

**SUPPORTING STATEMENT**  
**for the Paperwork Reduction Act Information Collection Submission for**  
**“Rule 17j-1”**

**A. JUSTIFICATION**

**1. Information Collection Necessity**

Conflicts of interest between investment company personnel (such as portfolio managers) and their funds can arise when these persons buy and sell securities for their own accounts (“personal investment activities”). These conflicts arise because fund personnel have the opportunity to profit from information about fund transactions, often to the detriment of fund investors. Section 17(j) of the Investment Company Act of 1940 (the “Investment Company Act”) (15 U.S.C. 80a-17(j)) makes it unlawful for persons affiliated with a registered investment company (“fund”) or with the fund’s investment adviser or principal underwriter (each a “17j-1 organization”), in connection with the purchase or sale of securities held or to be acquired by the investment company, to engage in any fraudulent, deceptive, or manipulative act or practice in contravention of the Commission’s rules and regulations. Section 17(j) also authorizes the Commission to promulgate rules requiring 17j-1 organizations to adopt codes of ethics.

In order to implement section 17(j), rule 17j-1 imposes certain requirements on 17j-1 organizations and “Access Persons”<sup>1</sup> of those organizations. The rule prohibits fraudulent, deceptive or manipulative acts by persons affiliated with a 17j-1 organization in connection with their personal securities transactions in securities held or to be acquired by the fund. The rule requires each 17j-1 organization, unless it is a money market fund or a fund that does not invest in Covered Securities,<sup>2</sup> to: (i) adopt a written codes of ethics; (ii) submit the code and any material changes to the code, along with a certification that it has

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<sup>1</sup> Rule 17j-1(a)(1) defines an “access person” as “Any Advisory Person of a Fund or of a Fund’s investment adviser. If an investment adviser’s primary business is advising Funds or other advisory clients, all of the investment adviser’s directors, officers, and general partners are presumed to be Access Persons of any Fund advised by the investment adviser. All of a Fund’s directors, officers, and general partners are presumed to be Access Persons of the Fund.” The definition of Access Person also includes “Any director, officer or general partner of a principal underwriter who, in the ordinary course of business, makes, participates in or obtains information regarding, the purchase or sale of Covered Securities by the Fund for which the principal underwriter acts, or whose functions or duties in the ordinary course of business relate to the making of any recommendation to the Fund regarding the purchase or sale of Covered Securities.” Rule 17j-1(a)(1).

<sup>2</sup> A “Covered Security” is any security that falls within the definition in section 2(a)(36) of the Act, except for direct obligations of the U.S. Government, bankers’ acceptances, bank certificates of deposit, commercial paper and high quality short-term debt instruments, including repurchase agreements, and shares issued by open-end funds. Rule 17j-1(a)(4).

adopted procedures reasonably necessary to prevent Access Persons from violating the code of ethics, to the fund board for approval; (iii) use reasonable diligence and institute procedures reasonably necessary to prevent violations of the code; (iv) submit a written report to the fund describing any issues arising under the code and procedures and certifying that the 17j-1 entity has adopted procedures reasonably necessary to prevent Access Persons from violating the code; (v) identify Access Persons and notify them of their reporting obligations; and (vi) maintain and make available to the Commission for review certain records related to the code of ethics and transaction reporting by Access Persons.

The rule requires each Access Person of a fund (other than a money market fund or a fund that does not invest in Covered Securities) and of an investment adviser or principal underwriter of the fund, who is not subject to an exception,<sup>3</sup> to file: (i) within 10 days of becoming an Access Person, a dated initial holdings report that sets forth certain information with respect to the Access Person's securities and accounts; (ii) dated quarterly transaction reports within 30 days of the end of each calendar quarter providing certain information with respect to any securities transactions during the quarter and any account established by the Access Person in which any securities were held during the quarter; and (iii) dated annual holding reports providing information with respect to each Covered Security the Access Person beneficially owns and accounts in which securities are held for his or her benefit. In addition, rule 17j-1

