

SUPPORTING STATEMENT
for the Paperwork Reduction Act New Information Collection Submission for
Rule 15c3-3

A. Justification

1. Necessity of Information Collection

During the “Paperwork Crisis” of 1967-1970, many brokers-dealers mishandled and misused customer funds and securities because they had inadequate and inefficient record keeping and segregation systems. Furthermore, the “bear market” of 1969-1970 caused many firms that lacked sufficient capital to utilize, properly or otherwise, customer funds and securities to obtain financing for their continued operation. In order to rectify these problems, the Securities and Exchange Commission (“Commission”) adopted Rule 15c3-3 (“Rule”) (17 CFR 240.15c3-3) to provide increased protection for the funds and securities of customers. The Rule is an integral part of the Commission’s financial responsibility program for brokers-dealers.

The Rule applies to all broker-dealers that hold securities or cash belonging to customers. Under the Rule, these broker-dealers must obtain and maintain possession or control of all the fully-paid and excess margin securities of their customers. In addition, they must make a periodic computation (“reserve computation”) to ascertain the amount of money they are holding that constitutes customer funds or funds obtained from the use of customer securities. If this amount known as “customer credits” exceeds the amount of money customers owe the firm (*i.e.*, customer debits), the broker-dealer must deposit the excess in a special reserve bank account for the exclusive benefit of the firm’s customers (“Special Reserve Bank Account”).¹ In this way, the Rule protects customer assets by requiring firms to maintain possession or control of customer securities, and by permitting firms to use customer money only to the extent necessary to finance customer related business.

The Rule requires broker-dealers to make the reserve computation on either a weekly or monthly basis. It also requires them (1) to maintain a description of the procedures utilized to comply with the possession and control requirements of the Rule; (2) to maintain a written notification from the bank where the Special Reserve Bank Account is located that all assets in the account are for the exclusive benefit of the broker-dealer’s customers; and (3) to give telegraphic notice to the Commission, and the appropriate Self-Regulatory Organization (“SRO”) if they fail to make a required deposit into the Special Reserve Bank Account.

In addition, paragraph (o) of Rule 15c3-3 requires that a broker-dealer that effects transactions in security futures products (“SFP”) for customers also must (1) establish written policies and procedures for determining whether customer SFPs will be placed in

¹ For purposes of this PRA, the term Special Reserve Bank Account includes accounts set up in accordance with both paragraph (e)(1) and paragraph (k)(2)(i).

a securities account or a futures account, and, if applicable, the process by which a customer may elect the type of account in which SFPs will be held, (2) provide each customer that plans to effect SFP transactions with a disclosure document containing certain information, (3) make a record of each change in account type, and (4) send each SFP customer notification of any change of account type.²

The Commission is statutorily authorized by Section 15(c)(3) of the Securities Exchange Act of 1934 (“Act”) (15 U.S.C. 782(c)(3)) to adopt rules as necessary for the protection of investors and to provide safeguards with respect to the financial responsibility and related practices of brokers and dealers. Further statutory authority is found in Sections 17(a) and 23(a) of the Act (15 U.S.C. 78q and 78w).

2. Purpose and Use of the Information Collection

The Rule is an integral part of the Commission’s financial responsibility program for broker-dealers. Its purpose is to protect the rights of customers to promptly obtain their property from a broker-dealer. The reserve and notice requirements in the Rule facilitate the process by which the Commission and the various SROs monitor how broker-dealers are fulfilling their custodial responsibilities to investors. With the exception of the telegraphic notice requirement, governmental agencies do not regularly receive any of the information described above. Instead, the information is stored by the broker-dealer and made available to the various securities regulatory authorities as required to facilitate examinations and investigations. If broker-dealers were not required to create and maintain this information, the Commission’s ability to fulfill its statutory directive to protect investors would be diminished.

Rule 15c3-3 also requires that a broker-dealer provide each customer that wishes to engage in SFP activities with a disclosure document and notification of any change of account type. Without these disclosures and notifications, customers may be uncertain or confused, if a liquidation were to occur, as to which regulatory scheme is applicable to their account.

3. Consideration Given to Information Technology

Nothing in Rule 15c3-3 would prevent a broker-dealer from using computers or other mechanical devices to generate, obtain, disclose or maintain the records and information required under these Rules, and most firms subject to Rule 15c3-3 presently utilize automated systems to comply with it. The Commission is not aware of any technical or legal obstacle to reducing the burden through the use of improved information technology.

² Exchange Act Release No. 46473 (September 9, 2002), 67 FR 58284 (September 13, 2002).

4. Duplication

There are no similar rules that are duplicative of Rule 15c3-3. Copies of notices required to be filed with the Commission under Rule 15c3-3(i) must also be filed with the regulatory authority that examines the broker-dealer for compliance with financial responsibility, helping to avoid duplication of rules.

