

SUPPORTING STATEMENT

Rule 203A-5

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 has at least \$25 million in assets under management generally is prohibited from registering with the Securities and Exchange Commission (“Commission” or “SEC”).¹ The Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”)² amends section 203A to prohibit from Commission registration a “mid-sized adviser” that has assets under management between \$25 million and \$100 million, and: (i) is required to be registered as an investment adviser with the state in which it maintains its principal office and place of business; and (ii) if registered, would be subject to examination as an adviser by that state.³ The Commission also is adopting a rule that raises the threshold above which a mid-sized investment adviser must register with the Commission to \$110 million; but, once registered with the Commission, an adviser need not withdraw its registration until it has less than \$90 million of assets under management.⁴ As a consequence of section 410 of the Dodd-Frank Act and the new threshold the Commission is adopting, we estimate that approximately 3,200 SEC-

¹ 15 U.S.C. 80b-3a. An adviser must register with the Commission if it is not regulated or required to be regulated as an investment adviser in the state in which it maintains its principal office and place of business or if it advises a Commission-registered investment company. *Id.*

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

³ See section 410 of the Dodd-Frank Act. A mid-sized adviser may register with the Commission if it would be required to register with 15 or more states, or if it is an adviser to a registered investment company or business development company under the Investment Company Act of 1940. *See id.*

⁴ Amended rule 203A-1(a)(1).

registered advisers will be required to withdraw their registrations and register with one or more state securities authorities.⁵

The Commission is adopting a new rule, rule 203A-5, to provide for a transitional process by which an adviser no longer eligible for Commission registration will transition to state registration. Rule 203A-5 requires *each* investment adviser registered with the Commission on January 1, 2012 to file an amendment to its Form ADV no later than March 30, 2012.⁶ The amendment to Form ADV will, among other things, require each adviser to declare whether it remains eligible for Commission registration and to report the market value of its assets under management determined within 90 days of the filing.⁷ An adviser no longer eligible for Commission registration will have to withdraw its Commission registration by filing Form ADV-W no later than June 28, 2012.⁸

⁵ According to data from the Investment Adviser Registration Depository (“IARD”) as of April 7, 2011, 3,531 SEC-registered advisers either: (i) had assets under management between \$25 million and \$90 million and did not indicate on Form ADV Part 1A that they are relying on an exemption from the prohibition on Commission registration; or (ii) were permitted to register with us because they rely on the registration of an SEC-registered affiliate that has assets under management between \$25 million and \$90 million and they are not relying on an exemption. We estimate that 350 of these advisers are mid-sized advisers and will not switch to state registration because their principal office and place of business is located in Minnesota, New York, or Wyoming. *See Rules Implementing Amendments to the Investment Advisers Act of 1940*, Investment Advisers Act Release No. 3221, note 152 (attached as appendix A) (“Appendix A”) (according to IARD data as of April 7, 2011, there were 63 advisers in Minnesota, 286 in New York, and 1 in Wyoming). As a result, we estimate that approximately 3,200 advisers will switch to state registration. 3,531 SEC-registered advisers – 350 advisers not switching to state registration = 3,181 advisers.

⁶ New rule 203A-5(b); Appendix A section, II.A.1. Advisers registered with the Commission on July 21, 2011 that have at least \$25 million in assets under management will be exempt from the new prohibition on Commission registration for mid-sized advisers until 2012, when the rule will require them to switch to state registration and withdraw their SEC registration. *See* new rule 203A-5(a), Appendix A, section II.A.1.

⁷ *See* new rule 203A-5(b); Appendix A, sections II.A.1. and II.A.2.

⁸ New rule 203A-5(c)(1). The rule also would permit the Commission to postpone the effectiveness of, and impose additional terms and conditions on, an adviser’s withdrawal from SEC registration if the Commission institutes certain proceedings before the adviser files Form ADV-W. New rule 203A-5(c)(2).

