

SUPPORTING STATEMENT
Rule 206(3)-3T

A. JUSTIFICATION

1. Necessity of Information Collection

Section 206(3) of the Investment Advisers Act of 1940 requires an investment adviser to follow certain procedures if the adviser trades with its clients as principal (selling securities it owns to clients or buying securities from clients). Rule 206(3)-3T (17 CFR 275.206(3)-3T) provides an alternative means for investment advisers that are also registered broker-dealers to comply with section 206(3). Absent further Commission action the temporary rule will expire and no longer be effective on December 31, 2009.

The rule contains two types of collections of information: information provided by an adviser to its advisory clients and information collected from advisory clients by an adviser. The information collection requirements of the rule consist of the following:

- (i) prospective disclosure in writing of the conflicts arising from principal trades;
- (ii) obtaining written, revocable consent from the client prospectively authorizing the adviser to enter into principal trades;
- (iii) trade-by-trade oral or written disclosure of principal trading and oral or written client consent before each principal transaction;
- (iv) trade-by-trade written confirmation statements disclosing the capacity in which the adviser acted; and
- (v) delivering to the client an annual report itemizing the principal transactions.

Providing the information required by rule 206(3)-3T is necessary for dually-registered advisers to obtain the benefit of the alternative means of complying with section 206(3) of the Advisers Act.

2. Purpose of the Information Collection

Rule 206(3)-3T establishes an alternative means for certain advisers to meet the requirements of section 206(3) of the Advisers Act when they act in a principal capacity in transactions with certain advisory clients. The rule contains information collection requirements that provide important protections to investors when advisers engage in principal trades. Specifically, the rule requires advisers, among other things, to apprise their clients regarding the conflicts of interests arising from principal trades. The rule also requires advisers to provide information to clients regarding transactions that the adviser executed on a principal basis. We believe clients of advisers will primarily use the information collections for the purpose of monitoring principal trades.

3. Role of Improved Information Technology

Investment advisers are permitted to provide to clients the information required by rule 206(3)-3T electronically.¹

4. Efforts to Identify Duplication

There are no rules that duplicate or conflict with rule 206(3)-3T. There are rules that require broker-dealers to provide certain information in a confirmation statement to their customers regarding the transactions they effect. While rule 206(3)-3T requires information in a confirmation statement, the rule is designed to work efficiently together with those rules by permitting firms to incorporate the required disclosure into one confirmation statement.

¹ Use of Electronic Media by Broker-Dealers, Transfer Agents, and Investment Advisers for Delivery of Information; Additional Examples Under the Securities Act of 1933, Securities Exchange Act of 1932, and Investment Company Act of 1940, Investment Advisers Act Release No. 1562 (May 9, 1996).

5. Effect on Small Entities

Small entities registered with the Commission as investment advisers seeking to rely on the rule would be subject to the same disclosure requirements as larger entities. In developing the requirements of the rule, the Commission considered the extent to which they would have a significant impact on a substantial number of small entities, and included flexibility where possible, calling for disclosures that are already generated by the relevant firms in one form or another whenever possible in the light of the objectives of the rule, to reduce the corresponding burdens imposed. It would defeat the purpose of the rule to exempt small entities from the rule.

6. Consequences of Less Frequent Collection

Information must be given to a client at the following times: (i) before the adviser engages in principal trades with respect to the client's account, so the client can consent to prospective transactions; (ii) prior to the execution of each principal trade; (iii) after completion of each principal trade in the form of a confirmation statement; and (iv) annually, a report itemizing all principal transactions. Less frequent reporting would not give clients adequate information regarding principal trades executed by advisers.

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

The collection of information imposes no additional requirements regarding record retention.

8. Consultation Outside the Agency

The Commission and the staff of the Division of Investment Management participate in an ongoing dialogue with representatives of the investment adviser profession through public conferences, meetings, and informal exchanges. These various forums

provide the Commission and the staff with a means of ascertaining and acting upon paperwork burdens facing the industry. At the time the Commission issued temporary rule 206(3)-3T on an interim-final basis, it requested comment on the rule and the collection of information. No comments were submitted on the Commission's Paperwork Reduction Act of 1995 (44 U.S.C. 350 et seq.), ("PRA") estimate for the burden imposed by the collection.

The Commission requested public comment on the collection of information requirements in temporary rule 206(3)-3T before it submitted this request for extension and approval to the Office of Management and Budget. The Commission received no comments in response to its request.

9. Payment or Gift to Respondents

Not applicable.

10. Assurance of Confidentiality

The rule contains two types of collections of information: information provided by an adviser to its advisory clients and information collected from advisory clients by an adviser. Although the rule does not call for any of the information collected to be provided to us, to the extent advisers include any of the information required by the rule in a filing, such as Form ADV, the information will not be kept confidential. The collection of information delivered by clients to advisers would be subject to the confidentiality strictures that govern those relationships, and we would expect them to be confidential communications.

11. Sensitive Questions

Not applicable.

