SUPPORTING STATEMENT

FOR THE PAPERWORK REDUCTION ACT INFORMATION COLLECTION SUBMISSION

Proposed Rule 18f-4

A. JUSTIFICATION

1. Necessity for the Information Collection

Section 18 of the Investment Company Act of 1940 ("Investment Company Act")[1] imposes various limitations on the capital structure of funds, including, in part, by restricting the ability of funds to issue "senior securities," as defined in that section.[2] The protection of investors against the potentially adverse effects of a fund's issuance of senior securities is a core purpose of the Investment Company Act.[3] Section 18(g) of the Investment Company Act defines "senior security," in part, as "any bond, debenture, note, or similar obligation or instrument constituting a security and evidencing indebtedness."[4]

On December 11, 2015, the Commission issued a release proposing new rule 18f-4, which would require a fund that relies on the rule in order to enter into derivatives transactions to: (i) comply with one of two alternative portfolio limitations designed to impose a limit on the amount of leverage the fund may obtain through derivatives transactions and other senior securities transactions; (ii) manage the risks associated with its derivatives transactions by maintaining an amount of certain assets, defined in the rule as "qualifying coverage assets," designed to enable the fund to meet its obligations under its derivatives transactions; and (iii) depending on the extent of its derivatives usage, establish a derivatives risk management

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1 15 U.S.C. 80a-1 *et seq.*

2 *See* 15 U.S.C. 80a-18.

3 *See*, *e.g.*, 15 U.S.C. 80a-1(b)(7), 1(b)(8), 18(a), and 18(f).

4 The definition of senior security in section 15 U.S.C. 80a-18 also includes "any stock of a class having priority over any other class as to the distribution of assets or payment of dividends" and excludes certain limited temporary borrowings.

program. A fund that relies on the proposed rule in order to enter into financial commitment transactions would be required to maintain qualifying coverage assets equal in value to the fund's full obligations under those transactions.[5]

Compliance with proposed rule 18f-4 would be mandatory for all funds that seek to engage in derivatives transactions and financial commitment transactions in reliance on the rule, which would otherwise be subject to the restrictions of section 18. No information would be submitted directly to the Commission under proposed rule 18f-4. To the extent that records required to be created and maintained by funds under the rule are provided to Commission staff in connection with examinations or investigations, such information would be kept confidential subject to the provisions of applicable law.

2. Purpose and Use of the Information Collection

Certain of the provisions of the proposed rule contain "collection of information" requirements within the meaning on the Paperwork Reduction Act of 1995 ("Paperwork Reduction Act"),[6] and the Commission is submitting the collection of information to the Office of Management and Budget ("OMB") for review in accordance with 44 U.S.C. 3507(d) and 5 CFR 1320.11. The proposed rule is designed to address the investor protection purposes and concerns underlying section 18 of the Act and to provide an updated and more comprehensive approach to the regulation of funds' use of derivatives transactions in light of the dramatic growth in the volume and complexity of the derivatives markets over the past two decades and the increased use of derivatives by certain funds.

The information collection requirements of proposed rule 18f-4 are designed to ensure that funds appropriately limit the amount of leverage that may be obtained through derivatives transactions and other senior securities transactions and manage the risks associated with derivatives transactions and financial commitment transactions. The information collections also

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[5] Investment Company Act Release No. 31933 (Dec. 11, 2015) [80 FR 80883 (Dec. 28, 2015)].

[6] 44 U.S.C. 3501 *et seq.*

assist the Commission's examination staff in assessing funds' compliance with the proposed rule and identifying weaknesses in a fund's management of derivatives transactions and financial commitment transactions if violations occur or are uncorrected.

3. Consideration Given to Information Technology

Proposed rule 18f-4 requires that each fund relying on the proposed rule maintain certain written records relating to the fund's selection of a portfolio limitation; its compliance with the portfolio limitation, asset segregation and other requirements of the proposed rule; and if the fund is required to implement a formalized derivatives risk management program, copies of the program's policies and procedures and copies of any materials provided to the board of directors related to the operation of the program. The Electronic Signatures in Global and National Commerce Act[7] and the conforming amendments to rules under the Investment Company Act permit funds to maintain records electronically.

4. Duplication

The Commission periodically evaluates rule-based reporting and recordkeeping requirements for duplication and reevaluates them whenever it proposes a rule or a change in a rule. Proposed rule 18f-4 imposes a requirement that funds relying on the proposed rule maintain certain written records relating to the fund's selection of a portfolio limitation; its compliance with the portfolio limitation, asset segregation and other requirements of the proposed rule; and if the fund is required to implement a formalized derivatives risk management program, copies of the program's policies and procedures and copies of any materials provided to the board of directors related to the operation of the program. The information required by proposed rule 18f-4 is not generally duplicated elsewhere.

[7] P.L. 106-229, 114 Stat. 464 (June 30, 2000).

5. Effect on Small Entities

The information collection requirements of proposed rule 18f-4 do not distinguish between small entities and other funds. The burden of the conditions on smaller funds may be proportionally greater than for larger funds. The Commission believes, however, that imposing different requirements on smaller investment companies would not be consistent with investor protection and the purposes of the rule's conditions and could potentially jeopardize the interests of investors in small funds. The Commission reviews all rules periodically, as required by the Regulatory Flexibility Act, to identify methods to minimize recordkeeping or reporting requirements affecting small businesses.

