

SUPPORTING STATEMENT

Exemption for Certain Multi-State Investment Advisers (Rule 203A-2(d))

A. JUSTIFICATION

1. Necessity of Information Collections

Pursuant to section 203A of the Investment Advisers Act of 1940 (“Advisers Act” or “Act”), an investment adviser that is regulated or required to be regulated as an investment adviser in the state in which it maintains its principal office and place of business is prohibited from registering with the Securities and Exchange Commission (“Commission” or “SEC”) unless that adviser has at least \$25 million in assets under management or advises a Commission-registered investment company. Advisers failing to meet either requirement are prohibited from registering with the Commission.¹ The Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”)² amends section 203A to prohibit from Commission registration an adviser that: (i) has assets under management between \$25 million and \$100 million; (ii) is required to be registered as an investment adviser with the state in which it maintains its principal office and place of business; and (iii) if registered, would be subject to examination as an adviser by that state.³ A mid-sized adviser that otherwise would be prohibited may register with the Commission if it would be required to register with 15 or more states.⁴ Section 203A(c) of the Advisers Act authorizes the Commission to exempt an adviser from the prohibition on Commission registration if the prohibition would be “unfair, a

¹ 15 U.S.C. 80b-3a.

² Pub. L. No. 111-203, 124 Stat. 1376 (2010).

³ See section 410 of the Dodd-Frank Act.

⁴ See section 410 of the Dodd-Frank Act. A mid-sized adviser also will be required to register with the Commission if it is an adviser to a registered investment company or business development company under the Investment Company Act. *Id.*

burden on interstate commerce, or otherwise inconsistent with the purposes” of section 203A of the Act.⁵ Under this authority, the Commission adopted rule 203A-2 to provide certain types of advisers with exemptions from the prohibition on registration.

Rule 203A-2(e) currently provides that the prohibition on registration with the Commission does not apply to an investment adviser that is required to register in 30 or more states. Once registered with the Commission, the adviser remains eligible for Commission registration as long as it would be obligated, absent the exemption, to register in at least 25 states.⁶ An investment adviser relying on this exemption also must: (i) include a representation on Schedule D of Form ADV that the investment adviser has concluded that it must register as an investment adviser with the required number of states; (ii) undertake to withdraw from registration with the Commission if the adviser indicates on an annual updating amendment to Form ADV that it would be required by the laws of fewer than 25 states to register as an investment adviser with the state; and (iii) maintain in an easily accessible place a record of the states in which the investment adviser has determined it would, but for the exemption, be required to register for a period of not less than five years from the filing of a Form ADV relying on the rule.⁷ The Commission proposed to align the rule with the Dodd-Frank Act’s multi-state exemption for mid-sized advisers by permitting all investment advisers required to register as advisers with 15 or more states to register with the Commission, and proposed to

⁵ 15 U.S.C. 80b-3a(c).

⁶ 17 CFR 275.203A-2(e)(1).

⁷ 17 CFR 275.203A-2(e)(2)-(4). The five-year record retention period is a similar recordkeeping retention period as imposed on all SEC-registered advisers under rule 204-2 of the Adviser Act. See rule 204-2 (17 CFR 275.204-2).

renumber the rule as rule 203A-2(d).⁸ The Commission also proposed to eliminate the cushion for advisers that must register with 25 to 30 states, and did not propose a similar cushion for the 15-state threshold.⁹ An investment adviser relying on this exemption would be required to maintain in an easily accessible place a record of the states in which the investment adviser has determined it would, but for the exemption, be required to register for a period of not less than five years from the filing of a Form ADV relying on the rule.¹⁰ The rule’s record maintenance requirement is a “collection of information” for Paperwork Reduction Act (“PRA”) purposes.¹¹

Respondents to this collection of information would be investment advisers required to register in 15 or more states absent the exemption that rely on rule 203A-2(d) to register with the Commission. The records kept by investment advisers in compliance with the rule would be necessary for the Commission staff to use in its examination and oversight program.

The title of the new collection of information is: “Exemption for Certain Multi-State Investment Advisers (Rule 203A-2(d)).” We have submitted this collection of

⁸ Proposed rule 203A-2(d). The proposing release is attached as Appendix A (“Proposing Release”). We also note that proposed rule 203A-2(d) would permit an adviser to choose to maintain its state registrations and not switch to SEC registration. See proposed rule 203A-2(d)(2) (adviser elects to rely on the exemption by making the required representations on Form ADV).

⁹ Proposed rule 203A-2(d).