5. Effects on Small Entities

Most small broker-dealers are exempt from the requirements of Rule 15c3-3 pursuant to paragraph 15c3-3(k). In addition, those small broker-dealers that are not exempt from the Rule can make the required computation monthly so long as they have aggregate indebtedness not exceeding 800% of net capital and carry aggregate customer funds not exceeding \$1,000,000.

6. Consequences of not Conducting Collection

If the required information were not conducted or were conducted less frequently, the level of protection afforded to the public by Rule 15c3-3 would be reduced.

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

There are no special circumstances. This collection is consistent with the guidelines in 5 CFR 1320.5(d)(2).

8. Consultations Outside the Agency

All Commission rule proposals are published in the Federal Register for public comment. This comment period is generally thirty days, which affords the public an opportunity to respond to any such proposals.

9. Payment or Gift

No payments of gifts have been provided to respondents.

10. Assurance of Confidentiality

The information collected under this Rule is kept confidential to the extent permitted by the Freedom of Information Act and any other applicable law.

11. Sensitive Questions

Questions of a sensitive nature are not asked.

12. Burden of Information Collection

As of December 31, 2009, there were approximately 279 broker-dealers fully subject to the Rule (*i.e.*, broker-dealers that can not claim any of the exemptions enumerated at paragraph (k)), of which approximately 13 make daily, 210 make weekly,

and 56 make monthly, reserve computations.³ The rule requires that each broker-dealer make a record of each such computation.⁴ The variation in size and complexity between these firms makes it very difficult to develop a meaningful figure for the amount of time required to make a record of each reserve computation. Based on experience in the area, Commission staff estimates that it takes between one and five hours, and that the average time spent across all the firms is 2.5 hours. Accordingly, Commission staff estimates that the resulting burden totals 36,780 hours annually ((2.5 hours x 240 computations x 13 respondents that calculate daily) + (2.5 hours x 52 computations x 210 respondents that calculate weekly) + (2.5 hours x 12 computations x 56 respondents that calculate monthly)). This is an ongoing recordkeeping burden.

A broker-dealer required to maintain the Special Reserve Bank Account prescribed by Rule 15c3-3 must obtain and retain a written notification from each bank in which it has a Special Reserve Bank Account to evidence bank's acknowledgement that assets deposited in the Account are being held by the bank for the exclusive benefit of the broker-dealer's customers.⁵ As stated previously, 279 broker-dealers are presently fully-subject to Rule 15c3-3. In addition, 120 broker-dealers operate in accordance with the exemption provided in paragraph (k)(2)(i) which also requires that a broker-dealer maintain a Special Reserve Bank Account. Broker-dealers generally maintain longstanding relationships with banks where they hold their Special Reserve Bank Accounts and thus do not need to obtain these letters often. The staff estimates that of the total broker-dealers that must comply with this rule, only 25%, or approximately 100 ((279 + 120) x .25) must obtain 1 new letter each year (either because the broker-dealer changed the type of business it does and became subject to either paragraph (e)(3) or (k)(2)(i) or simply because the broker-dealer established a new Special Reserve Bank Account). The staff estimates that it would take a broker-dealer approximately 1 hour to obtain this written notification from a bank regarding a Special Reserve Bank Account.⁶ Therefore, Commission staff estimates that broker-dealers will spend approximately 100 hours each year to obtain these written notifications. This is an ongoing recordkeeping burden.

In addition, a broker-dealer must immediately notify the Commission and its designated examining authority if it fails to make a required deposit to its Special Reserve Bank Account.⁷ Commission staff estimates that broker-dealers file approximately 33 such notices per year.⁸ Based on staff experience with the industry, it would take a broker-dealer approximately 30 minutes to file the notice required under the Rule. Therefore, Commission staff estimates that broker-dealers would spend a total of

³ Per December 31, 2009 FOCUS II reports filed with the Commission by broker-dealers in compliance with Rule 17a-5 (17 CFR 240.17a-5).

⁴ 17 CFR 240.15c3-3(e)(3).

⁵ 17 CFR 240.15c3-3(f).

⁶ The language in these letters is largely standardized.

⁷ 17 CFR 15c3-3(i).

⁸ From January 1, 2010 to October 1, 2010, broker-dealers had filed 25 such notices with the Commission. This amounts to approximately 2.78 notices per month. (2.78 x 12 months) = 33.36, or approximately 33 notices per year.

approximately 17 hours each year to comply with the notice requirement of Rule 15c3-3. This is an ongoing reporting and third party disclosure burden.