6. Consequences of Not Conducting Collection

Proposed rule 18f-4 requires funds relying on the proposed rule to maintain certain written records relating to the fund's selection of a portfolio limitation; its compliance with the portfolio limitation, asset segregation and other requirements of the proposed rule; and if the fund is required to implement a formalized derivatives risk management program, copies of the program's policies and procedures and copies of any materials provided to the board of directors related to the operation of the program.

Not collecting information or collecting such information less frequently would be incompatible with the objectives of rule 18f-4. The reporting of information and the establishment of written policies and procedures and maintaining written reports are integral parts to ensuring compliance with the proposed rule and detecting and correcting any violations or potential violations before irrevocable or widespread harm is inflicted upon investors. Not requiring the collection of information increases the likelihood that such harm could go unchecked.

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

Proposed rule 18f-4 would require a fund to maintain for at least five years: (i) a record of each determination made by the fund's board that the fund will comply with one of the portfolio limitations; (ii) certain written records that document the fund's ongoing compliance with the conditions of the proposed rule, including a written copy of the policies and procedures approved by the board regarding the fund's maintenance of qualifying coverage assets and a written record demonstrating that the fund complied with the applicable portfolio limitation; (iii) written records reflecting the fund's mark-to-market and risk-based coverage amounts and the fund's financial commitment obligations, and identifying the qualifying coverage assets maintained by the fund to cover these amounts; and (iv) records relating to the derivatives risk management program, if the fund is required to adopt and implement a derivatives risk management program.[8] Although this five-year period exceeds the three-year guideline for most kinds of records under 5 CFR 1320.5(d)(2), the staff believes that this is warranted because the rule contributes to the effectiveness of the Commission's examination and inspection program. Because the period between examinations may be as long as five years, it is important that the Commission have access to records that cover the entire period between examinations.

The five-year retention period in proposed rule 18f-4 is consistent with that in rule 38a-1(d) under the Investment Company Act. We believe that consistency in these retention periods is appropriate because funds currently have program-related recordkeeping procedures in place incorporating a five-year retention period. Furthermore, we believe that a five-year retention period would lessen the compliance burden of proposed rule 18f-4 slightly, compared to choosing a different retention period, such as the six-year recordkeeping retention period under rule 31a-2 of the Investment Company Act.

8. Consultation Outside the Agency

Before adopting proposed rule 18f-4, the Commission will receive and evaluate public comments on the proposal and its collection of information requirements. Moreover, the Commission and the staff of the Division of Investment Management participate in an ongoing

[8] *See* proposed rule 18f-4(a)(6)(iii).

dialogue with representatives of the investment company industry through public conferences, meetings, and information exchanges. These various forums provide the Commission and staff with a means of ascertaining and acting upon the paperwork burdens confronting the industry.

9. Payment or Gift

No payment or gift to respondents was provided.

10. Assurance of Confidentiality

No information would be submitted directly to the Commission under proposed rule 18f-4. Other information provided to the Commission in connection with staff examinations or investigations would be kept confidential subject to the provisions of applicable law. If information collected pursuant to proposed rule 18f-4 is reviewed by the Commission's examination staff, it will be accorded the same level of confidentiality accorded to other responses provided to the Commission in the context of its examination and oversight program.

11. Sensitive Questions

No PII collected/Not applicable.

12. Estimate of Hour Burden

The following estimates of average burden hours and costs are made solely for purposes of the Paperwork Reduction Act and are not derived from a comprehensive or even representative survey or study of the cost of Commission rules and forms. Compliance with proposed rule 18f-4 would be mandatory for all funds that seek to engage in derivatives transactions and financial commitment transactions in reliance on the proposed rule, which would otherwise be subject to the restrictions of section 18.

A. <u>Portfolio Limitations for Derivatives Transactions</u>

Proposed rule 18f-4 would require a fund that engages in derivatives transactions in reliance on the proposed rule to comply with one of two alternative portfolio limitations.[9] Under

[9] Proposed rule 18f-4(a)(1).

the exposure-based portfolio limit, a fund generally would be required to determine that, immediately after entering into any senior securities transaction, its aggregate exposure does not exceed 150% of the value of the fund's net assets.[10] Under the risk-based portfolio limit, a fund generally would be required to determine that, immediately after entering into any senior securities transaction, (1) the fund's full portfolio VaR does not exceed its securities VaR and (2) the fund's aggregate exposure does not exceed 300% of the value of the fund's net assets.[11] Proposed rule 18f-4 would require a fund's board of directors, including a majority of the directors who are not interested persons of the fund, to approve (a) the fund's determination to comply with either the exposure-based portfolio limit or the risk-based portfolio limit under the proposed rule, and (b) if applicable, the fund's determination to limit its aggregate exposure under derivatives transactions to not more than 50% of its NAV and not to use complex derivatives transactions.[12]

Staff estimates that 3,831 funds will seek to rely on this part of proposed rule 18f-4 and therefore comply with the portfolio limitation requirements. These funds would be subject to the collections of information described below with respect to their applicable portfolio limitations.

Initial Determination of Portfolio Limitations

We estimate a one-time burden of 3 hours per fund associated with a board's review and approval of a fund's portfolio limitation or, amortized over a three-year period, a burden of approximately 1 hour annually per fund. We therefore estimate that the total hourly burden for the initial reviews and approvals of funds' portfolio limitations would be 11,493 hours.[13] We

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[10] Proposed rule 18f-4(a)(1)(i).