Rule 203A-5 that the Commission is adopting differs from the rule the Commission proposed in several respects. First, the transition period begins on January 1, 2012, not the July 21, 2011 effective date of the Dodd-Frank Act, as proposed.⁹ Second, advisers will be required to file an amended Form ADV by March 30, 2012 (instead of August 20, 2011, as proposed), and mid-sized advisers no longer eligible for Commission registration will be required to withdraw by June 28, 2012 (instead of October 19, 2011, as proposed), which provides 180 days instead of the 90 days proposed.¹⁰ Third, the Commission is providing additional flexibility for an adviser to choose the date by which it must calculate its assets under management that it reports on Form ADV by requiring the same 90 day period as in Form ADV today, instead of 30 days, as proposed.¹¹

The rule's requirement to file an amendment to Form ADV will be a "collection of information" for Paperwork Reduction Act ("PRA") purposes.¹² The title of the new collection of information is: "Rule 203A-5." The likely respondents to this information collection are all investment advisers registered with the Commission on January 1, 2012. We have submitted this collection of information to OMB for review, and OMB has not yet assigned this collection a control number. 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. This collection of information will be found at 17

⁹ See proposed rule 203A-5(a)-(b); Appendix A, section II.A.1.

¹⁰ See proposed rule 203A-5(b)-(c); Appendix A, section II.A.1.

¹¹ See new rule 203A-5(b); amended Form ADV: Instructions for Part 1A, instr. 5.b.(4); Appendix A, section II.A.1.

¹² The PRA burden of the Form ADV-W filings that mid-sized advisers would be required to file to withdraw from Commission registration is reflected in the revised PRA burden for Form ADV-W. See Appendix A, notes 784-786 and accompanying text.

CFR 275.203a-5 and is mandatory. The information collected on Form ADV is not kept confidential.

2. Purposes of Information Collection

The Form ADV filing required by rule 203A-5 enables each investment adviser to determine whether it meets the revised eligibility criteria for Commission registration, and provides the Commission and the state regulatory authorities with information necessary to identify those advisers required to transition to state registration and to understand the reason for the transition or basis for continued Commission registration.¹³

3. Role of Improved Information Technology

The information collected pursuant to Form ADV takes the form of disclosures made by investment advisers to their clients and potential clients and reporting to the Commission. Investment advisers currently file their Form ADV electronically on the IARD system. This method of collecting information reduces the regulatory burden upon investment advisers by permitting them to file applications for registration, and amendments thereto, at one central location, rather than filing Form ADV separately with the Commission and the states for notice filing purposes.

4. Efforts to Identify Duplication

The collection of information requirements of rule 203A-5 are not duplicated elsewhere for investment advisers that must comply with these collection requirements.

5. Effect on Small Entities

The requirements of rule 203A-5 are the same for all investment advisers

¹³ Amended Item 2.A. of Form ADV, Part 1A reflects the requirements of the Advisers Act (as amended by the Dodd-Frank Act) and the related rules, and requires an investment adviser to mark Item 2.A.(13) if the adviser is no longer eligible to remain registered with the Commission. For a discussion of the rules, see Appendix A, sections II.A.5. and II.A.7., and for a discussion of Item 2.A, see Appendix A, section II.A.2.

registered with the Commission on January 1, 2012, including those advisers that are small entities. The rule does not affect most advisers that are small entities because they are generally required to be registered with one or more state securities authorities and not with the Commission. It would defeat the purpose of the rule to exempt small entities from these requirements. The Commission and state securities authorities need to be able to identify all of the advisers (both small advisers and larger advisers) switching to state registration or remaining registered with the Commission so they are able to verify which advisers should switch.

6. Consequences of Less Frequent Collection

Rule 203A-5 requires each investment adviser registered with the Commission on January 1, 2012 to file an amendment to its Form ADV that will, among other things, require each adviser to declare whether it remains eligible for Commission registration and to report the market value of its assets under management determined within 90 days of the filing.¹⁴ This collection of information is necessary to enable the Commission and the state regulatory authorities to identify those advisers required to transition to state registration and to understand the reason for the transition or basis for continued Commission registration. If the required information is not collected, the Commission and state regulatory authorities would not be able to verify which advisers should switch to state registration. Completing Form ADV also will assist each adviser to determine whether it meets the revised eligibility criteria for Commission registration.

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

Not applicable.

8. Consultations Outside of the Agency

¹⁴ See new rule 203A-5(b); Appendix A, sections II.A.1. and II.A.2.

In its release proposing new rules and rule amendments to implement the Dodd-Frank Act (“Proposing Release”), the Commission requested public comment on the effect of the information collection under this rule. The comments received are discussed below in item 12 in connection with the current estimates of the hour burden associated with rule 203A-5. In addition, 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

The information collected pursuant to rule 203A-5 will be provided through Form ADV filings with the Commission. These disclosures are not kept confidential.

11. Sensitive Questions

Not applicable.

