

SUPPORTING STATEMENT

For the Paperwork Reduction Act Information Collection Submission for Rule 203A-2(e)

A. JUSTIFICATION

1. Necessity for the Information Collection

Section 203A of the Investment Advisers Act of 1940 (“Advisers Act” or “Act”) prohibits certain advisers from registering with the Securities and Exchange Commission (the “Commission”) under the Act. In general, a small adviser with less than \$25 million in assets under management that is regulated or required to be regulated as an adviser in the state where it maintains its principal office and place of business, and a mid-sized adviser with between \$25 million and \$100 million in assets under management that is required to be registered as an adviser in the state where it maintains its principal office and place of business and that is subject to examination by its state securities commission, are not eligible to register with the Commission.¹ A mid-sized adviser that otherwise would be prohibited may register with the Commission if it would be required to register with 15 or more states.² A mid-sized adviser also will be required to register with the Commission if it is an adviser to a registered investment company or business development company under the Investment Company Act.³ Section 203A(c) of the Advisers Act also authorizes the Commission to exempt an adviser from the prohibition on Commission registration if the prohibition would be “unfair, a burden on interstate

¹ 15 U.S.C. 80b-3a(a).

² *See id.*

³ *See id.*

commerce, or otherwise inconsistent with the purposes” of section 203A of the Act.⁴ Under this authority, the Commission adopted rule 203A-2 in 1997 to provide certain types of advisers with exemptions from the prohibition on registration. Rule 203A-2 was amended by the Commission in 2002 when it adopted an exemption for Internet advisers,⁵ and was amended again in 2011 when, among other changes, the internet adviser exemption was redesignated as subsection (e) of Rule 203A-2.⁶

Rule 203A-2(e) exempts from the prohibition on Commission registration an Internet investment adviser who (1) provides investment advice to all of its clients exclusively through computer software-based models or applications termed under the rule as “interactive websites”⁷ and (2) maintains in an easily accessible place, for a period of not less than five years from the filing of a Form ADV,⁸ a record demonstrating that the adviser provides investment advice to its clients exclusively through an interactive

⁴ 15 U.S.C. 80b-3a(c).

⁵ See Exemption for Certain Investment Advisers Operating Through the Internet, Investment Advisers Act Release No. 2091 (December 12, 2002) (67 F.R. 77620 (Dec. 18, 2002)).

⁶ See Rules Implementing Amendments to the Investment Advisers Act of 1940, Investment Advisers Act Release No. 3221 (June 22, 2011) (76 FR 42950 (July 19, 2011)). The Commission did not make substantive amendments to the internet adviser exemption as part of this rulemaking.

Other exempted advisers under Rule 203A-2 include: (1) pension consultants that provide investment advice to employee benefit plans with respect to assets of plans having an aggregate value of at least \$200 million during the adviser’s last fiscal year; (2) an adviser that controls, is controlled by, or is under common control with a Commission-registered adviser if the two advisers have the same principal office and place of business; (3) a newly formed adviser with a reasonable expectation that it would be eligible for Commission registration within 120 days after its registration has become effective with the Commission; and (4) an adviser required to register with the securities authorities in at least 15 states. 17 CFR 275.203A-2.

⁷ 17 CFR 275.203A-2(e). Included in rule 203A-2(e) is a limited exception to the interactive website requirement which allows these advisers to provide investment advice to fewer than 15 clients through other means on an annual basis. 17 CFR 275.203A-2(e)(1)(i). The rule also precludes advisers in a control relationship with an SEC-registered Internet adviser from registering with the Commission under the common control exemption provided by rule 203A-2(b) (17 CFR 275.203A-2(b)).

17 CFR 275.203A-2(e)(1)(iii).

⁸ The five-year record retention period is a similar recordkeeping retention period as imposed on all SEC-registered advisers under rule 204-2 of the Adviser Act. See rule 204-2 (17 CFR 275.204-2).

website in accordance with the rule. Rule 203A-2(e)'s record maintenance requirement is a "collection of information" for Paperwork Reduction Act ("PRA") purposes. The title for the collection of information is "Exemption for Certain Investment Advisers Operating Through the Internet (Rule 203A-2(e))". This collection of information is necessary for use by the Commission staff in its examination and oversight program. The collection of information for rule 203A-2(e) is currently approved under OMB control number 3235-0559 (expires July 31, 2017).