[11] Proposed rule 18f-4(a)(1)(ii).

[12] Proposed rule 18f-4(a)(5)(i). The cost burdens associated with a fund board's approvals include costs incurred to prepare materials for the board's determinations, as well as the board's review and approval of determinations required by the proposed rule.

[13] This estimate is based on the following calculation: 3 hours x 3,831 funds = 11,493 hours.

estimate that each fund would incur a time cost of approximately $5,121 to obtain this initial approval, for a total initial time cost for all funds of approximately $19,618,551.[14]

Recordkeeping

The proposed rule would require a fund to maintain a record of each determination made by the fund's board that the fund will comply with one of the portfolio limitations under the proposed rule, which would include the fund's initial determination as well as a record of any determination made by the fund's board to change the portfolio limitation.[15] We estimate a one-time burden of 0.6 hours per fund associated with maintaining a record of a board's initial determination of the fund's portfolio limit or, amortized over a three-year period, a burden of about 0.2 hours annually per fund. We therefore estimate that the total burden for maintaining a record of a board's initial determination of the fund's portfolio limit would be 2,299 hours.[16] We also estimate that each fund would incur a time cost of approximately $38 to meet this requirement, for a total initial time cost of approximately $164,733.[17]

In addition, a fund that relies on the proposed rule also would be subject to an ongoing requirement to maintain a written record demonstrating that immediately after the fund entered

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14 This estimate is based on the following calculations: 0.6 hours x $301 (hourly rate for a senior portfolio manager) = $181; 0.6 hours x $455.5 (blended hourly rate for assistant general counsel ($426) and chief compliance officer ($485) = $273; 1.0 hours x $4,400 (hourly rate for a board of 8 directors) = $4,400; 0.8 hours (for a fund attorney's time to prepare materials for the board's determinations) x $334 (hourly rate for a compliance attorney) = $267. $181 + $273 + $4,400 + $267 = $5,121; $5,121 x 3,831 funds = $19,618,551. The hourly wages used are from SIFMA's Management & Professional Earnings in the Securities Industry 2013, modified to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits, and overhead. The staff previously estimated in 2009 that the average cost of board of director time was $4,000 per hour for the board as a whole, based on information received from funds and their counsel. Adjusting for inflation, the staff estimates that the current average cost of board of director time is approximately $4,400.

15 Proposed rule 18f-4(a)(6)(i). The fund would be required to maintain this record for a period of not less than five years (the first two years in an easily accessible place) following each determination.

16 This estimate is based on the following calculation: 0.6 hours x 3,831 funds = 2,299 hours.

17 This estimate is based on the following calculation: 0.3 hours x $57 (hourly rate for a general clerk) = $17; 0.3 hours x $87 (hourly rate for a senior computer operator) = $26. $17 + $26 = $43; $43 x 3,831 funds = $164,733.

into any senior securities transaction, the fund complied with its applicable portfolio limit, with such record reflecting the fund's aggregate exposure, the value of its net assets and, if applicable, the fund's full portfolio VaR and its securities VaR.[18] We estimate that each fund would incur an average burden of 50 hours to retain these records.[19] We therefore estimate that the total annual burden for maintaining these records would be 191,550 hours.[20] We also estimate that each fund would incur an annual time cost of approximately $3,600, and a total annual time cost for all funds of approximately $13,791,600.[21]

Accordingly, we estimate that, for recordkeeping associated with a fund's portfolio limitations, including maintenance of a record of a board's initial determination of the fund's portfolio limit and maintenance of written records demonstrating the fund's ongoing compliance with applicable portfolio limits, the time burden per fund would be 50.6 hours and the time cost per fund would be $3,638.[22] We therefore estimate that the total burden for maintaining such records would be 193,849 hours, at an aggregate time cost of $13,937,178.[23]

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18 Proposed rule 18f-4(a)(6)(iv). The fund would be required to maintain this record for a period of not less than five years (the first two years in an easily accessible place) following each senior securities transaction. This written record requirement would also apply to a fund's monitoring of the 50% portfolio limit for purposes of the derivatives risk management program requirement (discussed below).

19 We assume for purposes of this estimate that funds would implement automated processes for creating a written record of their compliance with the applicable portfolio limit immediately after entering into any senior securities transaction, and that a fund would enter into at least one derivatives transaction or other senior securities transaction per trading day. Based on 250 trading days per year, and assuming 0.1 hours per trading day spent by a general clerk and 0.1 hours per trading day spent by a senior computer operator, we estimate the annual time cost to be (0.1 x 250) = 25 hours per year per fund for each general clerk and senior computer operator.

20 This estimate is based on the following calculations: 50 hours x 3,831 funds = 191,550 hours.

21 This estimate is based on the following calculation: 25 hours x $57 (hourly rate for a general clerk) = $1,425; 25 hours x $87 (hourly rate for a senior computer operator) = $2,175. $1,425 + $2,175 = $3,600; $3,600 x 3,831 funds = $13,791,600.

22 This estimate is based on the following calculations: 0.6 hours (maintenance of a record of board's initial determination of fund's portfolio limit) + 50 hours (maintenance of written records demonstrating fund's compliance with applicable portfolio limits) = 50.6 hours; $38 (maintenance of a record of a board's initial determination of a fund's portfolio limit) + $3,600 (maintenance of written records demonstrating funds' compliance with applicable portfolio limits) = $3,638.