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<sup>3</sup> Rule 17j-1(d)(2) contains the following exceptions: (i) an Access Person need not file a report for transactions effected for, and securities held in, any account over which the Access Person does not have control; (ii) an independent director of the fund, who would otherwise be required to report solely by reason of being a fund director and who does not have information with respect to the fund's transactions in a particular security, does not have to file an initial holdings report or a quarterly transaction report; (iii) an Access Person of a principal underwriter of the fund does not have to file reports if the principal underwriter is not affiliated with the fund (unless the fund is a unit investment trust) or any investment adviser of the fund and the principal underwriter of the fund does not have any officer, director, or general partner who serves in one of those capacities for the fund or any investment adviser of the fund; (iv) an Access Person to an investment adviser need not make quarterly reports if the report would duplicate information provided under the reporting provisions of the Investment Adviser's Act of 1940; (v) an Access Person need not make quarterly transaction reports if the information provided in the report would duplicate information received by the 17j-1 organization in the form of broker trade confirmations or account statements or information otherwise in the records of the 17j-1 organization; and (vi) an Access Person need not make quarterly transaction reports with respect to transactions effected pursuant to an Automatic Investment Plan.

requires investment personnel of a fund or its investment adviser, before acquiring beneficial ownership in securities through an initial public offering (IPO) or in a private placement, to obtain approval from the fund or the fund's investment adviser.

## **2. Purpose of the Information Collection**

Rule 17j-1 provides for oversight by a fund's board of directors of the codes of ethics and procedures employed by the fund, its investment advisers and underwriters to prevent fraudulent, deceptive, or manipulative acts in connection with the purchase or sale by persons associated with those entities of securities held or to be acquired by the fund. Without the rule, fund boards and the Commission would be hampered in their ability to monitor fully the conduct of such persons for activities that are fraudulent, deceptive or manipulative.

## **3. Role of Improved Information Technology**

Some 17j-1 entities employ computerized transaction reporting and recordkeeping systems to reduce the burden in connection with rule 17j-1. Although these systems can impose substantial start-up and maintenance costs, they can help to reduce the information collection burdens arising under rule 17j-1. The Commission permits the use of such technologies to comply with rule 17j-1.

## **4. Duplication**

The Commission is not aware of any duplicate reporting or recordkeeping requirements. Rule 17j-1(d)(2)(iv) under the Investment Company Act relieves an Access Person of the duty to file reports if those reports would duplicate reports required by rules under the Investment Advisers Act of 1940.<sup>4</sup> Rule 17j-1(d)(2)(v) exempts an Access Person from filing the quarterly transaction report if it would duplicate information already received by the 17j-1 organization in the form of broker trade confirmations or account statements or information otherwise in the records of the 17j-1 organization.

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<sup>4</sup> Investment Adviser Codes of Ethics, Investment Advisers Act Release No. 2256 (Jul. 2, 2004) (69 FR 41696 (Jul. 9, 2004)).

Information collected under the rule is intended to improve board oversight of personal investment activities of fund personnel. Similar information would not achieve that goal.

**5. Effect on Small Entities**

All rule 17j-1 organizations, regardless of size, must adopt a code of ethics and keep records of reports submitted by Access Persons. The reporting and recordkeeping requirements for small entities could not be reduced without risking harm to investors' interests.

**6. Consequences of Less Frequent Collection**

In order for fund boards to play a meaningful oversight role, it is necessary for them to receive no less frequently than annually reports from the fund, its investment advisers and underwriters regarding issues arising under the code of ethics. Rule 17j-1, by requiring Access Persons to provide initial holdings reports, quarterly transactions reports, and annual holdings reports, enables rule 17j-1 organizations to monitor the securities transactions of Access Persons to ensure compliance with their codes of ethics. Less frequent collection of such reports would hinder these organizations from enforcing their codes.

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

Not applicable.

**8. Consultation Outside the Agency**

The Commission requested public comment on the collection of information requirements in rule 17j-1 before it submitted this request for approval to the Office of Management and Budget. The Commission received no comments in response to this request.

More generally, the Commission and the staff participate in an ongoing dialogue with representatives of the investment company industry through public conferences, meetings, and informal exchanges. These various forums provide the Commission and the staff with a means of ascertaining and acting upon the paperwork burdens confronting the industry.

**9. Payment or Gift**

Not applicable.

**10. Confidentiality**

Not applicable.

**11. Sensitive Questions**

Not applicable.

