

SUPPORTING STATEMENT
for the Paperwork Reduction Act Information Collection Submission for
Rule 17a-4

A. JUSTIFICATION

1. Information Collection Necessity

All brokers and dealers in the ordinary course of their businesses need to maintain certain books and records reflecting, among other things, income and expenses, assets and liabilities, daily trading activity, and the status of customer and firm accounts. These books and records are, for the most part, standard and would be kept by any prudent individual engaging in a securities business.

The Commission is statutorily authorized by Sections 17(a)¹ and 23(a)² of the Securities Exchange Act of 1934 (“Exchange Act”) to promulgate rules and regulations regarding the maintenance and preservation of books and records of exchange members, brokers, and dealers (“broker-dealers”). Section 17(a)(1) provides in pertinent part:

“[all members of a national securities exchange and registered brokers and dealers] shall make and keep for prescribed periods such records...as the Commission, by rule, prescribes as necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the [Exchange Act].”

To standardize recordkeeping practices throughout the industry, the Commission, in 1940, adopted Rules 17a-3 and 17a-4 (one of the “Books and Records Rules”),³ which codified and specified minimum standards with respect to business records that broker-dealers must create and maintain. Rule 17a-3 requires exchange members, brokers and dealers to make and keep current certain records relating to a broker’s or dealer’s financial condition and operations. Rule 17a-4 requires broker-dealers to preserve, for prescribed periods of time, certain records required to be created under Rule 17a-3 and certain other Commission rules. In addition, Rule 17a-4 requires broker-dealers to preserve other records that may be created or received by the broker-dealer in the ordinary course of its business for prescribed periods of time.

To aggregate the entire burden of Rule 17a-4 into one information collection (and OMB control number), the Commission is moving the annual burden hours for paragraph (b)(11) of Rule 17a-4 into this information collection.⁴

¹ 15 U.S.C. 78q(a).

² 15 U.S.C. 78w(a).

³ 17 CFR 240.17a-3 and 17 CFR 240.17a-4.

⁴ The burden estimate for paragraph (b)(11) of Rule 17a-4 was in a separate information collection (OMB control number 3235-0506) with paragraph (a)(16) of Rule 17a-3. Paragraph (a)(16) of Rule 17a-3 is being moved to the information collection for Rule 17a-3.

2. Information Collection Purpose and Use

The purpose of requiring that broker-dealers maintain the records specified in Rule 17a-4 is to help ensure that examiners and other representatives of the Commission, State securities regulatory authorities, and the SROs have access to the information and documents necessary to determine whether broker-dealers are in compliance with the Commission's antifraud and anti-manipulation rules, financial responsibility program, and other Commission, SRO, and state laws, rules, and regulations. Without Rule 17a-4, it would be impossible for the Commission to determine whether a broker-dealer that chose not to preserve records was in compliance with these rules. Such a situation would not be in the public interest and would be detrimental to investors and the financial community as a whole.

3. Consideration Given to Information Technology

Rule 17a-4 specifically allows brokers and dealers to use electronic storage media to comply with the record-keeping requirements under the Securities and Exchange Act of 1934. In fact, because it simply sets minimum standards for the electronic storage media employed, Rule 17a-4 does not limit broker-dealers to using forms of electronic storage which may become obsolete as new technology is developed. The Commission believes that improvements in telecommunications and data processing technology may reduce any burdens that result from Rule 17a-4.

4. Duplication

There is no duplication.

5. Effects on Small Entities

The number and complexity of records required to be preserved by Rule 17a-4 vary proportionately with the volume and complexity of the broker-dealer's business. Further, broker-dealers may choose which media (hard-copy, microfiche, electronic storage, etc.) is most appropriate given their size and the type of business they do. The books and records required under Rule 17a-4 are normally retained by small broker-dealers.

6. Consequences of Not Conducting Collection

Rule 17a-4 is a record preservation rule. Without Rule 17a-4, it would be impossible for the Commission to determine whether a broker-dealer that chose not to preserve records was in compliance with the Commission's antifraud and anti-manipulation rules, financial responsibility program, and other Commission, SRO, and State laws, rules, and regulations. Such a situation would not be in the public interest and would be detrimental to investors and the financial community as a whole.

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

Certain provisions of Rule 17a-4 require respondents to retain records for more than three years. Specifically, Rule 17a-4(a) requires broker-dealers to preserve for a period of not less than six years:

1. Purchase and sales blotters, securities and cash receipts, and disbursements blotters;
2. Ledgers of a broker-dealer's assets, liabilities, income and expense, and capital accounts;
3. Customer account ledgers;
4. Securities position reports;
5. Lists of office employees able to explain records to examiners; and
6. A record of persons responsible for establishing policies and procedures designed to ensure that the broker-dealer is compliant with applicable rules and regulations.

After the closing of any customer's account, broker-dealers must preserve for at least six years any account cards or records which relate to the terms and conditions of opening and maintaining the account. Broker-dealers are required to maintain and preserve in an easily accessible place:

1. Employment records of associated persons until at least three years after the employment has terminated;
2. Processed fingerprint cards and other related information until at least three years after the termination of employment or association;
3. All records required pursuant to paragraph (a)(15) of Rule 17a-3 for the life of the enterprise;
4. All account record information required pursuant to Rule 17a-3(a)(17) until at least six years after the earlier of the date the account was closed or the date on which the information was replaced or updated; and
5. Each compliance, supervisory, and procedures manual, including any updates, modifications, and revisions to the manual, describing the policies and practices of the member, broker, or dealer with respect to compliance with applicable laws and rules, and supervision of the activities of each natural person associated with the member, broker, or dealer until three years after the termination of the use of the manual.