23 This estimate is based on the following calculations: 50.6 hours x 3,831 funds = 193,849 hours; $3,638 x 3,831 funds = $13,937,178.

Estimated Total Burden

Amortized over a three-year time period, the hour burdens and time costs for collections of information associated with portfolio limitations under proposed rule 18f-4, including the burdens associated with (a) board review and approval of funds' initial portfolio limitations, (b) maintenance of records of initial board determinations of funds' portfolio limits, and (c) maintenance of written records demonstrating funds' compliance with applicable portfolio limits, are estimated to result in an aggregate average annual hour burden of 196,147 hours and aggregate time cost of $20,386,028.[24]

B. <u>Asset Segregation: Derivatives Transactions</u>

Proposed rule 18f-4 would require a fund that enters into derivatives transactions in reliance on the proposed rule to manage the risks associated with its derivatives transactions by maintaining an amount of qualifying coverage assets designed to enable the fund to meet its obligations arising from such transactions.[25] A fund would be required to identify on the books and records of the fund, at least once each business day, qualifying coverage assets with a value equal to at least the fund's aggregate "mark-to-market coverage amounts" and "risk-based coverage amounts."[26] A fund would also be required to have policies and procedures approved by its board of directors that are reasonably designed to provide for the fund's maintenance of qualifying coverage assets.[27]

Staff estimates that 3,831 funds will seek to rely on this aspect of proposed rule 18f-4 and therefore comply with the asset segregation requirements. These funds would be subject to the collections of information described below with respect to asset segregation requirements.

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24 These estimates are based on the following calculations: (11,493 hours (year 1) + 2,299 hours (year 1) + (3 x 191,550 hours) (years 1, 2 and 3)) ÷ 3 = 196,147 hours; ($19,618,551 (year 1) + ($164,733 (year 1) + (3 x $13,791,600)) ÷ 3 = $20,386,028.

25 Proposed rule 18f-4(a)(2), (c)(6), (c)(8), (c)(9).

26 Proposed rule 18f-4(a)(2).

27 Proposed rule 18f-4(a)(5)(ii).

Identification of Qualifying Coverage Assets

We estimate that each fund would incur an average annual burden of 110 hours associated with the identification of qualifying coverage assets. We therefore estimate that the total annual burden for the identification of qualifying coverage assets would be 421,410 hours.[28] We also estimate that each fund would incur an annual time cost of approximately $11,530 to identify qualifying coverage assets, for a total annual time cost for all funds of approximately $44,171,430.[29]

Board-Approved Policies & Procedures

Proposed rule 18f-4 would require funds to have written policies and procedures reasonably designed to provide for the fund's maintenance of qualifying coverage assets. We estimate that a fund would incur a one-time average burden of 15 hours associated with documenting its policies and procedures. The proposed rule would also require that the fund's board approve such policies and procedures and we estimate a one-time burden of 1 hour per fund associated with fund boards' review and approval of its policies and procedures. Amortized over a three-year period, this would be an annual burden per fund of approximately 5.3 hours. We estimate that the total one-time burden for the initial documentation, and board approval of, written policies and procedures to provide for a fund's maintenance of qualifying coverage assets would be 61,296 hours.[30] We also estimate that each fund would incur a time cost of approximately $6,291, and a total initial time cost for all funds of approximately $38,593,494.[31] We estimate that there are no ongoing annual costs associated with this collection of information.

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28 This estimate is based on the following calculation: 110 hours x 3,831 funds = 421,410 hours.

29 This estimate is based on the following calculations: 100 hours x $87 (hourly rate for a senior computer operator) = $8,700; 10 hours x $283 (hourly rate for compliance manager) = $2,830. $8,700 + $2,830 = $11,530; $11,530 x 3,831 funds = $44,171,430.

30 This estimate is based on the following calculation: 16 hours x 3,831 funds = 61,296 hours.

31 This estimate is based on the following calculations: 7.5 hours x $301 (hourly rate for a senior portfolio manager) = $2,258; 7.5 hours x $455.5 (blended hourly rate for assistant general counsel ($426) and chief compliance officer ($485)) = $3,416; 1 hour x $4,400 (hourly rate for a board of 8 directors) = $4,400. $2,258 + $3,416 + $4,400= $10,074; $10,074 x 3,831 funds = $38,593,494.

Recordkeeping

The proposed rule would require a fund to maintain a written copy of the policies and procedures approved by the fund's board of directors that are in effect, or at any time within the past five years were in effect, in an easily accessible place. We estimate a one-time burden (and no ongoing annual burden) of 1 hour per fund associated with maintaining a written copy of the fund's board-approved policies and procedures or, amortized over a three-year period, a burden of approximately 0.3 hours annually per fund. We therefore estimate that the total one-time burden for maintaining this record would be 3,831 hours.[32] We also estimate that each fund would incur a time cost of approximately $57, and a total initial time cost for all funds of approximately $218,367.[33]

In addition, a fund that relies on the proposed rule also would be subject to an ongoing requirement to maintain a written record reflecting the mark-to-market coverage amount and risk-based coverage amount for each derivatives transaction entered into by the fund and identifying the associated qualifying coverage assets, as determined by the fund at least once each business day, for a period of not less than five years (the first two years in an easily accessible place).[34] We estimate that each fund would incur an average annual burden of 50 hours to retain these records.[35] We therefore estimate that the total annual burden for maintaining these records would

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32 This estimate is based on the following calculation: 1 hour x 3,831 funds = 3,831 hours.