In addition, a broker-dealer that effects transactions in SFPs for customers⁹ also will have paperwork burdens associated with the requirement in paragraph (o) of Rule 15c3-3 to make a record of each change in account type and to provide certain customers with disclosure documents containing certain information SFP products.¹⁰ More specifically, a broker-dealer that changes the type of account in which a customer's SFPs are held must create a record of each change in account type that includes the name of the customer, the account number, the date the broker-dealer received the customer's request to change the account type, and the date the change in account type took place. As of December 31, 2010, broker-dealers that were also registered as FCMs reported that they maintained 35,242,468 customer accounts.¹¹ The staff estimates that 8% of these customers may engage in SFP transactions¹² (35,242,468 accounts x 8% = 2,819,397). Further, the staff estimates that 20% per year may change account type, therefore, a broker-dealer must promptly notify the customer in writing of the date that change became effective.¹³ Thus, broker-dealers may be required to create these records for up to 563,879 accounts (2,819,397 accounts x 20%). The staff believes that it will take approximately 3 minutes to create each record.¹⁴ Thus, the total annual burden associated with the paperwork burdens associated with paragraph (o) will be 28,194 hours (563,879 accounts x (3min/60min)). This is an ongoing recordkeeping and third party disclosure burden.

Consequently, the staff estimates that the total annual burden hours associated with Rule 15c3-3 would be approximately 65,091 hours (36,780 hours + 100 hours + 17 hours + 28,194 hours).

Commission staff believes that a broker-dealer would have 1) a financial reporting manager make a record of its reserve computations and send the required notices to the Commission, 2) an attorney obtain the written notifications from banks where it has a Special Reserve Bank Account to evidence bank's acknowledgement that assets deposited in the Account are being held by the bank for the exclusive benefit of

⁹ Broker-dealers that do not engage in an SFP business with or for customers are not affected by this section of Rule 15c3-3.

¹⁰ 17 CFR 240.15c3-3(o)(2) and (o)(3).

¹¹ Per December 31, 2009, FOCUS Schedule 1 filings.

¹² The staff derived its estimate from the number of active options accounts and conversations with industry representatives.

¹³ Broker-dealers that engage in an SFP business may choose not to allow customers to change account type because it may be costly to facilitate such conversions. In addition, once a customer has researched the issue and made a choice as to account type, it may be unlikely for the customer to change his or her account type.

¹⁴ In fact, the staff believes that most firms will have this process automated. To the extent that no person need be involved in the generation of this record, the burden will be very minimal.

customers, and 3) a compliance clerk create a record of each change in account type. The staff estimates that the hourly rate of a financial reporting manager and an attorney are \$290 and \$354, respectively,¹⁵ and the hourly rate of a compliance clerk is \$67.¹⁶ Consequently, the total cost of the above-described hour burden would be \$12,595,528.¹⁷ The staff notes these are internal labor costs only.

13. Costs to Respondents

In addition, a broker-dealer that effects transactions in SFPs for customers¹⁸ also will have an annualized cost burden associated with the requirements in paragraph (o) of Rule 15c3-3 to (1) provide each customer that plans to effect SFP transactions with a disclosure document containing certain information,¹⁹ and (2) send each SFP customer notification of any change of account type.²⁰

Pursuant to Rule 15c3-3(o)(2)(i), a broker-dealer that effects transactions in SFPs for customers must provide each customer that engages in SFP transactions with a disclosure document containing certain information. The costs of printing and sending the disclosure document to customers will be based on the number of customer accounts that will be opened by customers to effect transactions in SFPs. As stated previously in section 12 above, the staff estimates that 8% of the accounts held by broker-dealers that are also registered as FCMs, or 2,819,397 accounts, may engage in SFP transactions.²¹ The staff estimates that the cost of printing and sending each disclosure document will be approximately \$.15 per document sent.²² Thus, the staff estimates that the cost of printing and sending the disclosure document required pursuant to paragraph 15c3-3(o)(2)(i) will

¹⁵ The \$290/hour figure for a financial reporting manager and the \$354/hour figure for an attorney are derived from SIFMA's Management & Professional Salaries in the Securities Industry 2010, as modified by Commission staff to account for an 1,800 hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

¹⁶ The \$67/hour figure for a compliance clerk is derived from SIFMA's Office Salaries in the Securities Industry 2010, modified by Commission staff to account for an 1,800 hour work-year and multiplied by 2.93 to account for bonuses, firm size, employee benefits and overhead.

¹⁷ $((36,780 \text{ hours} + 17 \text{ hours}) \times \$290/\text{hour}) + (100 \text{ hours} \times \$354/\text{hour}) + (28,194 \text{ hours} \times \$67/\text{hour})$.

¹⁸ Broker-dealers that do not engage in an SFP business with or for customers are not affected by this section of Rule 15c3-3.

¹⁹ 17 CFR 240.15c3-3(o)(2).

²⁰ 17 CFR 240.15c3-3(o)(3)(ii).

²¹ The staff derived its estimate from the number of active options accounts and conversations with industry representatives.