12. Estimate of Hour Burden

The Commission's estimates of the burden of each of the collections reflects the fact that the alternative means of compliance provided by the rule is substantially similar to the approach advisers currently employ to comply with the disclosure and consent obligations of section 206(3) of the Advisers Act and the approach that broker-dealers employ to comply with the confirmation requirements of rule 10b-10 under the Exchange Act. The Commission's estimate of the burden hours that will be imposed by the collections of information in rule 206(3)-3T are set forth below.

a. Prospective Disclosure Statement and Consent

i. Drafting prospective disclosure statement

1.	Respondents relying on the rule	
	380*	
2.	Responses per respondent	
	1	
3.	Burden hours per response	
	5	
4.	Initial hours requested	<hr/>
	1,900	

*As of August 1, 2007, there were 634 advisers that were eligible to rely on the temporary rule (i.e., also registered as broker-dealers), 395 of which indicate that they have non-discretionary accounts. For PRA purposes, we estimate that 90 percent of those advisers, or 356 entities, will rely on the rule. Of the 239 eligible advisers that do not currently provide non-discretionary services, we estimate that 10 percent, or 24 advisers, will create non-discretionary advisory programs and rely on the rule. Thus, the total number of advisers we anticipate will rely on the rule is 380.

ii. Distributing prospective disclosure statement

1.	Number of affected accounts	796,200*
2.	Responses per account	1
3.	Burden hours per response	0.1 (six minutes)
4.	Initial hours requested	<hr/>
		79,620

*Registration data indicate that there are approximately 796,200 accounts likely to receive prospective disclosure. This figure takes into account programs, such as mutual fund assets allocation programs, to which the rule will not apply and retirement accounts that are unlikely to participate in principal trading.

iii. <u>Reviewing prospective disclosure and responding to consent solicitation</u>		
1. Number of affected accountholders		796,200
2. Responses per accountholder		1
3. Burden hours per response		0.05 (3 minutes)
4. Initial hours requested		39,810
iv. <u>Updating disclosure, maintaining records, and processing revocations and prospective consents</u>		
1. Respondents relying on the rule		380
2. Responses per respondent		1
3. Burden hours per response		100
4. Annual hours requested		38,000
b. Trade-by-Trade Disclosure and Consent		
i. Number of affected accountholders		716,580*
ii. Responses per accountholder		50*
iii. Burden hours per response		0.0083 (30 seconds)
iv. Initial and annual hours requested		297,381
*We estimate that 90 percent of the 796,200 accountholders, or 716,580 accountholders, will execute and return the consent. We also estimate that non-discretionary advisory accountholders at eligible advisers engage in an average of approximately 50 trades per year.		
c. Principal Transactions Report		
i. <u>Programming computer systems</u>		
1. Respondents relying on the rule		380
2. Responses per respondent		1
3. Burden hours per response		5
4. Initial hours requested		1,900
ii. <u>Electronically-generated reports</u>		
1. Affected accounts		716,580
2. Responses per account		1

3. Burden hours per response	.05 (3 minutes)
4. Initial and annual hours requested	<u>35,829</u>
d. Total Burden Hours Requested	
	1,900
	79,620
	39,810
	38,000
	297,381
	1,900
	35,829
	<u>494,440</u>

The dollar cost estimates corresponding to each hour burden described above are as follows:

a. Prospective Disclosure Statement and Consent

i. Drafting prospective disclosure statement

1. Total hour burden	1,900
2. Hour burden per adviser	5
3. Cost per hour \$56*	
4. Cost per adviser \$280*	
5. Total cost	<u>\$106,400*</u>

*We expect that the internal preparation function will most likely be performed by compliance professionals. Data from the SIA's Report on Office Salaries in the Securities Industry 2006 ("Industry's Salary Report"), modified to account for an 1,800-hour work-year and multiplied by 2.93 to account for bonuses, firm size, employee benefits and overhead, suggest that the cost for a Compliance Clerk is approximately \$56 per hour. \$56 per hour x 5 hours on average per adviser = \$280 on average per adviser of internal costs for preparation of the prospective disclosure. \$280 on average per adviser of internal costs x 380 advisers = \$106,400 in total hour burden-related costs for preparation of the prospective disclosure.

ii. Distributing prospective disclosure statement

1. Total hour burden	79,620
2. Hour burden per adviser	210
3. Cost per hour \$41*	
4. Cost per adviser \$8,591*	

5. Total cost	<u>\$3,264,420*</u>
---------------	---------------------

* We expect that the distribution function for the prospective written disclosure and consent solicitation will most likely be performed by a general clerk. Data from the Industry’s Salary Report, modified to account for an 1,800-hour work-year and multiplied by 2.93 to account for bonuses, firm size, employee benefits and overhead, suggest that cost for a General Clerk is approximately \$41 per hour. \$41 per hour 79,620 total hours = \$3,264,420 (which, if divided by the estimated 380 eligible advisers, equals a total cost for distribution of approximately \$8,591 on average per eligible adviser).

iii. Reviewing prospective disclosure and responding to consent solicitation

1. Total hour burden (on accountholders)	39,810
2. Total number of accountholders	796,200
3. Hour burden per accountholder	0.05 (3 minutes)*
4. Cost per accountholder	\$0.50*
5. Cost per hour	\$10*
6. Total cost	<u>\$398,100*</u>