33 This estimate is based on the following calculation: 1 hour x $57 (hourly rate for a general clerk) = $57. $57 x 3,831 funds = $218,367.

34 Proposed rule 18f-4(a)(6)(v).

35 We assume for purposes of this estimate that funds would implement automated processes for creating a written record of their compliance with the qualifying coverage asset requirements and that a fund would enter into at least one derivatives transaction per trading day. Based on 250 trading days per year, and assuming 0.1 hours per trading day spent by a general clerk and 0.1 hours per trading day spent by a senior computer operator, we estimate the annual time cost to be (0.1 x 250) = 25 hours per year per fund for each general clerk and senior computer operator.

be 191,550 hours.[36] We also estimate that each fund would incur an annual time cost of approximately $3,600, and a total annual time cost for all funds of approximately $13,791,600.[37]

Estimated Total Burden

Amortized over a three-year time period, the hour burdens and time costs for collections of information associated with the asset segregation requirement for derivatives transactions under proposed rule 18f-4, including the burdens associated with (a) identifying qualifying coverage assets; (b) documenting board-approved policies and procedures; and (c) maintaining required records, are estimated to result in an aggregate average annual hour burden of 634,669 hours and aggregate time costs of $70,900,317.[38]

C. Asset Segregation: Financial Commitment Transactions

Proposed rule 18f-4 would require a fund that enters into financial commitment transactions in reliance on the proposed rule to similarly maintain qualifying coverage assets designed to enable the fund to meet its obligations arising from such transactions. A fund would be required to identify on the books and records of the fund, at least once each business day, qualifying coverage assets with a value equal to at least the fund's aggregate financial commitment obligations.[39] A fund that enters solely into financial commitment transactions would, as described above for a fund that enters into derivatives transactions, be required to have policies and procedures approved by its board of directors that are reasonably designed to provide for the fund's maintenance of qualifying coverage assets.[40]

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36 This estimate is based on the following calculations: 50 hours x 3,831 funds = 191,550 hours.

37 This estimate is based on the following calculation: 25 hours x $57 (hourly rate for a general clerk) = $1,425; 25 hours x $87 (hourly rate for a senior computer operator) = $2,175. $1,425 + $2,175 = $3,600; $3,600 x 3,831 funds = $13,791,600.

38 These estimates are based on the following calculations: ((3 x 421,410 hours) (years 1, 2 and 3) + 61,296 (year 1) + 3,831 (year 1) + (3 x 191,550 hours) (years 1, 2 and 3)) ÷ 3 = 634,669 hours; ((3 x $44,171,430) + ($38,593,494 (year 1)) + ($218,367 (year 1)) + (3 x $13,791,600) (years 1, 2, and 3)) ÷ 3 = $70,900,317.

39 Proposed rule 18f-4(b)(1).

40 Proposed rule 18f-4(b)(2)(3).

Staff estimates 359 funds would comply with the asset segregation requirements in proposed rule 18f-4 applicable to financial commitment transactions and would not also be complying with the asset segregation and other requirements applicable to derivatives transactions. In addition, staff estimates that 537 money market funds and 88 BDCs may engage in certain types of financial commitment transactions. In sum, staff estimates that 984 funds would comply with the asset segregation requirements applicable to financial commitment transactions and incur the same costs we estimate above (with regard to funds that engage in derivatives transactions). These funds would be subject to the collections of information described below.

Identification of Qualifying Coverage Assets

We estimate that each fund would incur an average annual burden of 110 hours (and no initial one-time burdens) associated with the identification of qualifying coverage assets. We therefore estimate that the total annual burden for the identification of qualifying coverage assets would be 108,240 hours.[41] We also estimate that each fund would incur an ongoing annual time cost of approximately $11,530 to identify qualifying coverage assets, for a total ongoing annual time cost for all funds of approximately $11,345,520.[42]

Board-Approved Policies & Procedures

A fund that enters solely into financial commitment transactions, like a fund that enters into derivatives transactions, would be required under the proposed rule to have board-approved policies and procedures regarding the maintenance of qualifying coverage assets. Accordingly, we estimate that a fund would incur a one-time average burden of 15 hours associated with documenting its policies and procedures. The proposed rule would also require that the fund's board approve such policies and procedures and we estimate a one-time burden of 1 hour per fund

41 This estimate is based on the following calculation: 110 hours x 984 funds = 108,240 hours.

42 This estimate is based on the following calculations: 100 hours x $87 (hourly rate for a senior computer operator) = $8,700; 10 hours x $283 (hourly rate for compliance manager) = $2,830. $8,700 + $2,830 = $11,530; $11,530 x 984 funds = $11,345,520.

associated with fund boards' review and approval of its policies and procedures. Amortized over a three-year period, this would be an annual burden per fund of approximately 5.3 hours. We estimate that the total one-time burden for the initial documentation, and board approval of, written policies and procedures to provide for a fund's maintenance of qualifying coverage assets would be 15,744 hours.[43] We also estimate that each fund would incur a time cost of approximately $6,291, and a total initial time cost for all funds of approximately $9,912,816.[44] We estimate that there are no annual time costs associated with this collection of information.