12. Estimate of Hour Burden

We anticipate that the hour burden to refile Form ADV to comply with rule 203A-5 will be more like the burden to file an annual amendment than the burden to complete an other-than-annual amendment, as a result of our proposed changes to Part 1A. For purposes of calculating the currently approved PRA burden for Form ADV, Commission staff estimated that an annual updating amendment would take each adviser approximately 6 hours per amendment, on average.¹⁵ In addition, for purposes of the

¹⁵ See Appendix A, section VI.B.2.a.iii.

increased PRA burden for Form ADV, Commission staff estimates that the proposed amendments to Part 1A of Form ADV would take each adviser approximately 4.5 hours, on average, to complete.¹⁶ As a result, we estimate a total average time burden of 10.5 hours for each respondent completing the amendment to Form ADV (excluding private fund information which is addressed below).¹⁷

In the Proposing Release, we estimated that 11,850 advisers would file the Form,¹⁸ resulting in a total one-time burden of 157,775 hours.¹⁹ Several commenters expressed general concerns about the paperwork burdens of requiring all advisers to make an additional one-time filing of Form ADV.²⁰ Some commenters argued that the Commission should decrease the paperwork burden by exempting advisers unaffected by the statutory changes from the Form ADV filing requirement,²¹ or only requiring advisers to report their assets under management.²² Several commenters agreed with the Commission that the transition should be delayed until the IARD is able to accept filings of reviewed Form ADV, instead of implementing an alternative, such as requiring interim

¹⁶ See Appendix A, sections VI.B.1.a.

¹⁷ [6 hours (Form ADV annual amendment) + 4.5 hours (new new Form ADV items)] = 10.5 hours.

¹⁸ See Proposing Release, at n.293 and accompanying text.

¹⁹ 124,425 hours (Form ADV amendment) + 33,350 hours (private fund reporting) = 157,775 hours. See Proposing Release, at nn.403, 444.

²⁰ See, e.g., ICI Letter; MFA Letter; NYSBA Committee Letter; Shearman Letter.

²¹ ICI Letter (recommending exempting advisers that do not rely on assets under management to register with the SEC); MFA Letter (recommending exempting private fund advisers that file an initial Form ADV by July 21); NYSBA Committee Letter (recommending exempting advisers who will continue to be eligible for Commission registration and advisers relying on the section 203(b)(3) exemption that the Commission proposed would have to register with the Commission by July 21, 2011).

²² Shearman Letter.

paper filings that would increase the paperwork burdens.²³

Delaying the deadline under rule 203A-5 for advisers to re-file amended Form ADV until March 30, 2012, which coincides with most advisers' required annual updating amendment, significantly reduces the paperwork burden of rule 203A-5 by eliminating the requirement that these advisers incur the costs associated with a special one-time filing requirement for most registered advisers.²⁴ This deadline also coincides with the filing deadline for newly registering private fund advisers, which, as one commenter points out results in "a single, comprehensive Form ADV filing to register with the Commission" instead of requiring two filings that "would be costly, inefficient and potentially confusing."²⁵ As a result, approximately 7,600 advisers that will remain registered with the SEC after the transition will satisfy the Form ADV filing requirement by filing their annual amendment following their fiscal year ending on December 31, 2011, which reduces the number of advisers that will file an additional Form ADV

²³ See NASAA Letter ("the benefits of electronic filing, including easy public access to the documents, are significant and would outweigh any disadvantages imposed by a delay in filing deadlines."); NRS Letter (urging Commission not to "regress to paper filings" which would be "a huge step into the past" and "appears to be counter to Dodd-Frank Act purposes of transparency and consistency."). See also Dezellem Letter (the IARD is efficient and reduces risks of misplacing paper documents and possible filing errors); NYSBA Committee Letter (the IARD is the "most efficient mechanism for advisers and exempt reporting advisers to meet their filing obligations and make such filings to the public."). FINRA informed us that the IARD will be updated to reflect the revisions to Form ADV that we are adopting today beginning in November. See Appendix A, section II.A.1.

²⁴ See *infra* note 26. See also CMC Letter (suggesting "timing of the transition from federal to state registration could be centered around renewals for 2012").