**12. Estimate of Time Burden**

The staff spoke with representatives of a number of 17j-1 organizations. Based upon these conversations and its experience with the industry, the staff has made the following estimates with respect to the reporting burden. As noted above, Access Persons must file initial and annual holdings reports and quarterly transaction reports. Investment personnel must obtain approval before acquiring beneficial ownership in any securities through an IPO or private placement. In addition, rule 17j-1 organizations have a number of responsibilities, most of which are carried out at the fund complex level<sup>5</sup>, arising from information collection requirements under rule 17j-1. The organizations must notify Access Persons of their reporting obligations, prepare an annual rule 17j-1 report and certification for the board, document their approval or rejection of IPO and private placement requests, maintain annual rule 17j-1 records, maintain electronic reporting and recordkeeping systems, amend their codes of ethics as necessary, and, for new fund complexes, adopt a code of ethics.

The estimated burdens associated with these information collections are set forth in the table below.

<b>Information Collection</b>	<b>Annual Hours Per Person or Complex</b>	<b>Annual Aggregate Hours</b>	<b>Person Responsible</b>	<b>Hourly Rate (\$)<sup>6</sup></b>	<b>Annual Aggregate Cost (\$)</b>
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<sup>5</sup> The staff estimates that there are 832 fund complexes currently operating.

<sup>6</sup> All hourly rates used in this analysis (except for the “Access Person” average rate of \$246 per hour and the aggregate board rate) are derived from salaries reported in Securities Industry and Financial Markets Association, Management and Professional Earnings in the Securities Industry (2011) and Securities Industry and Financial Markets Association,

<b>Information Collection</b>	<b>Annual Hours Per Person or Complex</b>	<b>Annual Aggregate Hours</b>	<b>Person Responsible</b>	<b>Hourly Rate (\$)<sup>6</sup></b>	<b>Annual Aggregate Cost (\$)</b>
Initial Holdings Report	2	13,312 <sup>7</sup>	New Access Person	246 <sup>8</sup>	3,274,752 <sup>9</sup>
Quarterly Transaction Report	1/4	6,250 <sup>10</sup>	Access Person	246	1,537,500 <sup>11</sup>
Annual Holdings Report	3/4	52,500 <sup>12</sup>	Access Person	246	12,915,000 <sup>13</sup>
IPO/Private Placement Preapproval Request	1	4,992 <sup>14</sup>	Investment Personnel	246	1,228,032 <sup>15</sup>
Informing Access Persons of Reporting Obligation	3	2,496	Compliance Officer	279	696,384 <sup>16</sup>

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Office Salaries in the Securities Industry (2011) modified to account for an 1800-hour work-year and multiplied by 2.93 or 5.35 to account for bonuses, firm size, employee benefits and overhead.

<sup>7</sup> We estimate that there are approximately 8 new Access Persons per fund complex each year and 5,240 total new Access Persons each year (8 new Access Persons × 832 fund complexes = 6,656 new Access Persons). In addition, we estimate that the total number of Access Persons remains approximately steady due to attrition. This is based on the following calculation: (6,656 new Access Persons × 2 hours = 13,312 hours).

<sup>8</sup> Although hourly rates of Access Persons differ, we estimate that, on average, the time for Access Persons required to complete initial holdings reports and other transaction reports costs \$246 per hour. Access Persons would include portfolio managers, directors and other officers of the fund. The \$246 rate is that of a typical mid level portfolio manager.

<sup>9</sup> This is based on the following calculations: (6,656 new Access Persons × 2 hours = 13,312 hours; 13,312 hours × \$246 rate = \$3,274,752).

<sup>10</sup> We estimate that annually 25,000 quarterly transactions reports are filed. Access Persons do not have to file such reports in certain instances including, for example, when they have not engaged in any securities transactions during a particular quarter, or when the relevant information is contained in duplicate broker trade confirmations or account statements received by the firm.

<sup>11</sup> This is based on the following calculations: (25,000 quarterly reports × .25 hour = 6,250 hours; 6,250 hours × \$246 rate = \$1,537,500).

<sup>12</sup> Each of the approximately 70,000 Access Persons must file an annual holdings report. This is based on the following calculation: (70,000 Access Persons × .75 hour = 52,500 hours).

