

## **Rule 103 of Regulation M Supporting Statement**

### **A. Justification**

#### **1. Necessity of Information Collection**

##### **a. Background**

Congress granted broad rulemaking authority to the Commission in Sections 9(a)(2), 10(b), and 15(c) under the Securities Exchange Act of 1934 (“Exchange Act”) to combat manipulative abuses in whatever form they may take. In exercising its authority, the Commission has focused on the market activities of persons participating in a securities offering and determined that securities offerings present special opportunities for manipulation that require specific regulatory attention. On December 20, 1996, the Commission adopted Regulation M, consisting of new Rules 100 through 105, which govern the activities of underwriters, issuers, selling security holders, and others in connection with a securities offering. Regulation M significantly eased regulatory burdens on offering participants by eliminating the trading restrictions for underwriters of actively traded securities; reducing the scope of coverage for other securities; reducing restrictions on issuer plans; providing a more flexible framework for stabilizing transactions; and deregulating rights offerings.

##### **b. Overview of Rule**

Rule 103 governs Nasdaq passive market making by distribution participants.

##### **c. Information Collection Requirements**

Rule 103 requires notification and disclosure of passive market making activity in Nasdaq securities. Regulation M incorporated many previously-existing requirements of the trading practices rules, together with their information collection requirements. However, by removing many categories of activities, securities, and persons from anti-manipulation regulation, Regulation M reduced the burdens of anti-manipulation regulation.

Rule 103 permits "passive market making" during a distribution of Nasdaq securities. This passive market making cannot exceed the purchase limitation of 30% average daily trading volume (“ADTV”) limitation or 200 shares, whichever is greater. Rule 103 requires passive market makers to notify the self-regulatory organization (“SRO”) formerly known as the NASD (now succeeded by FINRA) in advance if they intend to conduct such activity and submit information prescribed by that organization. Rule 103 also

requires the disclosure pursuant to Items 502 and 508 under Regulations S-K and S-B with respect to the intended passive market making activities.

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

The written notice submitted to the SRO pursuant to Rule 103 provides the SRO with the opportunity to calculate the ADTV of the security in distribution for which the potential passive market maker has been responsible. Rule 103 requires that the NASD make this calculation. The prospectus disclosure required by Rule 103 informs potential investors that passive market making may be conducted by the underwriters in the offering. Investors use this information in evaluating the offering price of the securities in distribution.

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

Improvements in telecommunication and data processing technology reduce regulatory burdens that might otherwise result from Rule 103. The Commission is not aware of any technical or legal obstacles to reducing the burden through the use of improved information technology.

## **4. Efforts to Identify Duplication**

The information required by Rule 103 does not duplicate that required by any other federal regulation. At the time Regulation M and related amendments were proposed, the Commission solicited and received comments without receiving any reference to federal regulations that may duplicate the requirements mandated by Regulation M. The Commission continues to believe that there is no duplication of the information required by the rules described herein.

## **5. Effects on Small Entities**

The information requirements of Rule 103 apply equally to all entities engaging in Nasdaq passive market making, regardless of the size of the entity. To the extent that Rule 103 affects small entities, the Commission believes that the burdens are minimal compared to the expanded business opportunities through passive market making now available for all Nasdaq securities.

## **6. Consequences of Less Frequent Collection**

Not applicable.

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

The collection of information requested in the rules described herein is conducted in a manner consistent with the guidelines in 5 C.F.R.1320.5(d)(2).

**8. Consultations Outside the Agency**

The amendments adopted by the Commission in 1996 were subject to public review and comment following the issuance of a Concept Release in 1994 and a Proposing Release in 1996.

**9. Payment or Gift to Respondents**

Not applicable.

**10. Assurance of Confidentiality**

No assurance of confidentiality is provided.

**11. Sensitive Questions**

No questions of a sensitive nature are asked.

**12. Estimates of Respondent Reporting Burden**

In every firm commitment offering of a Nasdaq security, the underwriters may seek to engage in passive market making. The managing underwriter would inform the NASD, receive the data, and inform the syndicate members of their passive market making status. The Commission estimates that the written notice required to be provided to the NASD requires one hour of preparation. There were a total of 214 secondary offerings of Nasdaq securities in 2006. Assuming 214 is the number of offerings in a typical year and assuming that passive market making is available under Rule 103 for all of these offerings, the Commission estimates that the total burden of Rule 103 is 214 hours.

**13. Estimates of Total Annualized Cost Burden**

The Commission estimates that a typical employee of a broker-dealer charged to ensure compliance with Commission regulations receives annual compensation of \$117,000. This compensation is the equivalent of \$56.25 per hour (\$117,000 divided by 2,080 payroll hours per year). Based on that estimate, the

Commission estimates that the annual salary cost to comply with Rule 103 is \$12,037.50 (\$56.25 per hour times 214 hours).

**14. Estimated Cost to the Federal Government**

The government does not experience significant costs based on the recordkeeping required pursuant to Rule 103. The information collected by the respondents is normally reviewed only pursuant to an investigation, not as a matter of routine.

**15. Explanation of Changes in Burden**

The increase in burden hours overall is due to an increase in the estimate of Nasdaq secondary offerings used in prior years. The increase in total annualized cost burden is due to inflation adjustments to the annual compensation for the typical employee charged with compliance with Commission regulations. There are no other changes in the burden.

**16. Information Collection Planned for Statistical Purposes**

Not applicable. There are no plans to require the publication of these records in the future.

**17. Explanation of Why Expiration Date Will Not Be Displayed**

Not applicable.

**18. Exceptions to the Certification**

Not applicable.

**B. Collecting Information Employing Statistical Methods**

Not applicable.