Recordkeeping

A fund that enters solely into financial commitment transactions would also be required under the proposed rule to retain a written copy of the fund's board-approved policies and procedures regarding the maintenance of qualifying coverage assets. This requirement also applies to funds that enter into derivatives transactions. Accordingly, as discussed above for the recordkeeping burdens associated with asset segregation for derivatives transactions, we estimate a one-time burden (and no annual burden) of 1 hour per fund associated with maintaining a written copy of the fund's board-approved policies and procedures or, amortized over a three-year period, a burden of approximately 0.3 hours annually per fund. We therefore estimate that the total one-time burden for maintaining this record would be 984 hours.[45] We also estimate that each fund would incur a time cost of approximately $57, and a total initial time cost for all funds of approximately $56,088.[46]

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43 This estimate is based on the following calculation: 16 hours x 984 funds = 15,744 hours.

44 This estimate is based on the following calculations: 7.5 hours x $301 (hourly rate for a senior portfolio manager) = $2,258; 7.5 hours x $455.5 (blended hourly rate for assistant general counsel ($426) and chief compliance officer ($485)) = $3,416; 1 hour x $4,400 (hourly rate for a board of 8 directors) = $4,400. $2,258 + $3,416 + $4,400= $10,074; $10,074 x 984 funds = $9,912,816.

45 This estimate is based on the following calculation: 1 hour x 984 funds = 984 hours.

46 This estimate is based on the following calculation: 1 hour x $57 (hourly rate for a general clerk) = $57. $57 x 984 funds = $56,088.

In addition, a fund that relies on the proposed rule also would be subject to an ongoing requirement to maintain a written record reflecting the amount of each financial commitment obligation associated with each financial commitment transaction entered into by the fund and identifying the associated qualifying coverage assets, as determined by the fund at least once each business day, for a period of not less than five years (the first two years in an easily accessible place).[47] We estimate that each fund would incur an average annual burden of 50 hours to retain these records.[48] We therefore estimate that the total annual hour burden for maintaining these records would be 49,200 hours.[49] We also estimate that each fund would incur an annual time cost of approximately $3,600, and a total annual time cost for all funds of approximately $3,542,400.[50]

Estimated Total Burden

Amortized over a three-year time period, the hour burdens and time costs for collections of information associated with the asset segregation requirement for financial commitment transactions under proposed rule 18f-4, including the burdens associated with (a) identifying qualifying coverage assets; (b) documenting board-approved policies and procedures; and (c) maintaining required records, are estimated to result in an aggregate average annual hour burden of 163,016 hours and aggregate time costs of $18,210,888.[51]

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47 Proposed rule 18f-4(b)(3)(ii).

48 We assume for purposes of this estimate that funds would implement automated processes for creating a written record of their compliance with the qualifying coverage asset requirements and that a fund would enter into at least one financial commitment transaction per trading day. Based on 250 trading days per year, and assuming 0.1 hours per trading day spent by a general clerk and 0.1 hours per trading day spent by a senior computer operator, we estimate the annual time cost to be (0.1 x 250) = 25 hours per year per fund for each general clerk and senior computer operator.

49 This estimate is based on the following calculations: 50 hours x 984 funds = 49,200 hours.

50 This estimate is based on the following calculation: 25 hours x $57 (hourly rate for a general clerk) = $1,425; 25 hours x $87 (hourly rate for a senior computer operator) = $2,175. $1,425 + $2,175 = $3,600; $3,600 x 984 funds = $3,542,400.

51 These estimates are based on the following calculations: ((3 x 108,240 hours) (years 1, 2 and 3) + 15,744 (year 1) + 984 (year 1) + (3 x 49,200) (years 1, 2 and 3)) ÷ 3 = 163,016 hours; ((3 x $11,345,520) (years 1, 2 and 3) + ($9,912,816 (year 1)) + ($56,088 (year 1)) + (3 x $3,542,400) (years 1, 2 and 3)) ÷ 3 = $18,210,888.

D. Derivatives Risk Management Program

Proposed rule 18f-4 would require that a fund that engages in more than a limited amount of derivatives transactions, or that uses complex derivatives transactions, to adopt and implement a derivatives risk management program.[52] This risk management program would require a fund to adopt and implement policies and procedures reasonably designed to assess and manage the risks of the fund's derivatives transactions, reasonably segregate the functions associated with the program from the portfolio management function of the fund, and periodically review and update the program at least annually.[53] The proposed rule would also require a fund to designate a derivatives risk manager responsible for administering the program and require that the risk manager, no less frequently than quarterly, prepare a written report that describes the adequacy and effectiveness of the fund's risk management program.[54] A fund's board of directors must also (1) approve the fund's derivatives risk management program, including any material changes to the program; (2) approve the fund's designation of the fund's derivatives risk manager (who cannot be a portfolio manager of the fund); and (3) review, no less frequently than quarterly, the written report prepared by the fund's derivatives risk manager that describes the adequacy and effectiveness of the fund's risk management program.[55]

Staff estimates that approximately 1,676 funds[56] and no BDCs would be required to establish a derivatives risk management program. These funds would be subject to the collections of information described below with respect to the derivatives risk management program provision.

