

SUPPORTING STATEMENT
for the Paperwork Reduction Act Information Collection Submission for
“Rule 17g-3”

A. JUSTIFICATION

1. Necessity of Information Collection

The Credit Rating Agency Reform Act of 2006¹ (“Rating Agency Act”), enacted on September 29, 2006, defines the term “nationally recognized statistical rating organization,” or “NRSRO” and provides authority for the Securities and Exchange Commission (“Commission”) to implement registration, recordkeeping, financial reporting, and oversight rules with respect to registered credit rating agencies.

The Commission adopted rule amendments that will impose additional requirements on NRSROs in order to address concerns about the integrity of their credit rating procedures and methodologies in light of the role they played in determining credit ratings for securities collateralized by or linked to subprime residential mortgages.²

Rule 17g-3 contains reporting requirements.³ The collection of information obligations imposed by this rule is mandatory. The requirements of Rule 17g-3, however, apply only to credit rating agencies that are registered with the Commission as NRSROs, and registration is voluntary.

The Rating Agency Act added Section 15E, “Registration of Nationally Recognized Statistical Rating Organizations,”⁴ to the Securities Exchange Act of 1934 (“Exchange Act”). Exchange Act Section 15E(k) requires an NRSRO to furnish to the Commission, on a confidential basis and at intervals determined by the Commission, such financial statements and information concerning its financial condition that the Commission, by rule, may prescribe as necessary or appropriate in the public interest or for the protection of investors.⁵

2. Purpose and Use of the Information Collection

Information collected under Rule 17g-3 is necessary for Commission oversight of registered NRSROs.

3. Consideration Given to Information Technology

The requirements of Rule 17g-3 are not designed to collect information through electronic submission. NRSROs will submit the report in paper format.

¹ Pub. L. No. 109-291, 120 Stat. 1327 (2006).

² Amendments to Rules for Nationally Recognized Statistical Rating Organizations, Exchange Act Release No. 59342 (February 2, 2009), 74 FR 6456 (February 9, 2009).

³ The OMB Control Number for Rule 17g-3 is 3235-0626.

⁴ 15 U.S.C. 78o-7.

⁵ 15 U.S.C. 78o-7(k).

4. Duplication

We are not aware of duplication of this information.

5. Effect on Small Entities

Small entities may be affected by Rule 17g-3 because all NRSROs, regardless of size, will be required to submit the financial reports to the Commission on an annual basis.

6. Consequences of Not Conducting Collection

If the required reports were not collected frequently, the Commission would be unable to ascertain, on an ongoing basis, whether a credit rating agency registered as an NRSRO “fail[ed] to maintain adequate financial and managerial resources to consistently produce credit ratings with integrity.”⁶ Further, if the required collections were conducted less frequently, the information in the reports would become outdated.

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

The required Federal Register notice with a 60-day comment period soliciting comments on this collection of information was published. No public comments were received.

9. Payment or Gift

No payment or gift is provided to respondents.

10. Confidentiality

Pursuant to section 15E(k) of the Exchange Act, reports submitted to the Commission are submitted on a “confidential basis.”

11. Sensitive Questions

Not applicable; no information of a sensitive nature is required.

12. Burden of Information Collection

The number of respondents subject to the rule depends, in part, on the number of entities that meet the statutory requirements for eligibility for registration. Further,

⁶ 15 U.S.C. 78o-7(d)(1)(E).

registration is voluntary, and, consequently, the number of respondents will also depend on the number of entities that choose to register with the Commission. The Commission previously estimated that approximately 30 credit rating agencies would register with the Commission as NRSROs under section 15E of the Exchange Act.⁷

Since that time, ten credit rating agencies have registered with the Commission as NRSROs. Consequently, while the Commission expects several more credit rating agencies may become registered as NRSROs over the next few years, the Commission believes that the actual number of NRSROs (*i.e.*, ten) should be used for purposes of the Paperwork Reduction Act.⁸

The Commission estimates that each NRSRO that registers with the Commission will take, on average, approximately 200 hours to prepare for and submit its annual audited financial statements for an industry-wide total of 2,000 hours (200 hours x 10 NRSROs).⁹