¹⁰ See proposed rule 203A-2(d)(3). An investment adviser relying on this exemption also would continue to be required to: (i) include a representation on Schedule D of Form ADV that the investment adviser has reviewed applicable law and concluded that it must register as an investment adviser with 15 or more states; and (ii) undertake on Schedule D to withdraw from registration with the Commission if the adviser indicates on an annual updating amendment to Form ADV that the investment adviser would be required by the laws of fewer than 15 states to register as an investment adviser with the state. See proposed rule 203A-2(d)(2).

¹¹ The PRA burden for Form ADV reflects the required representations on Schedule D of Form ADV. See Appendix A.

information to OMB for review, and OMB has not yet assigned this collection a control numbers. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid OMB control number. If the proposal is adopted, this collection of information would be found at 17 CFR 275.203a-2(d) (currently 17 CFR 275.203a-2(e)) and would be mandatory to qualify for and maintain Commission registration eligibility under rule 203A-2(d) (currently rule 203A-2(e)). Responses provided to the Commission in the context of its examination and oversight program are generally kept confidential under section 210(b) of the Advisers Act.¹²

2. Purposes of Information Collection

The information collected under rule 203A-2(d) would permit the Commission's examination staff to determine an advisers' eligibility for registration with the Commission under this exemptive rule.

3. Role of Improved Information Technology

An investment adviser registering or registered with the Commission under rule 203A-2(d) would be required to maintain in an easily accessible place a record of the states in which the investment adviser has determined it would, but for the exemption, be required to register for five years from the filing of a Form ADV.¹³ Advisers would be permitted to meet the recordkeeping obligation under the rule micrographically or electronically, and their storage of this required record in such media would be governed by Advisers Act rule 204-2(g).¹⁴

¹² 15 U.S.C. 80b-10(b).

¹³ Proposed rule 203A-2(d)(3).

¹⁴ 17 CFR 275.204-2(g). Rule 204-2 requires that the record be arranged and indexed in a way that permits easy location, access, and retrieval of any particular record, 17 CFR

4. Efforts to Identify Duplication

The recordkeeping requirement of rule 203A-2(d) is not duplicated elsewhere for investment advisers that must comply with this collection requirement.

5. Effect on Small Entities

The collection of information requirements are the same for all investment advisers registering or registered with the Commission, including those that are small entities. Under section 203A, as amended by the Dodd-Frank Act, advisers with assets under management of less than \$100 million generally are not eligible to register with the Commission; however, under rule 203A-2(d), these entities, which include small entities, would be permitted to register with the Commission if they meet the conditions of the rule. The recordkeeping requirement under the rule affects small advisers and larger advisers similarly, because the required information is about the adviser maintaining the records and about its regulatory requirements and business, which should be readily available to any adviser regardless of size. It would defeat the purpose of the rule to exempt small entities from these requirements. Moreover, although the records are mandatory, the rule is a permissive exemption. A small adviser can choose not to rely on the rule and thus not be subject to the collection of information.

6. Consequences of Less Frequent Collection

An adviser registering with the Commission under rule 203A-2(d) would be required to maintain a record of the states in which the investment adviser has determined it would, but for the exemption, be required to register for a period of not less than five

275.204-2(g)(2)(ii), and that the micrographic or electronic duplicate of the record be separately stored for five years, 17 CFR 275.204-2(g)(2)(iii). An investment adviser must establish and maintain procedures to keep the required records so as to reasonably safeguard the records from loss, alteration, or destruction; and to limit access to the records to properly authorized personnel and the Commission. See 17 CFR 275.204-2(g)(3).

years from the filing of a Form ADV.¹⁵ Because the period between examinations may be as long as five years, it is important that the Commission have access to records that cover the period between examinations. If the required information is not collected, the Commission's examiners would not be able to verify that an investment adviser's reliance on rule 203A-2(d) in registering with the Commission was appropriate.

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

Rule 203A-2(d) would include a recordkeeping provision under which an adviser relying on the rule to register with the Commission would be required to maintain certain information, specified more fully in Item 1 above, for five years. Although this period exceeds the three-year guideline for most kinds of records under 5 CFR 1320.5(d)(2)(iv), the long-term retention of these records is designed to contribute to the effectiveness of the Commission's examination and inspection program, and is necessary for the Commission's inspection program to determine compliance with the Advisers Act, including an adviser's continued eligibility to register with the Commission. Because the period between examinations may be as long as five years, it is important that the Commission have access to records that cover the period between examinations.

8. Consultations Outside of the Agency

In its release proposing new rules and rule amendments to implement the Dodd-Frank Act, the Commission requests public comment on the effect of information collection under this rule. Comments received may be viewed at <http://www.sec.gov/comments/s7-36-10/s73610.shtml>. We will consider all comments received on the proposal. In addition,

¹⁵ Proposed rule 203A-2(d)(3).