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[52] A derivatives risk management program would not be required if the fund complies with a portfolio limitation under which, immediately after entering into any derivatives transaction, the fund's aggregate exposure associated with the fund's derivatives transactions does not exceed 50% of the value of the fund's net assets, and the fund does not use "complex derivatives" (as defined in proposed rule 18f-4(c)(1)).

[53] *See* proposed rule 18f-4(a)(3)(i)(A) through (D).

[54] *See* proposed rule 18f-4(a)(3)(ii)(B) and (C).

[55] Proposed rule 18f-4(a)(3)(ii).

[56] This estimate is based on the following calculation: 11,973 funds x 14% = 1,676 funds.

Establishing a Derivatives Risk Management Program

We estimate that each fund would incur an average initial burden of 30 hours associated with establishing a derivatives risk management program, including (1) adopting and implementing (including documenting) policies and procedures reasonably designed to assess and manage the risks of the fund's derivatives transactions and designating a derivatives risk manager (24 hours); and (2) obtaining initial board approval of the derivatives risk management program and the designation of the fund's derivatives risk manager (6 hours). Amortized over a three-year period, this would be an annual burden per fund of 10 hours. Accordingly, we estimate that the total average annual initial burden for establishing a derivatives risk management program would be 50,280 hours.[57] We also estimate that each fund would incur an initial time cost of $27,346 in relation to this hour burden, for a total initial time cost for all funds of approximately $45,831,896.[58]

In addition to the initial burden, we estimate that each fund would incur an average annual burden of 38 hours associated with its derivatives risk management program, including that: (1) the fund review and update its risk management program at least annually (8 hours); (2) the derivatives risk manager prepare, on a quarterly basis, a written report that describes the adequacy and effectiveness of the fund's risk management program (24 hours[59]); and (3) the fund's board review, on a quarterly basis, the written report prepared by the fund's derivatives risk manager that describes the adequacy and effectiveness of the fund's risk management program, and approve any material changes to the derivatives risk management program (6

57 This estimate is based on the following calculation: 30 hours x 1,676 funds = 50,280 hours.

58 This estimate is based on the following calculations: 12 hours x $301 (hourly rate for a senior portfolio manager) = $3,612; 12 hours x $455.5 (blended hourly rate for assistant general counsel ($426) and chief compliance officer ($485) = $5,466; 4 hours x $4,400 (hourly rate for a board of 8 directors) = $17,600; 2 hours (for a fund attorney's time to prepare materials for the board's determinations) x $334 (hourly rate for a compliance attorney) = $668. $3,612 + $5,466 + $17,600 + $668 = $27,346; $27,346 x 1,676 funds = $45,831,896.

59 The estimate is based on the following calculation: 4 quarterly reports x 6 hours to prepare each written report = 24 hours.

hours). Accordingly, we estimate that the total average annual burden for establishing a derivatives risk management program would be 63,688 hours.[60] We also estimate that each fund would incur an annual time cost of $41,066, for a total annual time cost for all funds of approximately $68,826,616.[61]

Recordkeeping

Proposed rule 18f-4 would require a fund that adopts and implements a derivatives risk management program to maintain (1) a written copy of the policies and procedures adopted by the fund (as required in proposed rule 18f-4(a)(3)) that are in effect, or any time within the past five years were in effect, in an easily accessible place; (2) copies of any materials provided to the board of directors in connection with its approval of the derivatives risk management program, including any material changes to the program, and any written reports provided to the board relating to the derivatives risk management program, for at least five years after the end of the fiscal year in which the documents were provided (the first two years in an easily accessible place); and (3) records documenting the periodic reviews and updates required under proposed rule 18f-4(a)(3)(i)(D), for a period of not less than five years (the first two years in an easily accessible place) following each review or update.

We estimate that each fund would incur an annual average burden of 4 hours to retain these records.[62] We therefore estimate that the total annual burden for maintaining these records would be 6,704 hours.[63] We also estimate that each fund would incur an annual time cost of

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60 This estimate is based on the following calculation: 38 hours x 1,676 funds = 63,688 hours.

61 This estimate is based on the following calculations: Reviewing/updating the risk management program (8 hours): 4 hours x $301 (hourly rate for a senior portfolio manager) = $1,204; 4 hours x $455.5 (blended hourly rate for assistant general counsel ($426) and chief compliance officer ($485) = $1,822; Preparing quarterly reports by the derivatives risk manager (6 hours x 4 reports = 24 hours): 24 hours x $485 (hourly rate for chief compliance officer functioning as proposed derivatives risk manager) = $11,640; Reviewing quarterly reports by the fund’s board (1.5 hours x 4 reports = 6 hours): 6 hours x $4,400 (hourly rate for a board of 8 directors) = $26,400. $1,204 + $1,822 + $11,640 + $26,400 = 41,066; $41,066 x 1,676 funds = $68,826,616.

