 filings
Amendments to Form ATS =	130 filings
Quarterly reports on Form ATS-R =	260 filings
Cessation of operations report on Form ATS =	3 filings
Fair access notices =	54 notices
Systems outage notices =	<u>10 notices</u>
	465 annual responses

The estimated average annual aggregate burden for alternative trading systems to comply with Rule 301 would be \$189,458.15. This estimate is broken down as follows:

Initial operation report filing on Form ATS =	\$ 17,957.36
Amendments to Form ATS =	\$ 69,661.80
Quarterly reports on Form ATS-R =	\$ 96,392.40
Cessation of operations report on Form ATS =	\$ 556.11
Fair access standards =	\$ 1,168.30
Fair access notices =	\$ 1,093.50
Systems capacity, integrity and security records =	\$ 2,336.58
Systems outage notices =	<u>\$ 292.10</u>
	\$189,485.15

14. Estimate of Cost to the Federal Government

The operational cost to the Commission for review of each initial operation report

filing on Form ATS and the related overhead value at 35 percent of the value of staff time is approximately \$695.25. These figures were derived in the following manner:

10 hours of legal work at \$50/hr =	\$ 500
1 hours of clerical work at \$15/hr =	\$ 15
printing, supplies =	<u>\$ 180.25</u>
	\$ 695.25

We have also estimated the annual operational cost to the Commission for review of amendments to the initial operation report, quarterly reports and cessation of operations reports and the related overhead value at 35 percent of the value of staff time is \$21,954.38. These figures were derived in the following manner:

8 initial operation reports at 11 hours of legal processing time =	88 hours
260 quarterly reports at 1.5 hour of legal processing time =	390 hours
130 amendments at 3 hour of legal processing time =	390 hours
3 cessation of operation reports at 1 hour of legal processing time =	3 hours
10 systems outage notices at .25 hours of legal processing time =	<u>2.5 hours</u>
	873.5 hours
873.5 hours legal processing time at \$50/hr =	\$ 43,675.00
overhead, including clerical work =	<u>\$ 15,286.25</u>
	\$ 58,961.25

The Commission estimates overhead costs (printing, supplies, copying and postage) to be approximately 35 percent of the value of labor costs. These estimates have been computed based on the GSA Guide to Estimating Reporting Costs (1973).

15. Explanation of Changes in Burden

The estimated burden has increased because the Commission has received a substantially greater number of initial operation reports than previously expected and because of the substantial increase in salaries of compliance personnel at broker-dealers. The estimated cost to the government has increased principally because the Commission staff has required more time than previously estimated to review initial operation reports and other documents required by Rule 301.

16. Information Collection Planned for Statistical Purposes

Not applicable. The information is not published for statistical use.

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

The Commission is not seeking approval to not display the expiration date for OMB approval.

18. Exceptions to Certification

The Commission is not seeking an exception to the certification statement.

B. Collection of Information Employing Statistical Methods

Not applicable because the collection of information will not employ statistical methods.