Respondents to this collection of information are advisers who provide investment advice through interactive websites and who rely on the exemption to register with the Commission. Providing this information is mandatory in qualifying for and maintaining Commission registration eligibility under rule 203A-2(e). Responses provided to the Commission in the context of its examination and oversight program are generally kept confidential under section 210(b) of the Advisers Act.⁹

2. Purpose and Use of the Information Collection

The information collected under rule 203A-2(e) permits the Commission's examination staff to determine an advisers' eligibility for registration with the Commission under this exemptive rule.

3. Consideration Given to Information Technology

An investment adviser registering or registered with the Commission under rule 203A-2(e) must maintain, in an easily accessible place, for five years from the filing of a Form ADV, a record that demonstrates that the adviser provides investment advice to its

⁹ 15 U.S.C. 80b-10(b).

clients exclusively through an interactive website as defined under the rule.¹⁰ Advisers are permitted to meet the recordkeeping obligation under the rule micrographically or electronically, and their storage of this required record in such media is governed by Advisers Act rule 204-2(g).¹¹ The rule does not require the reporting of any information to, or the filing of any documents with, the Commission, so the Commission's use of computer technology in its various electronic filing systems will be of no effect.

4. Duplication

The recordkeeping requirement of rule 203A-2(e) is not duplicated elsewhere for investment advisers that must comply with this collection requirement.

5. Effect on Small Entities

The collection of information requirements are the same for all investment advisers registering or registered with the Commission, including those that are small entities. Under section 203A, advisers with assets under management of less than \$100 million generally will not be eligible to register with the Commission. However, under rule 203A-2(e), these advisers are permitted to register with the Commission if they meet the conditions of the rule. The recordkeeping requirement under the rule affects small advisers and larger advisers similarly, because the required information is about the adviser maintaining the records and about its business, which should be readily available to any adviser regardless of size. It would defeat the purpose of the rule to exempt small

¹⁰ 17 CFR 275.203A-2(e).

¹¹ 17 CFR 275.204-2(g). Rule 204-2(g) requires that the record be arranged and indexed in a way that permits easy location, access, and retrieval of any particular record, and that the micrographic or electronic duplicate of the record be separately stored for the time required by rule 204-2 to preserve the original record. See 17 CFR 275.204-2(g)(2). An investment adviser must establish and maintain procedures to keep the required records so as to reasonably safeguard the records from loss, alteration, or destruction; to limit access to the records to properly authorized personnel and the Commission; and to reasonably ensure that any reproduction of a non-electronic original record is complete, true, and legible when retrieved. See 17 CFR 275.204-2(g)(3).

entities from these requirements.

6. Consequences of Not Conducting Collection

An adviser registering with the Commission under rule 203A-2(e) must maintain a record, for a period of not less than five years from the filing of a Form ADV, showing that substantially all of its advisory business has been conducted through an interactive website. 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 period between examinations. If the required information is not collected, the Commission's examiners would not be able to verify that an investment adviser's reliance on rule 203A-2(e) in registering with the Commission was appropriate.

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

Rule 203A-2(e) includes a recordkeeping provision under which an adviser relying on the rule to register with the Commission would be required to maintain certain information, specified more fully in Item 1 above, for five years. Although this period exceeds the three-year guideline for most kinds of records under 5 CFR 1320.5(d)(2)(iv), the long-term retention of these records is designed to contribute to the effectiveness of the Commission's examination and inspection program, and is necessary for the Commission's inspection program to determine compliance with the Advisers Act, including an adviser's continued eligibility to register with the Commission. 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 period between examinations.

8. Consultation Outside the Agency

The Commission and the staff of the Division of Investment Management

participate in an ongoing dialogue with representatives of the investment adviser 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 paperwork burdens confronting the industry.

