

SUPPORTING STATEMENT
RULE 17e-1

A. JUSTIFICATION

1. Necessity for the Information Collection

Section 17(e)(2)(A) of the Investment Company Act of 1940 (the “Act”)¹ limits the remuneration a broker affiliated with a registered investment company (“fund”) may receive in connection with the sale of securities to or by the fund, to no more than “the usual and customary broker’s commission if the sale is effected on a securities exchange.”² Rule 17e-1 under the Act requires a fund’s board of directors to establish, and review as necessary, procedures reasonably designed to provide that the remuneration to the affiliated broker is a fair amount compared to that received by other brokers in connection with transactions in similar securities during a comparable period of time.³ Each quarter, the board must determine that all transactions effected under the rule during the preceding quarter complied with the established procedures (“review requirement”). Rule 17e-1(c) also requires the fund to (i) maintain permanently a written copy of the procedures adopted by the board for complying with the requirements of the rule; and (ii) maintain for a period of six years a written record of each transaction subject to the rule setting forth the amount and source of the commission, fee or other remuneration received; the identity of the broker; the terms of the transaction; and the materials used to determine that the transactions were effected in compliance with the procedures adopted by the board (“recordkeeping requirement”).

Rule 17e-1 conditionally exempts funds from having to comply with the recordkeeping

¹ 15 U.S.C. 80a.

² 15. U.S.C. 80a-17(e)(2)(A).

³ 17 CFR 270.17e-1.

requirement when an affiliated subadviser that serves as a broker is not in a position to influence the fund's decision to participate in the transaction. To qualify for this exemption, rule 17e-1 requires that the advisory contracts of both the subadviser that enters into the transaction, and the subadviser that recommends that the fund engage in the transaction prohibit the subadvisers from consulting with one another concerning securities transactions of the fund. The rule's conditions are designed to limit the exemptions to those transactions in which the transacting subadviser has neither the ability nor the incentive to influence the investment decision of the participating fund.

2. Purpose of the Information Collection

The recordkeeping requirements under rule 17e-1 enable the Commission to ensure that affiliated brokers receive compensation that does not exceed the usual and customary broker's commission. Without the recordkeeping requirements, Commission inspectors would have difficulty ascertaining whether funds were complying with rule 17e-1. Commission rules also require funds to amend their subadvisory contracts before they can rely on rule 17e-1's exemption to ensure that the subadviser that engages in the transaction does not influence the fund's decision to participate in the transaction.

3. Role of Improved Information Technology

To the extent the rule includes recordkeeping requirements, the Electronic Signatures in Global and National Commerce Act⁴ and the conforming amendments to recordkeeping rules under the Investment Company Act permit funds to maintain records electronically.

4. Efforts to Identify Duplication

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P.L. 106-229, 114 Stat. 464 (June 30, 2000).

Section 31(a) of the Act and rules 31a-1 and 31a-2 thereunder, require investment companies to maintain and preserve records similar to those required to be kept under rule 17e-1. Rule 17e-1 does not require that duplicate records be kept, but reiterates the requirement to maintain and preserve such records.

5. Effect on Small Entities

The recordkeeping requirements of rule 17e-1 are the same for all funds subject to the rule, including small entities.

6. Consequence of Less Frequent Collection

Rule 17e-1(c) requires the investment company to (i) maintain permanently a written copy of the procedures adopted by the board for complying with the requirements of the rule; and (ii) maintain for a period of six years a written record of each transaction subject to the rule setting forth the amount and source of the commission, fee or other remuneration received; the identity of the broker; the terms of the transaction; and the materials used to determine that the transactions were effected in compliance with the procedures adopted by the board. Less frequent recordkeeping requirements would impair the Commission's ability to ascertain compliance with the rule. Rule 17e-1 also requires that a fund's subadvisory contract either be initially drafted or amended to qualify for the rule's exemption. This is not a recurring requirement; less frequent collection is not possible.

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

Rule 17e-1 requires funds to preserve certain records for six years and other records permanently. We believe that the long-term retention of records is necessary to carry out our examination and enforcement responsibilities, and our mandate to ensure that the Act's

provisions are legally enforceable. We periodically inspect the operations of funds to ensure compliance with the rules and regulations under the Act; however, each fund may be inspected only at intervals of several years due to limits on our resources. Furthermore, Congress has placed no time limit on the prosecution of persons engaged in certain types of conduct that violate the securities laws. For these reasons, we often need information relating to events or transactions that occurred years ago. Computerized record storage has made long-term retention of records less burdensome.

8. Consultation Outside the Agency

The Commission requested public comment on the collection of information requirements in rule 17e-1 before it submitted this request for approval to the Office of Management and Budget. The Commission received no comments in response to this request.

More generally, the Commission and the staff at the Division of Investment Management participate in an ongoing dialogue with representatives of the investment company industry 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 confronting the industry.