*We expect that the reviewing prospective disclosure and responding to the consent solicitation will be undertaken by accountholders, of which we estimate there are approximately 796,200. We do not believe there will be a significant difference in burden between those clients that consent and those that do not. As such, the burden per accountholder is 39,810 hours ÷ 796,200 accounts = 0.05 hours (3 minutes). We estimate the cost per accountholder to review the disclosure and respond to the consent solicitation will be \$0.50. As such, the total cost for all accountholders will be 796,200 accountholders x \$0.50 per account = \$398,100 (which, if divided by the total number of burden hours, equals a cost per hour of \$10).

iv. Updating disclosure, maintaining records, and processing revocations and prospective consents

1. Total hour burden	38,000
2. Hour burden per adviser	100
3. Cost per hour	\$56*
4. Cost per adviser	\$5,600*
5. Total cost	<u>\$2,128,000*</u>

*We expect that this function will most likely be performed by compliance professionals at \$56 per hour. See Industry’s Salary Report. 100 hours on average per adviser per year x \$56 per hour = \$5,600 on average per adviser per year. \$5,600 on average per adviser per year x 380 eligible advisers = \$2,128,000.

b. Trade-by-Trade Disclosure and Consent

i.	Total hour burden	297,381
ii.	Hour burden per adviser	783*
iii.	Cost per hour	\$56*
iv.	Cost per adviser	\$43,848*
v.	Total cost	<u>\$16,662,240*</u>

*The burden for the average adviser would be 297,381 total hours per year ÷ 380 eligible advisers = approximately 783 hours on average per adviser per year. We expect that this function will most likely be performed by compliance professionals at \$56 per hour (see Industry's Salary Report) and that the preparation. 783 hours on average per adviser per year x \$56 per hour = \$43,848 on average per adviser per year. \$43,848 on average per eligible adviser per year x 380 eligible advisers = \$16,662,240 total cost per year.

c. Principal Transactions Report

vi.	<u>Programming computer systems</u>	
1.	Total hour burden	1,900
2.	Hour burden per adviser	5
3.	Cost per hour	\$67*
4.	Cost per adviser	\$335*
5.	Total cost	<u>\$127,300*</u>

*We expect that the internal programming function most likely will be performed by computer programmers. Data from the Industry's Salary Report, modified to account for an 1,800-hour work-year and multiplied by 2.93 to account for bonuses, firm size, employee benefits and overhead, suggest that cost for a Sr. Computer Operator is approximately \$67 per hour. Five hours on average per adviser x \$67 per hour = \$335 on average per adviser (or, across all 380 eligible advisers, \$127,300).

vii.	<u>Electronically-generated reports</u>	
1.	Total hour burden	35,829
2.	Hour burden per adviser	94
3.	Cost per hour	\$41*
4.	Cost per adviser	\$3,866*
5.	Total cost	<u>\$1,468,989*</u>

*We expect that the generation and delivery of annual principal trade reports will most likely be performed by general clerks at \$41 per hour. \$41 per

hour x 35,829 total hours per year = \$1,468,989 (or, if divided among all 380 eligible advisers, approximately \$3,866 on average per adviser per year).

d. Total Costs Associated with Burden Hours Requested

Burden hours	Associated Cost
1,900	\$106,400
79,620	\$3,264,420
39,810	\$398,100
38,000	\$2,128,000
297,381	\$16,662,240
1,900	\$127,300
35,829	\$1,468,989
<u>494,440</u>	<u>\$24,155,449</u>

13. Estimate of Total Cost Burden

The Commission estimates that there are four additional cost burdens for the rule, excluding any cost of the burden hours as identified in Item 12 above.

a. Professional fees for preparation of disclosure statement

i. Advisers relying on the rule	380
ii. Cost burden per adviser	\$1,200
iii. Initial cost burden	<u>\$456,000</u>

b. Printing and distributing prospective disclosure statement

i. Accounts	796,200
ii. Cost burden per account	\$1.50
iii. Initial cost burden	<u>\$1,194,300</u>

c. Reprogramming computer systems to generate trade-by-trade confirmations

i. Advisers relying on the rule	380
ii. Cost burden per adviser	\$20,000
iii. Initial cost burden	<u>\$7,600,000</u>

d. Programming computer systems to generate annual principal transactions report

i. Advisers relying on the rule	380
ii. Cost burden per adviser	\$10,000
iii. Initial cost burden	<u>\$3,800,000</u>

e. Total Additional Cost Burden Estimate

\$456,000
\$1,194,300
\$7,600,000
\$3,800,000
<u>\$13,050,300</u>

14. Estimate of Cost to the Federal Government

There are no costs to the federal government directly attributable to Rule 206(3)-3T.

15. Explanation of Changes in Burden

Not applicable.

16. Information Collection Planned for Statistical Purposes

Not applicable.

17. Approval to not Display Expiration Date

Not applicable.

18. Exceptions to Certification Statement

Not applicable.

B. COLLECTIONS OF INFORMATION EMPLOYING STATISTICAL METHODS

Not applicable.