13. Cost to Respondents

The cost of an audit by an independent public accountant varies substantially with the size and complexity of the NRSRO. The current OMB estimate is that, on average, an NRSRO will pay an independent public accountant approximately \$15,000 per year to perform an audit or audit procedures that are required by Rule 17g-3.¹⁰ Therefore, the annual cost burden to the industry is approximately \$150,000.¹¹

Given the potentially sensitive nature of the proposed report, the Commission also preliminarily believes that an NRSRO would likely engage outside counsel to assist it in the process of drafting and reviewing the proposed report under Rule 17g-3. The Commission estimates that the time an outside attorney would spend on this work would depend on the size and complexity of the NRSRO. The Commission estimates that, on average, an outside counsel would spend approximately 20 hours assisting an NRSRO and its designated compliance officer in drafting and reviewing the proposed report on a one-time basis for an aggregate burden to the industry of 200 hours.¹² Based on industry sources, the Commission estimates that the cost of an outside counsel would be approximately \$400 per hour.¹³ For these reasons, the Commission estimates that the

⁷ See Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations, Exchange Act Release No. 55857 (June 5, 2007), 72 FR 33564 at 33607 (June 18, 2007).

⁸ See Nationally Recognized Statistical Rating Organizations, Exchange Act Release No. 64514 (May 18, 2011), 76 FR 33420 at 33499 (June 8, 2011).

⁹ See 17 CFR 240.15c3-1 and 17 CFR 240.17i-5.

¹⁰ Based on staff experience, it is estimated that the annual audit report for a small NRSRO will range from \$3,000 - \$5,000 while the annual audit report for a large NRSRO would be substantially greater.

¹¹ \$15,000 x 10 NRSROs = 150,000.

¹² 10 NRSROs x 20 hours = 200 hours.

¹³ The same estimate for the hourly cost for legal services was used by the Commission in its definitions release related to swaps and security-based swaps under Title VII of the Dodd-Frank Act. Further Definition of “Swap,” “Security-Based Swap,” and “Security-Based Swap Agreement”; Mixed Swaps: Security-Based Swap Agreement Recordkeeping, Exchange Act Release No. 67453 (July 18, 2012), 77 FR 48208 (Aug. 13, 2012).

average one-time cost to an NRSRO would be approximately \$8,000¹⁴ and the one-time cost to the industry would be approximately \$80,000. The Commission is averaging this burden estimate over the three year approval period.¹⁵ Therefore, the total annual cost per respondent is \$41,670 and the total annual cost to the industry would be approximately \$416,700.

14. Costs to Federal Government

There are no costs to the Federal government associated with the information collections required under Rule 17g-3.

15. Changes in Burden

The changes in annual burden hours are a result of the Commission's adjustment of the estimate of the number of registered NRSROs (i.e., 30 respondents) to the actual number of registered NRSROs (i.e., 10 respondents).¹⁶

16. Information Collection Planned for Statistical Purposes

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

17. Approval to Omit the OMB Expiration Date

The Commission is not seeking approval to omit the expiration date for this information collection.

18. Exceptions to Certification

This collection complies with the requirements in 5 CFR 1320.9.

B. COLLECTION OF INFORMATION EMPLOYING STATISTICAL METHODS

The collection does not involve any statistical methods.

¹⁴ \$400 per hour x 20 hours = \$8,000.

¹⁵ \$8,000 x 10 NRSROs = \$80,000/3 = \$26,670.

¹⁶ See Nationally Recognized Statistical Rating Organizations, Exchange Act Release No. 64514 at 301-302. "In adopting the first rules under the Rating Agency Act of 2006, the Commission estimated that approximately 30 credit rating agencies ultimately would be registered as NRSROs. Since that time, 10 credit rating agencies have registered with the Commission as NRSROs. This number has remained constant for several years. Consequently, while the Commission expects several more credit rating agencies may become registered as NRSROs over the next few years, the Commission preliminarily believes that the actual number of NRSROs should be used for purposes of the PRA." Id.