

SUPPORTING STATEMENT
For the Paperwork Reduction Act Information Collection Submission for
Rule 17f-2

A. JUSTIFICATION

1. Necessity for the Information Collection

Rule 17f-2 (17 CFR 270.17f-2), entitled “Custody of Investments by Registered Management Investment Company,” was adopted in 1940 under section 17(f) of the Investment Company Act of 1940 (15 U.S.C. 80a-17(f)) (the “Act”), and was last amended materially in 1947. Rule 17f-2 establishes safeguards for arrangements in which a registered management investment company ("fund") is deemed to maintain custody of its own assets, such as when the fund maintains its assets in a facility that provides safekeeping but not custodial services.¹ The rule includes several recordkeeping or reporting requirements. The fund's directors must prepare a resolution designating not more than five fund officers or responsible employees who may have access to the fund's assets. The designated access persons (two or more of whom must act jointly when handling fund assets) must prepare a written notation providing certain information about each deposit or withdrawal of fund assets, and must transmit the notation to another officer or director designated by the directors. An independent public accountant must verify the fund's assets three times each year, and two of those examinations must be unscheduled.²

2. Purpose and Use of the Information Collection

Rule 17f-2's requirement that directors designate access persons is intended to ensure that directors evaluate the trustworthiness of insiders who handle fund assets. The requirements that access persons act jointly in handling fund assets, prepare a written notation of each transaction,

¹ The rule generally requires all assets to be deposited in the safekeeping of a "bank or other company whose functions and physical facilities are supervised by Federal or State authority." The fund's securities must be physically segregated at all times from the securities of any other person.

² The accountant must transmit to the Commission promptly after each examination a certificate describing the examination on Form N-17f-2. The third (scheduled) examination may coincide with the annual verification required for every fund by section 30(g) of the Act (15 U.S.C. 80a-29(g)).

and transmit the notation to another designated person are intended to reduce the risk of misappropriation of fund assets by access persons, and to ensure that adequate records are prepared, reviewed by a responsible third person, and available for examination by the Commission. The requirement that auditors verify fund assets without notice twice each year is intended to provide an additional deterrent to the misappropriation of fund assets and to detect any irregularities. Less frequent examinations by a fund's accountants could impair the ability of the Commission's examination staff to ascertain the fund's compliance with the rule.

3. Consideration Given to Information Technology

The Commission's Electronic Data Gathering, Analysis and Retrieval System ("EDGAR") provides for the automated filing, processing, and dissemination of full disclosure filings. The automation provides for speed, accuracy and public availability of information, generating benefits to investors and financial markets. The Electronic Signatures in Global and National Commerce Act³ and the conforming amendments to recordkeeping rules under the Investment Company Act permit funds to maintain records electronically. The notations required under rule 17f-2 normally would be prepared and maintained on paper because they are required to appear on consecutively numbered forms.

4. Duplication

The Commission evaluates reporting requirements for duplication periodically, and whenever a rule or a change in a rule is proposed. Rule 17f-2 does not require recordkeeping or reporting of information available elsewhere. The scheduled verification of the fund's assets required each year by rule 17f-2 may be combined with the annual verification of every fund's assets required by section 30(g) of the Act (15 U.S.C. 80a-29(g)).

³ P.L. 106-229, 114 Stat. 464 (June 30, 2000).

5. Effect on Small Entities

Rule 17f-2 potentially benefits smaller funds by permitting them to use self-custody procedures that may be simpler or less expensive than the bank custody arrangements used by most funds. The Commission believes that the rule's safeguards are necessary to protect fund assets from potential misappropriation by fund insiders.

6. Consequences of Not Conducting Collection

The frequency with which the fund prepares notations of transactions under rule 17f-2 depends on circumstances within the control of the fund. Elimination of one or both of the twice-annual unscheduled verifications of fund assets under the rule might lessen the deterrent and detection value of these verifications and increase the risk of misappropriation of fund assets. In addition, less frequent collection under rule 17f-2 could inhibit the dissemination of timely information to the public and could impair the ability of the Commission's examination staff to ascertain compliance with the rule.

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

None.

8. Consultation Outside the Agency

The Commission requested public comment on the collection of information requirements in rule 17f-2 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.

The Commission and staff of the Division of Investment Management participate in an ongoing dialogue with representatives of the fund industry through public conferences, meetings, and informal exchanges. These forums provide the Commission and the staff means of ascertaining and acting upon paperwork burdens confronting the industry.

9. Payment or Gift

Not applicable.

10. Confidentiality

Not applicable.

11. Sensitive Questions

No information of a sensitive nature, including social security numbers, will be required under this collection of information. The information collection does not collect personally identifiable information (PII). The agency has determined that a system of records notice (SORN) and privacy impact assessment (PIA) are not required in connection with the collection of information.