<sup>13</sup> This is based on the following calculation: (52,500 hours × \$246 rate = \$12,915,000).

<sup>14</sup> We estimate that each of the 832 fund complexes receives approximately 6 such requests each year, for a total of approximately 4,992 such requests filed each year.

<sup>15</sup> This is based on the following calculations: (4,992 IPO requests × 1 hour = 4,992 hours; 4,992 hours × \$246 rate = \$1,228,032).

<sup>16</sup> This is based on the following calculations: (832 fund complexes × 3 hours = 2,496 hours; 2,496 hours × \$279 rate = \$696,384).

<b>Information Collection</b>	<b>Annual Hours Per Person or Complex</b>	<b>Annual Aggregate Hours</b>	<b>Person Responsible</b>	<b>Hourly Rate (\$)<sup>6</sup></b>	<b>Annual Aggregate Cost (\$)</b>
Preparation of Annual Report to Board and Certification	8 1/2	7,072	Chief Compliance Officer (50%) Attorney for Fund Complex (50%)	433 <hr/> <hr/> 378	2,867,696 <sup>17</sup>
Documentation of IPO/Private Placement Approval/Rejection	3 (½ hour per request)	2,496	Chief Compliance Officer	433	1,080,768 <sup>18</sup>
Rule 17j-1 Recordkeeping, Review and Analysis	300	249,600	Chief Compliance Officer (5%) Compliance Clerk (95%)	433 <hr/> <hr/> 60	19,631,040 <sup>19</sup>
Maintenance of Computer Systems for Use in 17j-1 Reporting and Recordkeeping	50	41,600	Programmer Analyst	196	8,153,600 <sup>20</sup>

<sup>17</sup> This is based on the following calculations: (832 fund complexes × 8.5 hours = 7,072 hours; 7,072 ÷ 2 = 3,536 hours (50% division between CCO and attorney); 3,536 hours × \$433 rate = \$1,531,088 CCO costs; 3,536 hours × \$378 rate = \$1,336,608 attorney costs; \$1,531,088 CCO costs + \$1,336,608 attorney costs = \$2,867,696 total costs).

<sup>18</sup> This is based on the following calculations: (4,992 IPO requests × .5 hour for processing each request = 2,496 hours; 1965 hours × \$433 rate = \$1,080,768).

<sup>19</sup> This is based on the following calculations: (832 fund complexes × 300 hours = 249,600 hours; 249,600 × .95 = 237,120 hours clerk time (12,480 hours CCO time with a 95% and 5% division between clerk and CCO); 12,480 CCO hours × \$433 rate = \$5,403,840 CCO costs; 237,120 clerk hours × \$60 rate = \$14,227,200 clerk costs; \$5,403,840 CCO costs + \$14,227,200 clerk costs = \$19,631,040 total costs).

<sup>20</sup> This is based on the following calculations: (832 fund complexes × 50 hours = 41,600 hours; 41,600 hours × \$196 rate = \$8,153,600).

<b>Information Collection</b>	<b>Annual Hours Per Person or Complex</b>	<b>Annual Aggregate Hours</b>	<b>Person Responsible</b>	<b>Hourly Rate (\$)<sup>6</sup></b>	<b>Annual Aggregate Cost (\$)</b>
Preparation and Board Approval of New Code of Ethics for New Fund Complex	25	625 <sup>21</sup>	Chief Compliance Officer (40%) Attorney for Fund Complex (40%) Board of Directors (20%)	433 <u>378</u> <u>4,500<sup>22</sup></u>	765,250 <sup>23</sup>
Preparation and Board approval of Material Amendments to Existing Codes of Ethics, Implementing Policies and Procedures, and Board Review and Certification	8	6,656	Chief Compliance Officer (25%) Attorney for Fund Complex (50%) Board of Directors (25%)	433 <u>378</u> <u>4,500</u>	9,466,496 <sup>24</sup>
<b>TOTAL</b>		<b>387,599</b>			<b>61,616,518</b>

We estimate that annually there are approximately 75,496 respondents under rule 17j-1, of which

<sup>21</sup> We estimate that there are 25 new fund complexes formed each year.

<sup>22</sup> Commission staff estimates that a fund board's hourly rate is \$4500 per hour (on average, a board has 9 directors and the fund pays each director \$500 per hour).