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.

9. Payment or Gifts to Respondents

None.

10. Assurances of Confidentiality

Responses to the recordkeeping responses required under rule 203A-2(d) in the context of the Commission's examination and oversight program are generally kept confidential.¹⁶

11. Sensitive Questions

Not applicable.

12. Estimate of Hour Burden

As of September 1, 2010, there were approximately 40 advisers relying on the exemption under rule 203A-2(e).¹⁷ Although it is difficult to estimate the number of advisers that would rely on the exemption if amended as proposed because such reliance is entirely voluntary, we estimate that approximately 110 additional advisers would rely on the exemption, for a total of 150 advisers.¹⁸ These advisers would incur an average

¹⁶ See Section 210(b) of the Advisers Act.

¹⁷ Based on IARD data as of September 1, 2010, of the approximately 11,850 SEC-registered advisers, 40 checked Item 2.A.(9) of Part 1A of Form ADV to indicate their basis for SEC registration under the multi-state advisers rule.

¹⁸ Based on IARD data as of September 1, 2010, 94 of the advisers that have less than \$100 million of assets under management currently file notice filings with 15 or more states. This number may overestimate the number of advisers required to be registered with 15 or more states, and therefore eligible for the proposed multi-state exemption, because

one-time initial burden of approximately 8 hours, and an average ongoing burden of approximately 8 hours per year, to keep records sufficient to demonstrate that they meet the 15-state threshold. These estimates are based on an estimate that each year an investment adviser would spend approximately 0.5 hours creating a record of its determination whether it must register as an investment adviser with each of the 15 states required to rely on the exemption, and approximately 0.5 hours to maintain these records.¹⁹ Accordingly, the Commission staff estimates the total initial and annual burden of the recordkeeping requirements of rule 203A-2(d) would be 1,200 hours if the proposal is adopted.²⁰

We anticipate that investment advisers would likely utilize senior operations managers to maintain the required records. The Commission estimates the hourly wage rate for a senior operations manager to be \$311 per hour, including benefits.²¹ Each adviser relying on the exemption would incur average initial and annual recordkeeping costs associated with rule 203A-2(d) of \$2,488 per adviser.²² If the proposal is adopted,

notice filing requirements may differ from registration requirements. In addition, we are unable to determine the number of advisers currently registered with the states that are registered with 15 or more states that may rely on the proposed exemption and register with us. We expect this number to be small based on the scope of business of an adviser that has less than \$25 million in assets under management and because section 222(d) of the Advisers Act provides a de minimis exemption for limited state operations without registration. For purposes of this analysis, we estimate the number is 15. As a result, we estimate that approximately 150 advisers would rely on the proposed exemption (40 currently relying on it + estimated 95 eligible based on IARD data + 15 advisers required to be registered in 15 or more states that are not registered with us today).

¹⁹ [0.5 hours x 15 states] + 0.5 hours = 7.5 hours + 0.5 hours = 8 hours.

²⁰ [8 hours x 110 advisers newly relying on the exemption] + [8 hours x 40 advisers currently relying on the exemption] = 880 + 320 = 1,200 hours.

²¹ Data from the Securities Industry Financial Markets Association's *Management & Professional Earnings in the Securities Industry 2009*, modified to account for an 1,800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead, suggest that the hourly rate for this position is \$311.

²² 8 hours x \$311 = \$2,488.

the Commission staff estimates that the total recordkeeping costs would be approximately \$373,200 per year.²³

13. Estimate of Total Annual Cost Burden

Excluding the burden hours identified in Item 12, the collection of information requirement for rule 203A-2(d) is not expected to impose additional non-labor or capital costs. The Commission anticipates that most advisers registering under the rule would generate the necessary records in the ordinary conduct of their advisory businesses.

14. Estimate of Cost to the Federal Government

There are no costs to the federal government directly attributable to rule 203A-2(d).

15. Explanation of Changes in Burden

Not applicable. This is the first request for approval of the collection of information for rule 203A-2(d).

16. Information Collections Planned for Statistical Purposes

Not applicable.

17. Approval to Display Expiration Date

Not applicable.

18. Exception to Certification Requirement

Not applicable.

B. COLLECTIONS OF INFORMATION EMPLOYING STATISTICAL METHODS

Not applicable.

²³ [110 advisers newly relying on the exemption x \$2,488] + [40 advisers currently relying on the exemption x \$2,488] = \$273,680 + \$99,520 = \$373,200.