62 We estimate 2 hours spent by a general clerk and 2 hours spent by a senior computer operator.

63 This estimate is based on the following calculation: 4 hours x 1,676 funds = 6,704 hours.

approximately $288, and a total annual time cost for all funds of approximately $482,688 with respect to this hourly burden.[64]

Estimated Total Burden

Amortized over a three-year time period, the hour burdens and time costs for collections of information associated with the derivatives risk management program under proposed rule 18f-4, including the burdens associated with (a) establishing a derivatives risk management program; and (b) maintaining required records, are estimated to result in an aggregate average annual hour burden of 65,923 hours and aggregate time costs of $61,644,397.[65]

E. Estimated Total Burden

Amortized over a three-year time period, the hour burdens and time costs for collections of information associated with proposed rule 18f-4, including the burdens associated with (a) portfolio limitations for derivatives transactions; (b) asset segregation for derivatives transactions; (c) asset segregation for financial commitment transactions; and (d) derivatives risk management program, are estimated to result in an aggregate average annual hour burden of 1,059,755 hours and aggregate time costs of $171,141,630.[66]

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64 This estimate is based on the following calculation: 2 hours x $57 (hourly rate for a general clerk) = $114; 2 hours x $87 (hourly rate for a senior computer operator) = $174. $114 +$ 174 = $288; $288 x 1,676 funds = $482,688.

65 These estimates are based on the following calculations: (50,280 hours (year 1) + (2 x 63,688 hours) (years 2 and 3) + (3 x 6,704 hours) (years 1, 2 and 3)) ÷ 3 = 65,923 hours; ($45,831,896 (year 1) + (2 x $68,826,616) (years 2 and 3) + (3 x $482,688) (years 1, 2 and 3)) ÷ 3 = $61,644,397.

66 These estimates are based on the following calculations: (196,147 hours: portfolio limitations + 634,669 hours: asset segregation (derivatives) + 163,016 hours: asset segregation (financial commitment transactions) + 65,923 hours (risk management program) = 1,059,755 hours; ($20,386,028: portfolio limitations + $70,900,317: asset segregation (derivatives) + $18,210,888: asset segregation (financial commitment transactions) + $61,644,397 (risk management program) = $171,141,630.

13. Cost to Respondents

The cost burden is the cost associated with a fund board consulting its outside legal counsel with regard to the required board approvals. The cost burden does not include the hour burden discussed in Item 12.

We estimate that each fund would incur a one-time average external cost of $800 associated with a fund board consulting its outside legal counsel with regard to the required board approvals of the portfolio limitation.[67] We estimate that each fund would incur a one-time average external cost of $800 associated with a fund board consulting its outside legal counsel with regard to the required board approval of the policies and procedures for qualifying coverage assets for derivatives.[68] We also estimate that each fund would incur a one-time average external cost of $800 associated with a fund board consulting its outside legal counsel with regard to the required board approvals for policies and procedures for qualifying coverage assets for financial commitment transactions.[69] We estimate that each fund that is required to implement a derivatives risk management program would incur a one-time average external cost of $1,600 associated with a fund board consulting its outside legal counsel with regard to the required board approval for the program and the designation of the fund's derivatives risk manager.[70] In addition, we estimate that each fund would incur average annual external costs of $3,200 associated with a fund board's consulting its outside legal counsel with regard to quarterly reviews of the reports prepared by the fund's derivatives risk manager.[71] In sum, we estimate that each fund would incur an aggregate average one-time external cost of $4,000 and aggregate

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67 This estimate is based on the following calculation: 2 hours x $400 (hourly rate for outside legal services) = $800.

68 This estimate is based on the following calculation: 2 hours x $400 (hourly rate for outside legal services) = $800.

69 This estimate is based on the following calculation: 2 hours x $400 (hourly rate for outside legal services) = $800.

70 This estimate is based on the following calculation: 4 hours x $400 (hourly rate for outside legal services) = $1,600.

71 This estimate is based on the following calculation: 8 hours (2 hours x 4 quarterly reviews) x $400 (hourly rate for outside legal services) = $3,200.

average annual external costs of $3,200.[72] We estimate that all applicable funds would incur on average, in the aggregate, one-time external costs of $9,598,400 and annual external costs of $5,363,200.[73]

The staff estimates that rule 18f-4 does not impose any other material cost burdens on funds, apart from the costs and hour burdens discussed above. Although rule 18f-4 requires funds to maintain records for five years, these records may be maintained electronically and, even if maintained in hard copy, are unlikely to be voluminous. The staff has not estimated a capital cost in connection with the recordkeeping requirements because funds and their advisers would likely use existing recordkeeping systems to maintain the required records.

14. Costs to Federal Government

Proposed rule 18f-4 does not impose a cost to the federal government. Commission staff may, however, review records produced pursuant to the rule in order to assist the Commission in carrying out its examination and oversight program.

15. Changes in Burden

This is the first request for approval of the collection of information for this rule.

16. Information Collection Planned for Statistical Purposes

Not applicable.

17. Approval to Omit OMB Expiration Date

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

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72 These estimates are based on the following calculations: One-time costs: ($800: portfolio limitations + $800: asset segregation (derivatives) + $800: asset segregation (financial commitment transactions) + $1,600 (risk management program) = $4,000; Annual costs: ($3,200: risk management program).

73 These estimates are based on the following calculations: One-time costs: (($800: portfolio limitations x 3,831 funds) + ($800: asset segregation (derivatives) x 3,831 funds) + ($800: asset segregation (financial commitment transactions) x 984 funds) + ($1,600 (risk management program) x 1,676 funds) = $9,598,400; Annual costs: ($3,200: risk management program x 1,676 funds = $5,363,200).

18. Exceptions to Certification for Paperwork Reduction Act Submissions

The Commission is not seeking an exception to the certification statement.

B. COLLECTIONS OF INFORMATION EMPLOYING STATISTICAL METHODS

The collection of information will not employ statistical methods.