In addition, the Commission requested public comment on the information collection requirements in rule 203A-2(e) before it submitted this request for extension and approval to the Office of Management and Budget. The Commission received no comments in response to its request.

9. Payment or Gift

Not applicable.

10. Confidentiality

Responses to the recordkeeping responses required under rule 203A-2(e) in the context of the Commission's examination and oversight program are generally kept confidential.¹²

11. Sensitive Questions

No PII collected/Not applicable.

12. Burden of Information Collection

Rule 203A-2(e) requires advisers registering with the Commission under the exemption to maintain a record demonstrating that the adviser's advisory business has been conducted through an interactive website in accordance with the rule. Although most advisers registering under the rule usually generate the necessary records in the ordinary conduct of their Internet advisory business, the recordkeeping requirement of

¹² See Section 210(b) of the Advisers Act. 15 U.S.C. 80b-10b.

rule 203A-2(e) nonetheless may impose a small additional burden on these advisers. We continue to estimate that this recordkeeping burden should not exceed an average of four (4) hours annually per adviser.¹³

The number of respondents has increased from the estimated 74 advisers to 144 investment advisers.¹⁴ Accordingly, the total recordkeeping burden hours for all rule 203A-2(e) advisers has increased from 296 hours to 576 hours.¹⁵

The Commission estimates that the total cost to each Internet adviser to comply with the recordkeeping provision of rule 203A-2(e) would be approximately \$1,360,¹⁶ such that the total cost for the 144 advisers relying on this exemption at this time would be \$195,840.¹⁷

13. Cost to Respondents

Excluding the burden hours identified in item 12, the collection of information requirement for rule 203A-2(e) is not expected to impose additional non-labor or capital costs. The Commission anticipates that most advisers registering under the rule would

¹³ The adviser would need only to demonstrate that fewer than 15 of its clients obtain investment advice from the firm through means other than the interactive website. Internet advisers that conduct their business exclusively through interactive websites would likely need to spend very little time documenting their compliance with the condition. An adviser that also meets in person with some clients or communicates with them through other means may need to spend more time.

¹⁴ This estimate is based on information reported by advisers through the Investment Adviser Registration Depository (“IARD”). Based on IARD data as of October 31, 2016, of the approximately 12,240 SEC-registered advisers, 144 checked Item 2.A(11) of Part 1A of Form ADV to indicate their basis for SEC registration under the Internet advisers rule.

¹⁵ Four (4) hours x 144 advisers = 576 hours.

¹⁶ Four (4) hours x \$340 = \$1,360. The Commission estimated this figure by multiplying the burden hours to comply with rule 203A-2(e)’s recordkeeping requirements (4 hours) by an average hourly compensation rate of \$340. The compensation rate used is the rate for a Sr. Operations Manager in the Securities Industry and Financial Markets Association’s Report on Management & Professional Earnings in the Securities Industry 2013 and is modified to account for an 1,800-hour work-year and inflation and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

¹⁷ Four (4) hours x \$340 = \$1,360 x 144 advisers = \$195,840.

generate the necessary records in the ordinary conduct of their advisory businesses.

14. Cost to the Federal Government

There are no costs to the federal government directly attributable to rule 203A-2(e).

15. Change in Burden

The revised burden for rule 203A-2(e) results from an increase in the number of advisers relying on the rule for Commission registration eligibility. The annual recordkeeping burden under the rule previously was 296 hours, or four hours per adviser for a total of 74 advisers. Adjusting this number for the seventy additional advisers relying on the rule, the annual recordkeeping burden is revised from 296 hours to 576 hours.¹⁸

16. Information Collection Planned for Statistical Purposes

Not applicable.

17. Approval to Omit OMB Expiration Date

Not applicable.

18. Exceptions to Certification Statement for Paperwork Reduction Act

Submission

Not applicable.

B. COLLECTIONS OF INFORMATION EMPLOYING STATISTICAL METHODS

Not applicable.

¹⁸ Four (4) hours x 144 advisers = 576 hours.