²² This estimate is based on past conversations with industry representatives regarding other rule changes which required similar printing and postage costs. Postage may be minimized by including the disclosure document with other information mailed to customers. In addition, the estimate includes an inflation adjustment, and an increase to reflect the rise in postage costs.

be approximately \$422,910 (2,819,397 accounts x \$.15). This is an ongoing recordkeeping and third party disclosure burden.

Pursuant to Rule 15c3-3(o)(3)(ii), a broker-dealer that changes the type of account in which a customer's SFPs are held must promptly notify the customer in writing of the date that change became effective. The staff estimates that 563,879 accounts (2,819,397 accounts x 20%) may change account type per year, thus broker-dealers would be required to send this notification to 563,879 customers. The staff believes that firms will use the least cost method to comply with these requirements, and will probably include this notification with other mailings sent to the customer. The staff estimates that the cost of printing and posting each notification will be approximately \$.15 per document sent²³ (again, the rule is flexible enough that a broker-dealer may send this notification with other customer mailings, such as confirmations or customer account statements). Therefore, the staff estimates that the cost of sending this notification to customers will be about \$84,582 (563,879 accounts x \$.15). This is an ongoing recordkeeping and third party burden.

Consequently, the staff estimates that the total annual cost associated with Rule 15c3-3 would be \$507,492 (\$422,910 + \$84,582).

14. Costs to Federal Government

The government would experience no additional costs relating to the records broker-dealers must create pursuant to 15c3-3, but are not required to file with the Commission. However, the government would experience some costs associated with reviewing the notices broker-dealers are required to file pursuant to Rule 15c3-3. The staff estimates that reviewing these filings requires, on average, approximately fifteen minutes of Regulation Specialist staff time per filing at approximately \$70 an hour (based on an annual salary of \$84,000, adding average fringe benefits of 26% and average overhead of 25%, and dividing by 1,800 hours in a year). Consequently, the staff estimates that, the additional cost to the Federal Government associated with reviewing approximately 60 such notices per year would be \$1,050 (15 hours x \$70).

15. Changes in Burden

a. Burdens

The annual burden information collection of 65,091 hours listed on reflects a 12,075 decrease from the current OMB inventory of 77,166 hours. This change is due to a decrease in the number of broker-dealers; a decrease in the number of accounts of broker-dealers subject to paragraph (o) of Rule 15c3-3; and a decrease in the number of notices filed each year.

²³

See supra note 19.

Due to the fact that the calculation of burden hours is based on a number of factors (e.g., some respondents must make weekly calculations and others make monthly calculations, and certain of the burden hours are based on the number of accounts held by a distinct few of those respondents), the staff has divided the total number of annual burden hours by the number of respondents (279) to reach a number of hours per respondent in each of the three categories of reporting, recordkeeping and third party disclosure. For the 17 annual hours related to complying with the notice requirement of Rule 15c3-3(i), we have assumed that 50% of the annual hours relate to reporting and 50% relate to third party disclosure. For the 28,194 annual hours related to paragraph (o) of Rule 15c3-1, we have assumed that 50% of the annual hours relate to recordkeeping and 50% relate to third party disclosure. These assumptions result in an annual hour breakdown for recordkeeping, reporting and third party disclosure burdens as follows:

Recordkeeping	$\frac{[36,780 + 100 + (28,194/2)] \text{ hours annually}}{279 \text{ respondents}} = 182.71$	recordkeeping hours per respondent per year
Reporting	$\frac{(17/2) \text{ hours annually}}{279 \text{ respondents}} = 0.03$	reporting hours per respondent per year
Third party disclosure	$\frac{[(17/2) + (28,194/2)] \text{ hours annually}}{279 \text{ respondents}} = 50.56$	third party disclosure burden hours per respondent per year

b. Costs

The annual cost to respondents of \$507,492 each year as listed on OMB Form 83-I is \$60,344 more than the current OMB inventory of \$447,148. This increase is due to the increase cost estimate for printing and mailing related to SFP accounts subject to paragraph (o) of Rule 15c3-3.

Due to the fact that the calculation of costs is based on a number of factors that are not directly related to the calculation of burden hours above, for purposes of the Form 83-I, the staff has divided the total costs (\$507,492) by the number of respondents (279) to reach a number of cost per respondent (\$1,818.967). All of those costs related to reporting of information to customers (ongoing recordkeeping and

third party disclosure). We have assumed that 50% of these costs relate to recordkeeping and 50% related to third party disclosure.

16. Information Collection Planned for Statistical Purposes

This provision is not applicable because compliance with the Rule will not require the employment of statistical methods.

17. Display of OMB Approval Date

The Commission is not seeking approval not to display the expiration date for OMB approval.

18. Exceptions to Certification for Paperwork Reduction Act Submissions

This collection complies with the requirements in 5 CFR 1320.9

B. Collections of Information Employing Statistical Methods

This collection does not involve statistical methods.