²⁵ See MFA Letter.

attributable to rule 203A-5 to approximately 3,900,²⁶ for a total of 40,950 hours.²⁷ In addition, of these 3,900 registered advisers, we estimate that 850 advise one or more private funds and will have to complete the private fund reporting requirements.²⁸ We expect this will take 8,373 hours, in the aggregate.²⁹ We estimate that the total one-time burden for completing the Form ADV amendments to be 49,323 hours.³⁰

We anticipate that completing this filing would most likely be equally allocated between a senior compliance examiner and a compliance manager, at an hourly rate of \$235 and \$273 per hour, respectively.³¹ We estimate that each adviser would incur

²⁶ Based on IARD data as of April 7, 2011, 10,636 advisers reported on Form ADV a December 31 fiscal year end, of which we estimate approximately 3,013 will file a Form ADV to comply with the Form ADV filing requirement of new rule 203A-5 before switching to state registration because they reported assets under management of less than \$90 million and either: (i) they did not indicate on Part 1A of Form ADV that they are relying on an exemption from the prohibition on Commission registration; or (ii) they do not have a principal office and place of business in Minnesota, New York or Wyoming. Additionally, 868 advisers reported a fiscal year end other than December 31 and will file an additional, other-than-annual amendment to comply with new rule 203A-5. $3,013 + 868 = 3,881$. We have rounded this number to 3,900 for purposes of our analysis. The revised PRA burden for Form ADV includes the annual amendment filing by the approximately 7,600 advisers with a December 31 fiscal year end that we estimate will remain registered with the Commission after the switch.

²⁷ $10.5 \text{ hours} \times 3,900 \text{ advisers} = 40,950 \text{ hours}$.

²⁸ Based on IARD data as of April 7, 2011, 839 advisers out of the estimated 3,700 current SEC-registered advisers that advise private funds do not have a December fiscal year end or are expected to switch to state registration. We have rounded this number to 850 for purposes of this analysis.

²⁹ Based on IARD data as of April 7, 2011, we estimate that approximately 52 percent of these 850 private fund advisers, or 442, currently advise an average of 3 private funds each; 43 percent, or 365 advisers, currently advise an average of 10 private funds each; and the remaining 5 percent, or 43 advisers, currently advise an average of 79 private funds each. See Appendix A, note 697 and accompanying text. $(442 \text{ advisers} \times 3 \text{ funds} \times 1 \text{ burden hour per fund}) + (365 \times 10 \text{ funds} \times 1 \text{ burden hour per fund}) + (43 \text{ advisers} \times 79 \text{ funds} \times 1 \text{ burden hour per fund}) = 1,326 \text{ hours} + 3,650 \text{ hours} + 3,397 \text{ hours} = 8,373 \text{ hours}$.

³⁰ $40,950 \text{ (burden hours for Form ADV filing excluding private fund reporting)} + 8,373 \text{ (burden hours for private fund reporting)} = 49,323 \text{ total burden hours for Form ADV filing}$.

³¹ Data from the *Securities Industry Financial Markets Association's Management & Professional Earnings in the Securities Industry 2010*, modified to account for an 1,800-

average costs of approximately \$2,667 to complete the Form ADV amendment excluding private fund information,³² for a total aggregate cost of 10,401,300.³³ Additionally, we estimate the total aggregate cost for advisers to complete the private fund reporting requirements would be \$2,126,742,³⁴ resulting in total one-time costs of approximately \$12,528,042.³⁵

13. Estimate of Total Annual Cost Burden

\$0.

14. Estimate of Cost to the Federal Government

\$0.

15. Explanation of Changes in Burden

We have decreased the one-time total burden we established, and requested comment on, in the Proposing Release from 157,775 hours to 49,323 hours based on a lower estimated number of advisers that will refile Form ADV to comply with rule 203A-5, as adopted.

16. Information Collections Planned for Statistical Purposes

Not applicable.

hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead, suggest that costs for a senior compliance examiner and a compliance manager are \$235 and \$273 per hour, respectively.

³² [5.25 hours x \$235 = \$1,233.75] + [5.25 hours x \$273 = \$1,433.25] = \$2,667.

³³ 3,900 advisers x \$2,667 = \$10,401,300.

³⁴ (4,186.5 hours x \$235) + (4,186.5 x \$273) = \$983,827.5 + \$1,142,914.5 = \$2,126,742.

³⁵ \$10,401,300 (total cost for Form ADV filing excluding private fund reporting) + \$2,126,742 (total cost for private fund reporting) = \$12,528,042 (total cost for Form ADV filing).

17. Approval to Display Expiration Date

Not applicable.

18. Exception to Certification Requirement

Not applicable.

B. COLLECTIONS OF INFORMATION EMPLOYING STATISTICAL METHODS

Not applicable.