# SUPPORTING STATEMENT FOR RULE 701

This submission, pursuant to the Paperwork Reduction Act of 1995, 44 U.S.C. Section 3501 et seq., consists of this supporting statement and the following supporting exhibits:

A. - Rule 701
B. - Statutory Authority

## A. Justification

### 1. Necessity of Information Collection

Absent an available exemption, the Securities Act of 1933 (the "Securities Act") requires that a registration statement be filed with the Commission disclosing prescribed categories of information before the securities may be offered for sale to the public. The securities may not be sold to the public until the registration statement becomes effective. In addition, prospective investors must be furnished a prospectus containing the most significant information from the registration statement. However, Congress recognized that in some situations there may be no need for registration and thus provided a number of exemptions from registration. Section 28 of the Securities Act permits the Commission to "conditionally or unconditionally exempt any person, security or transaction, … from any provision … to the extent that such exemption is necessary or appropriate in the public interest, and is consistent with protection of investors."

Rule 701 permits a company that is not subject to the reporting provisions of the Securities Exchange Act of 1934 to offer and sell its securities through an employee benefit plan or contract relating to compensation without registration under the Securities Act. The total sales price or maximum amount of securities that may be sold in a year under the rule is the greatest of: $1 million; 15% of the total assets of the issuer or its parent company if the issuer is a wholly-owned subsidiary; or 15% of the outstanding amount of the class of securities being offered and sold in reliance on this section. The issuer must provide specific disclosure to each purchaser of securities if more than $5 million worth of securities are sold during any consecutive 12-month period. The required disclosure consists of: a copy of the compensatory benefit plan or contract (which must be given to all offerees under the rule); a copy of the summary plan description required by the Employee Retirement Income Security Act of 1974 ("ERISA") or, if the plan is not subject to ERISA, a summary of the plan's agreement; and the financial statements required in an offering statement on Form 1-A under Regulation A which generally dictates unaudited financial statements.

Because substantial amounts of securities can be issued under the exemption without registration, the public interest and the protection of investors demand that some disclosure requirement be imposed where amounts in excess of the "small issuer" exemption of $5 million are involved. Because these are compensatory rather that capital-raising transactions, the minimum level of disclosure to inform these employee-type investors is set forth in the rule.

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

The purpose of the Rule 701 collection is to ensure that a basic level of information is available to employees and others when substantial amounts of securities are issued in compensatory arrangements. For small issues under $5 million, no additional disclosure beyond the terms of the compensatory arrangement or plan is required to be provided. If companies issuing more than $5 million worth of their securities in a 12 months period do not provide basic risk and financial disclosure to their investors, even when these persons have a business or employment relationship with them, there is a danger that investment decisions will be made without sufficient information.

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

The required information is provided to the employee-investor and is not provided to the Commission. The information may be electronically transmitted to employee investors.

4. Effort to Identify Duplication

The information required by Rule 701 is not duplicative of other required disclosure.

5. Effect on Small Entities

Only small businesses that are able to sell more than $5 million worth of their securities pursuant to the calculation formulas and choose to do so are required to provide the specified disclosure to their employee-investors. Since most small entities will be offering less than $5 million, the rule by its terms minimizes the effect on these entities by not specifying the type of disclosure they need to provide.

6. Consequences of Less Frequent Collection

The legislative intent for collection of this information requires that the information be available prior to the making of the investment decision. It cannot be satisfied by fewer collections.

7. Inconsistencies with Guidelines in 5 CFR 1320.6

Not applicable.

8. Consultations Outside the Agency

Rule 701 was proposed for public comment. No comments were received on this request during the 60-day comment period prior to OMB’s approval of this submission.

9. Payment or Gift to Respondents

Not applicable.

10. Assurances of Confidentiality

The Rule 701 information is not filed with the agency but could be subject to confidentiality or other arrangements between and among relevant parties.

11. Sensitive Questions

Not applicable.

12. Estimate of Respondent Reporting Burden

Approximately 300 companies annually rely on the Rule 701 exemption and it takes 2 hours per response. We estimate that 25% of the 2 hours per response (.5 hours) is prepared by the company for total annual reporting burden of 150 hours (.5 hours per response x 300 responses). The estimated burden hours are solely for the purpose of the Paperwork Reduction Act.

13. Estimate of Total Annualized Cost Burden

We estimate that 75% of the 2 hours per response (1.5 hours) is prepared by an outside law firm hired by the firm. We estimate that it costs $400 per hour ($400 x 1.5 hours per response x 300) for a total cost burden of $180,000. The estimated cost burden is made solely for purposes of the Paperwork Reduction Act. The cost is not derived from a comprehensive or even a representative survey or study of the costs of Commission rules and forms.

14. Estimated Cost to the Federal Government

No special filing is required to be made with the government under the rule, so no cost is attributed to the review and processing of the information.

15. Explanation of Changes in Burden

The change in cost burden is due to an adjustment. The increase of $45,000 in cost burden reflects a change in the hourly cost to $400 per hour from $300 per hour.

16. Information Collections Planned for Statistical Purposes

Not applicable.

17. Explanation as to Why Expiration Will Not Be Displayed

Not applicable.

18. Exception to Certification

Not applicable.

B. Collection of Information Employing Statistical Methods

Not applicable.