

**PAPERWORK REDUCTION ACT SUBMISSION
SUPPORTING STATEMENT
RULE 206(4)-3**

A. JUSTIFICATION

1. Necessity of Information Collection

Rule 206(4)-3 (17 CFR 275.206(4)-3) under the Investment Advisers Act of 1940, which is entitled “Cash Payments for Client Solicitations,” prohibits investment advisers from paying cash fees to solicitors for client referrals unless certain conditions are met. The rule requires that an adviser pay all solicitors’ fees pursuant to a written agreement that the adviser is required to retain.¹ When an adviser will provide only impersonal advisory services to the prospective client, the rule imposes no disclosure requirements. When the solicitor is affiliated with the adviser and the adviser will provide individualized advisory services to the prospective client, the solicitor must, at the time of the solicitation or referral, indicate to the prospective client that he is affiliated with the adviser. When the solicitor is not affiliated with the adviser and the adviser will provide individualized advisory services to the prospective client, the solicitor must, at the time of the solicitation or referral, provide the prospective client with a copy of the adviser's brochure and a disclosure document containing information specified in rule 206(4)-3.

Amendments to rule 206(4)-3, adopted in 2010 in connection with rule 206(4)-5, specify that solicitation activities involving a government entity, as defined in rule 206(4)-5, are subject to the additional limitations in rule 206(4)-5.

The information rule 206(4)-3 requires is necessary to inform advisory clients about the nature of the solicitor’s financial interest in the recommendation so the prospective clients may

¹ Rule 204-2 requires advisers to keep records of documents required by Rule 206(4)-3. Accordingly, no

consider the solicitor's potential bias, and to protect clients against solicitation activities being carried out in a manner inconsistent with the adviser's fiduciary duty to clients. The likely respondents to this information collection would be each investment adviser registered with the Securities and Exchange Commission (the "Commission") that compensates a solicitor in cash for referrals.

Rule 206(4)-3 contains "collection of information" requirements within the meaning of the Paperwork Reduction Act of 1995.² The title of this collection is "Rule 206(4)-3 under the Investment Advisers Act of 1940 (17 CFR 275.206(4)-3)" and the Commission submitted it to the Office of Management and Budget ("OMB") for review in accordance with 44 U.S.C. 3507(d) and 5 CFR 1320.11. OMB approved this collection under control number 3235-0242 (expiring on November 30, 2012). 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 number.

2. Purpose of the Information Collection

Investors need accurate information about compensation arrangements between an investment adviser and a solicitor in order to determine whether to retain an adviser recommended by the solicitor.

3. Consideration Given to Information Technology

The Commission's use of computer technology in connection with this information collection, which has been previously approved by OMB, would not change. Investment

recordkeeping burdens are addressed by this supporting statement.

² 44 U.S.C. 3501 to 3520.

advisers are permitted to provide the information required by rule 206(4)-3 electronically.³

4. Duplication

No other rule requires investment advisers to provide clients or prospective clients with the same information that is required by rule 206(4)-3.

5. Effect on Small Entities

The requirements for rule 206(4)-3 are the same for all investment advisers registered with the Commission, including small entities. It would defeat the purpose of the rule to exempt small entities from these requirements. For purposes of Commission rulemaking, an investment adviser is a small business if it has assets under management of less than \$25 million and meets certain other requirements. Advisers with assets under management of less than \$25 million are eligible to register with the Commission only if they advise a registered investment company, are not regulated or required to be regulated as an investment adviser in the state in which they maintain their principal office and place of business, or are qualified under rule 203A-2.

6. Consequences of Less Frequent Collection

Rule 206(4)-3 requires a solicitor to provide the required disclosure at the time of the solicitation or referral; without this information at the time of the solicitation or referral, the client would be unaware of the solicitor's financial interest in the recommendation.

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

This collection is consistent with the guidelines in 5 CFR 1320.5(d)(2).

³ Use of Electronic Media by Broker-Dealers, Transfer Agents, and Investment Advisers for Delivery of Information; Additional Examples Under the Securities Act of 1933, Securities Exchange Act of 1934, and Investment Company Act of 1940, Investment Advisers Act Release No. 1562 (May 9, 1996).

8. Consultation Outside the Agency

The Commission and 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 staff with a means of ascertaining and acting upon paperwork burdens confronting the industry. In addition, the Commission requested public comment on the information collection requirements in rule 206(4)-3 before submitting this request for extension and approval to the Office of Management and Budget. The Commission received no comments in response to this request.

9. Payment or Gift to Respondents

The respondents receive no payments or gifts.

10. Confidentiality

The information collected pursuant to rule 206(4)-3 requires solicitors to provide information to advisory clients and prospective clients. Accordingly, these disclosures would not be kept confidential.

11. Sensitive Questions

Not applicable.

12. Burden of Information Collection

We estimate that about 35% of the approximately 11,737 investment advisers registered

with the Commission, or 4,159 advisers (11,737 x 35%) use rule 206(4)-3.⁴ Compliance with the rule will require approximately 7.04 burden hours each year per respondent, or a total of 29,279 hours (7.04 x 4,159). It is the experience of the Commission staff that the contract and solicitor disclosure documents used in compliance with the rule are generally quite brief and that on average not more than 11 referrals per adviser using the rule are made annually. We therefore estimate that compliance with the rule will result in 45,749 total annual responses (4,159 x 11). Compliance professionals and clerical staff are likely to prepare and deliver these documents, and we estimate the hourly wage rate for compliance professionals to be \$279,⁵ including benefits, and the hourly rate for clerical staff to be \$52,⁶ including benefits. Accordingly, we estimate the annual cost to each respondent of this hour burden to be \$1,165 (3.52 hours of professional time at \$279 per hour (approx. \$982), and 3.52 hours of clerical time at \$52 per hour (approx. \$183)) for a total annual cost of the hour burden of approximately \$4,845,734 (\$1,165 x 4,159).

13. Cost Burden to Respondents

Rule 206(4)-3 does not impose any cost burden on the respondents.

⁴ Previous estimates for purposes of the Paperwork Reduction Act concluded that approximately 20% of advisers registered with the Commission had cash referral fee arrangements and would thus be subject to the rule.

⁵ Data from the Securities Industry and Financial Markets Association's Management & Professional Earnings in the Securities Industry 2011 (the "SIFMA Report"), 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 cost for a Compliance Manager is approximately \$279 per hour.

⁶ Data from the SIFMA Report, modified to account for an 1,800-hour work-year and multiplied by 2.93 to account for bonuses, firm size, employee benefits and overhead, suggest that the cost for a General Clerk is approximately \$52 per hour.

14. Cost to the Federal Government

Rule 206(4)-3 does not impose any costs on the Federal government because there are no separate filing requirements with the Commission.

15. Explanation of Changes in Burden

The number of responses per investment adviser and the number of hours per response have not changed since the last estimate. The number of respondents increased from 2,321 investment advisers to 4,159 investment advisers. As a result, the total burden hours for all respondents has increased from 15,848 hours to 29,279. This increase is due to an increase in the estimated number of respondents. The revised average burden per Commission-registered adviser would be 7.04 hours.⁷

16. Information Collection Planned for Statistical Purposes

Not applicable. The information collection is not used for statistical purposes.

17. OMB Expiration Date Display

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

18. Exceptions to Certification Statement

This collection complies with the requirements in 5 CFR 1320.9.

B. COLLECTION OF INFORMATION EMPLOYING STATISTICAL METHODS

The collection of information does not employ statistical methods.

⁷ 29,279.36 (revised annual aggregate burden) divided by 4,159 (total number of registrants who rely on rule) = 7.04.