In addition, Rule 17a-4(d) requires that a broker-dealer maintain specified organizational documents for the life of the enterprise and any successor enterprise.

These extended retention periods are necessary with respect to the records itemized above in order to provide regulators with sufficient time to conduct comprehensive inspections and investigations. Due to budget constraints, regulators only examine broker-dealers and office locations periodically. Further, certain of these documents do not become obsolete (*e.g.*, organizational documents).

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

The Commission did not provide any payment or gift to respondents.

10. Confidentiality

The records required by Rule 17a-4 are available only to the examination staffs of the Commission, State regulatory authorities, and the SROs. Subject to the provisions of the Freedom of Information Act, 5 U.S.C. § 552 (“FOIA”) and the Commission’s rules thereunder (17 CFR 200.80(b)(4)(iii)), the Commission generally does not publish or make available information contained in reports, summaries, analyses, letters, or memoranda arising out of, in anticipation of, or in connection with an examination or inspection of the books and records of any person or any other investigation.

11. Sensitive Questions

No questions of a sensitive nature are asked. The information collection does not collect any Personally Identifiable Information (“PII”).

12. Information Collection Burden

The Commission estimates that, on average, each broker-dealer spends 254 hours each year to ensure that it is in compliance with Rule 17a-4 and to produce required records promptly at an office when so required.

To aggregate the entire burden of Rule 17a-4 into one information collection (and OMB control number), the Commission is moving the annual burden hours for paragraph (b)(11) of Rule 17a-4 into this information collection. Paragraph (b)(11) of Rule 17a-4 requires any broker-dealer that sponsors an internal broker-dealer system to maintain certain records relating to such system for at least three years, the first two years in an easily accessible place.⁵ The Commission estimates that paragraph (b)(11) of Rule 17a-4 imposes an annual burden of 3 hours per year to maintain the requisite records. The Commission estimates that there are approximately 150 internal broker-dealer systems,⁶ resulting in an annual recordkeeping burden of 450 hours.⁷

⁵ An internal broker-dealer system is any facility that provides a mechanism for collecting, receiving, disseminating, or displaying system orders and facilitating agreement to the basic terms of a purchase or sale of a security between a customer and the sponsor, but excludes a national securities exchange, an exchange exempt from registration based on limited volume, and an alternative trading system. *See* 17 C.F.R. 240.17a-3(a)(16)(ii)(A). Because an internal broker-dealer system is not included in the definition of an exchange, it is regulated under the broker-dealer regulatory scheme.

⁶ The Commission believes that most over-the-counter (“OTC”) market makers maintain an internal broker-dealer system. In 2010, the Commission estimated that there are approximately 150 OTC market makers responsible for more than 1% of the trading volume in an exchange-traded security. *See* Commission, Supporting Statement for the Paperwork Reduction Act Information Collection Submission for Rule 602 of Regulation NMS (Nov. 7, 2013), *available at* <http://www.reginfo.gov/public/do/DownloadDocument?documentID=431473&version=1>.

⁷ 3 hours x 150 internal broker-dealer systems = 450 hours.

Therefore, the Commission estimates that compliance with Rule 17a-4 requires 1,042,866 hours each year $((4,104 \text{ broker-dealers} \times 254 \text{ hours}) + (150 \text{ broker-dealers} \times 3 \text{ hours}))$.⁸ These burdens are recordkeeping burdens.

The Commission believes that requirements resulting from Rule 17a-4 would be performed by individuals in a broker-dealer's compliance department. A Compliance Clerk earns an average of \$65 per hour,⁹ resulting in a total internal cost of compliance of approximately \$67.8 million $((1,042,416 \times \$65) + (450 \times \$65))$.

13. Costs to Respondents

Based on conversations with members of the securities industry and the Commission's experience in the area, we estimate that the average broker-dealer spends approximately \$5,000 each year to store documents required to be retained under Rule 17a-4. Costs include the cost of physical space, computer hardware and software, etc., which vary widely depending on the size of the broker-dealer and the type of storage media employed. The Commission estimates that the annual reporting and recordkeeping cost burden is \$20,520,000. This cost is calculated by the number of active, registered broker-dealers multiplied by the recordkeeping cost for each respondent $(4,104 \text{ active, registered broker-dealers} \times \$5,000)$. This is a recordkeeping cost.

14. Costs to the Federal Government

The federal government does not incur a cost for this collection of information since it relates to a recordkeeping burden for the respondents.

15. Changes in Burden

The annual recordkeeping burden and cost decreased due to the decline in the number of respondents (active broker-dealers) to 4,104.

16. Information Collection Planned for Statistical Purposes

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

17. Approval to Omit OMB Expiration Date

The Commission is not seeking approval to omit the expiration date.

18. Exceptions to Certification for Paperwork Reduction Act Submissions

This collection complies with the requirements in 5 CFR 1320.9.

⁸ There were 4,104 broker-dealers as of April 1, 2016.

⁹ This figure is based on SIFMA's *Office Salaries in the Securities Industry 2016*, modified by Commission staff to account for an 1,800-hour work-year multiplied by 2.93 to account for bonuses, firm size, employee benefits, and overhead.

B. COLLECTIONS OF INFORMATION EMPLOYING STATISTICAL METHODS

This collection does not involve statistical methods.