

Rule 17g-4: Prevention of misuse of material nonpublic information

SUPPORTING STATEMENT

A. **Justification**

1. **Need For Information Collection**

The Credit Rating Agency Reform Act of 2006¹ (“Rating Agency Act”), enacted on September 29, 2006, defines the term “nationally recognized statistical rating organization,” or “NRSRO,” provides authority for the Securities and Exchange Commission (“Commission”) to implement registration, recordkeeping, financial reporting, and oversight rules with respect to registered credit rating agencies, and directs the Commission to issue implementing rules no later than 270 days after its enactment.

The rules proposed under the Rating Agency Act contain recordkeeping and disclosure requirements. The collection of information obligations imposed by the proposed rules would be mandatory. The proposed rules, however, would apply only to credit rating agencies that are applying to register or are registered with the Commission as NRSROs, and registration is voluntary.

The Rating Agency Act added a new Section 15E, “Registration of Nationally Recognized Statistical Rating Organizations,”² to the Securities Exchange Act of 1934 (“Exchange Act”). Exchange Act Section 15E(g)(1)³ requires an NRSRO to establish, maintain, and enforce written policies and procedures to prevent the misuse of material nonpublic information in violation of the Exchange Act. Section 15E(g)(2) of the Exchange Act provides that the Commission must adopt rules requiring an NRSRO to establish specific policies and procedures to prevent the misuse of material non-public information.⁴ Proposed Rule 17g-4 would implement this statutory provision by requiring that an NRSRO’s written policies and procedures to prevent the misuse of material nonpublic information include three specific types of procedures: procedures designed to prevent the inappropriate dissemination of material nonpublic information obtained in connection with the performance of credit rating services; procedures designed to prevent a person associated with the rating organization from trading on material nonpublic information; and procedures designed to prevent the inappropriate dissemination of a pending credit rating.⁵

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

¹ Pub. L. No. 109-291.

² 15 U.S.C. 78o-7.

³ 15 U.S.C. 78o-7(g)(1).

⁴ 15 U.S.C. 78o-7(g)(2).

⁵ See proposed Rule 17g-4. Release No. 34-55231 (Feb. 2, 2007), 72 FR 6378 (Feb. 9, 2007).

The collection of information included in proposed Rule 17g-4 is necessary for Commission oversight of NRSROs registered with the Commission. Specifically, the procedures that would be required by proposed Rule 17g-4 are designed to ensure that an NRSRO establishes adequate procedures and controls to protect material nonpublic information and prevent its misuse.

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

Proposed Rule 17g-4 would require NRSROs to have written policies and procedures to prevent the misuse of material nonpublic information. This record could be made and retained electronically. The Commission believes that improvements in telecommunications and data processing technology may reduce any burdens associated with proposed Rule 17g-4. NRSROs are not prevented by proposed Rule 17g-4 from using computers or other mechanical devices to generate the records required under the proposed Rule.

4. Efforts To Identify Duplication

No duplication is apparent.

5. Effects on Small Entities

Small entities may be affected by the proposed rule because all NRSROs, regardless of size, would be required to have written policies and procedures to prevent the misuse of material nonpublic information.

6. Consequences of Less Frequent Collection

If this information were not collected as frequently, the Commission would be unable to ascertain, on an ongoing basis, whether a credit rating agency registered as an NRSRO had written policies and procedures to prevent the misuse of material non-public information.

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

The collection of information would not be 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. The comment period for the release that discusses proposed Rule 17g-4⁶ is 30

⁶ Release No. 34-55231 (Feb. 2, 2007), 72 FR 6378 (Feb. 9, 2007).

days. This comment period will afford the public an opportunity to respond to the proposal.

9. Payment or Gift to Respondents

Not applicable.

10. Assurance of Confidentiality

The information collection under proposed Rule 17g-4 will not be confidential.

11. Sensitive Questions

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

12. Estimate of Respondent Reporting Burden

The number of respondents that would be subject to the proposed rule would depend, in part, on the number of entities that would meet the statutory requirements for eligibility for registration. Further, registration is voluntary, and, consequently, the number of respondents would also depend on the number of entities that would choose to register with the Commission. The Commission estimates that approximately 30 credit rating agencies would register with the Commission as NRSROs under section 15E of the Exchange Act.

The Commission expects that most credit rating agencies already have procedures in place to address the specific misuses of material nonpublic information identified in proposed Rule 17g-4.⁷ Nonetheless, the Commission anticipates that some NRSROs may need to modify their procedures to comply with the specific procedures that would be required by the proposed rule. Based on staff experience, the Commission estimates that it would take approximately 50 hours for an NRSRO to establish procedures in conformance with the proposed rule for a total one-time burden for the 30 credit rating agencies the Commission estimates will register as NRSROs of 1,500 hours.⁸

13. Estimate of Total Annualized Cost Burden

The Commission believes that there would be no additional reporting costs associated with the proposed rule, other than the costs described in Item 12 above.

14. Estimate of Cost to Federal Government

There would be no additional costs to the Federal Government.

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For example, the IOSCO Code requires credit rating agencies to develop such procedures.

⁸

50 hours x 30 NRSROs = 1,500 hours.

15. Explanation of Changes in Burden

Not applicable. Proposed Rule 17g-4 would be a new rule.

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.