12. Burden of Information Collection

The estimate of average burden hours is made solely for the purposes of the Paperwork Reduction Act, and is not derived from a comprehensive or even a representative survey or study of the costs of Commission rules and forms.

The Commission staff estimates that each fund makes 974 responses and spends an average of 252 hours annually in complying with the rule's requirements.⁴ Commission staff estimates that on an annual basis it takes: (i) 0.5 hours of fund accounting personnel at a total cost of \$102 to draft director resolutions;⁵ (ii) 0.5 hours of the fund's board of directors at a total cost of \$2,233 to adopt the resolution;⁶ (iii) 244 hours for the fund's accounting personnel at a

⁴ The 974 responses are: 1 (one) response to draft and adopt the resolution and 973 notations. Estimates of the number of hours are based on conversations with individuals in the fund industry. The actual number of hours may vary significantly depending on individual fund assets.

⁵ This estimate is based on the following calculation: 0.5 (burden hours per fund) x \$204 (senior accountant's hourly rate) = \$102. Unless otherwise indicated, the hourly wage figures used herein are from the Securities Industry and Financial Markets Association's Management & Professional Earnings in the Securities Industry 2013, modified by Commission staff to account for an 1800-hour work-year and inflation, and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

⁶ The estimate for the cost of board time as a whole is derived from estimates made by the staff regarding

total cost of \$65,745 to prepare written notations of transactions;⁷ and (iv) 7 hours for the fund's accounting personnel at a total cost of \$1,428 to assist the independent public accountants when they perform verifications of fund assets.⁸ Commission staff estimates that approximately 206 funds file Form N-17f-2 each year.⁹ Thus, the total annual hour burden for rule 17f-2 is estimated to be 51,912 hours.¹⁰ Based on the total costs per fund listed above, the total cost of rule 17f-2's collection of information requirements is estimated to be approximately \$13.5 million.¹¹

13. Cost to Respondents

Funds relying on rule 17f-2 generally use outside counsel to assist in drafting directors' resolutions. Commission staff estimates the annual cost of these services per fund is \$400.¹² In addition, rule 17f-2 requires an independent public accountant to verify the fund's assets three times each year and to prepare and file with the Commission a certificate of examination each

typical board size and compensation that is based on information received from fund representatives and publicly available sources.

⁷ Respondents estimated that each fund makes 974 responses on an annual basis and spends a total of 0.25 hours per response. The fund personnel involved are Accounts Payable Manager (\$192 hourly rate), Operations Manager (\$345 hourly rate) and Accounting Manager (\$274 hourly rate). The average hourly rate of these personnel is \$270. The estimated cost of preparing notations is based on the following calculation: $974 \times 0.25 \times \$270 = \$65,745$.

⁸ This estimate is based on the following calculation: $7 \times \$204$ (senior accountant's hourly rate) = \$1,428.

⁹ On average, each year approximately 206 funds filed Form N-17f-2 with the Commission during calendar years 2015-2017.

¹⁰ This estimate is based on the following calculation: 206 (funds) \times 252 (total annual hourly burden per fund) = 51,912 hours for rule. The annual burden for rule 17f-2 does not include time spent preparing Form N-17f-2. The burden for Form N-17f-2 is included in a separate collection of information.

¹¹ This estimate is based on the following calculation: $\$65,745$ (total annual cost per fund) \times 206 funds = \$13,543,470.

¹² This estimate is based on the following calculation: 1 (hour) \times $\$400$ (attorney's hourly billing rate) = \$400.

time it performs the verification. Commission staff estimates this cost per fund is \$35,700.¹³ Thus the total estimated annual cost to the industry is approximately \$7.9 million.¹⁴

14. Cost to the Federal Government

The federal government does not incur any direct costs in connection with the requirements of rule 17f-2.

15. Changes in Burden

The estimated total annual hour burden for rule 17f-2 has increased from 47,376 hours to 51,912 hours. The estimated total annual cost has increased from approximately \$7 million to approximately \$7.9 million. The increase in total hours and cost is mainly attributable to an increase in the number of funds relying on rule 17f-2. The increase in cost is also partly attributable to an increase in estimated salaries.

16. Information Collection Planned for Statistical Purposes

Not applicable.

17. Approval to Omit OMB Expiration Date

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

18. Exceptions to Certification Statement for Paperwork Reduction Act Submission

Not applicable.

B. COLLECTION OF INFORMATION EMPLOYING STATISTICAL METHODS

Not applicable.

¹³ This estimate is based on the following calculation: 175 (hours to verify fund assets) x \$204 (senior accountant's hourly billing rate) = \$35,700; 12 (hours to prepare certificates of examination) x \$204 (senior accountant's hourly billing rate) = \$2,448; \$35,700 + \$2,448 = \$38,148.

¹⁴ This estimate is based on the following calculation: 206 funds x (\$38,148 + \$400) = \$7,940,888.