<sup>23</sup> This is based on the following calculations: (25 new fund complexes × 25 hours = 625 hours; 625 hours × .40 = 250 hours (40% division each for CCO and attorney); 625 hours × .20 = 125 hours (board time); 250 hours × \$433 rate = \$108,250 CCO costs; 250 hours × \$378 rate = \$94,500 attorney costs; 125 hours × \$4,500 rate = \$562,500, \$108,250 CCO costs + \$94,500 attorney costs + \$562,500 board costs = \$765,250 total costs).

<sup>24</sup> This is based on the following calculations: (832 fund complexes × 8 hours = 6,656 hours, 6,656 hours × .25 = 1,664 hours (25% division each for CCO and Board); 6,656 hours × .50 = 3,328 hours (attorney time); 1,664 hours × \$433 rate = \$720,512 CCO costs; 3,328 hours × \$378 rate = \$1,257,984 attorney costs; 1,664 hours × \$4,500 rate = \$7,488,000, \$720,512 CCO costs + \$1,257,984 attorney costs + \$7,488,000 board costs = \$9,466,496 total costs).



5,496 are rule 17j-1 organizations<sup>25</sup> and 70,000 are Access Persons. In the aggregate, these respondents make approximately 107,780 responses annually.<sup>26</sup> As the table shows, we estimate that the total annual burden of complying with the information collection requirements in rule 17j-1 is approximately 387,599 hours and the cost of those hours is approximately \$61,616,518.

The estimate of average burden hours is made solely for the purposes of the Paperwork Reduction Act. The estimate is not derived from a comprehensive or even a representative survey or study of Commission rules. Reporting burdens may differ substantially across respondents.

### **13. Annual Cost Burden**

We estimate that there is an annual cost burden of approximately \$5,000 per fund complex, for a total of \$4,160,000<sup>27</sup>, associated with complying with the information collection requirements in rule 17j-1, aside from the cost of the burden hours discussed above.<sup>28</sup> This represents the costs of purchasing and maintaining computers and software to assist funds in carrying out rule 17j-1 recordkeeping. The estimate of the average cost burden is made solely for the purposes of the Paperwork Reduction Act. The estimate is not derived from a comprehensive or even a representative survey or study of Commission rules. Reporting burdens may differ substantially across respondents.

### **14. Cost to the Federal Government**

There is no cost to the federal government of administering the information collection requirements in rule 17j-1 under the Investment Company Act.

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<sup>25</sup> Currently, there are approximately 4,184 active funds, approximately 937 investment advisers to funds, and approximately 375 principal underwriters to funds, for a total of 5,496 17j-1 organizations.

<sup>26</sup> This estimate is based on the following calculation: (6,656 initial holdings reports by Access Persons + 25,000 quarterly transaction reports by Access Persons + 70,000 annual holdings reports by Access Persons + 4,992 preapproval requests by Access Persons for purchases of initial public offerings and private placements + 832 annual certifications by fund boards + 275 annual material amendments + 25 new codes of ethics for new fund complexes = 107,780 annual responses).

<sup>27</sup> This estimate is based on the following calculation: (\$5,000 software costs × 832 fund complexes = \$4,160,000 total costs).

<sup>28</sup> The cost burden associated with filing of new and amended codes of ethics on the Commission's Electronic Data Gathering, Analysis, and Retrieval system (EDGAR) is included in the Paperwork Reduction Act estimates for the relevant forms to which these codes must be appended.

**15. Changes in Burden**

The increase from 292,740 burden hours to 387,599 hours (an increase of 94,859 hours) reflects a change in the estimated number of Access Persons and fund complexes, as well as adjustments to the hour estimates we made based on discussions with representatives of fund complexes about their experiences in complying with rule 17j-1. The increase in costs from \$3,275,000 to \$4,160,000 (an increase of \$885,000) associated with the collections of information is attributable to an increase in the number of fund complexes currently operating.

**16. Information Collection Planned for Statistical Purposes**

Not applicable.

**17. Approval to Omit OMB Expiration Date**

Not applicable.

**18. Exception to Certification Statement**

Not applicable.

**B. COLLECTIONS OF INFORMATION EMPLOYING STATISTICAL METHODS**

Not applicable.