9. Payment or Gift to Respondents

Not applicable.

10. Assurance of Confidentiality

Not applicable.

11. Sensitive Questions

Not applicable.

12. Estimate of Hour Burden

Based on an analysis of fund filings, the staff estimates that approximately 252 fund portfolios enter into subadvisory agreements each year.⁵ Based on discussions with industry representatives, the staff estimates that it will require approximately 3 attorney hours to draft and execute additional clauses in new subadvisory contracts in order for funds and subadvisers to be able to rely on the exemptions in rule 17e-1. Because these additional clauses are identical to the clauses that a fund would need to insert in their subadvisory contracts to rely on rules 12d3-1, 10f-3, 17a-10, and because we believe that funds that use one such rule generally use all of these rules, we apportion this 3 hour time burden equally to all four rules. Therefore, we estimate that the burden allocated to rule 17e-1 for this contract change would be 0.75 hours.⁶ Assuming that all 252 funds that enter into new subadvisory contracts each year make the modification to their contract required by the rule, we estimate that the rule's contract modification requirement will result in 189 burden hours annually, with an associated cost of approximately \$59,724.⁷

Based on an analysis of fund filings, the staff estimates that approximately 1935 funds use at least one affiliated broker. Based on conversations with fund representatives, the staff estimates that rule 17e-1's exemption would free approximately 40 percent of transactions that occur under rule 17e-1 from the rule's recordkeeping and review requirements. This would

⁵ Based on information in Commission filings, we estimate that 42.5 percent of funds are advised by subadvisers.

⁶ This estimate is based on the following calculation (3 hours ÷ 4 rules = .75 hours).

⁷ These estimates are based on the following calculations: (0.75 hours × 252 portfolios = 189 burden hours); (\$316 per hour × 189 hours = \$59,724 total cost). The Commission staff's estimates concerning the wage rates for attorney time are based on salary information for the securities industry compiled by the Securities Industry Association. The \$316 per hour figure for an attorney is from the SIFMA Report on Management & Professional Earnings in the Securities Industry 2009, modified to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

leave approximately 1161 funds (1935 funds x .6 = 1161) still subject to the rule's recordkeeping and review requirements. The staff estimates that each of these funds spends approximately 59 hours per year (40 hours by accounting staff, 15 hours by an attorney, and 4 director hours) at a cost of approximately \$25,500 per year to comply with rule 17e-1's requirements that (i) the fund retain records of transactions entered into pursuant to the rule, and (ii) the fund's directors review those transactions quarterly.⁸ We estimate, therefore, that the total yearly hourly burden for all funds relying on this exemption is 68,499 hours,⁹ with yearly costs of approximately \$29,605,500.¹⁰ Therefore, the estimated annual aggregate burden hour associated with rule 17e-1 is 68,688,¹¹ and the estimated annual aggregate cost associated with it is \$29,665,224.¹²

13. Estimate of Total Annual Cost Burden

⁸ This estimate is based on the following calculations: (40 hours accounting staff x \$119 per hour = \$4760) (15 hours by an attorney x \$316 per hour = \$4740); (4 hours by directors x \$4000 = \$16,000) (\$4760 + \$4740 + \$16,000 = \$25,500 total cost). The Commission staff's estimates concerning the wage rate for professional time are based on salary information for the securities industry compiled by the Securities Industry Association, except for the estimate of \$4000 per hour for a board of directors. The \$316 per hour estimate for an attorney and the \$119 per hour estimate for accountant time is from the SIFMA Report on Management & Professional Earnings in the Securities Industry 2009, modified to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

⁹ This estimate is based on the following calculation: (1161 funds x 59 hours = 68,499).

¹⁰ This estimate is based on the following calculation: (\$25,500 x 1161 funds = \$29,605,500).

¹¹ This estimate is based on the following calculation: (189 hours + 68,499 hours = 68,688 total hours).

¹² This estimate is based on the following calculation: (\$59,724 + \$29,605,500 = \$29,665,224).

There is no cost burden of rule 17e-1 excluding any cost of the respondent recordkeeping burden identified in Item 12 of this Supporting Statement. Compliance with the rule is part of customary and usual investment company business practice to ensure compliance with applicable laws and regulations.

14. Estimate of Cost to the Federal Government

There are no costs to the Federal Government associated with rule 17e-1.

15. Explanation of Changes in Burden

The estimated hourly burden associated with Rule 17e-1 has increased from 11,250 hours to 68,688 hours (an increase of 57,438 hours). The increase is due to an increase in our estimate of the number of funds using at least one affiliated broker, which is based on responses from industry representatives.

16. Information Collection Planned for Statistical Purposes

Not applicable.

17. Approval to not be Display Expiration Date

Not applicable.

18. Exceptions to Certification Statement

Not applicable.

B. COLLECTIONS OF INFORMATION EMPLOYING STATISTICAL METHODS

Not applicable.