

**SUPPORTING STATEMENT
FOR PAPERWORK REDUCTION ACT SUBMISSION PROPOSAL TO AMEND RULE
204-2 UNDER THE ADVISERS ACT**

A. JUSTIFICATION

1. Necessity for the Information Collection

On April 18, 2018, the Securities and Exchange Commission (the “Commission” or “SEC”) issued a release proposing, among other things, to amend Form ADV to add a new Part 3, which would require certain registered investment advisers to provide a brief relationship summary to retail investors to inform them about certain aspects of the relationships and services the firm offers (the “relationship summary”). The relationship summary would be subject to Commission filing and recordkeeping requirements, and the Commission proposed amendments to rule 204-2 under the Investment Advisers Act of 1940 (the “Advisers Act”).¹ The proposed amendments to rule 204-2 would require registered advisers to retain copies of each relationship summary. Under the proposed amendments to the rule, investment advisers would also be required to maintain each amendment to the relationship summary as well as to make and preserve a record of dates that each relationship summary and each amendment was delivered to any client or to any prospective client who subsequently becomes a client, as well as to any retail investor before such retail investor opens an account. These records would be required to be maintained in the same manner, and for the same period of time, as other books and records required to be maintained under rule 204-2(a).

Section 204 of the Advisers Act provides that investment advisers required to register with the Commission must make and keep certain records for prescribed periods, and make and

¹ 15 U.S.C 80b-4.

disseminate certain reports. Advisers Act rule 204-2 sets forth mandatory requirements for maintaining and preserving specified books and records.² The records that an adviser must keep in accordance with rule 204-2 must generally be retained for not less than five years.³ These requirements constitute a mandatory “collection of information,” within the meaning of the Paperwork Reduction Act. The collection of information under rule 204-2 is necessary for the Commission staff to use in its examination and oversight program. The collection has been previously approved and subsequently extended under Office of Management and Budget (“OMB”) control number 3235-0278 (expiring March 31, 2020), and it is found at 17 CFR 275.204-2. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid OMB number.

2. Purpose and Use of the Information Collection

The proposed amendments to rule 204-2 would require registered advisers to retain copies of each relationship summary. Investment advisers would also be required to maintain each amendment to the relationship summary as well as to make and preserve a record of dates that each relationship summary and each amendment was delivered to any client or to any prospective client who subsequently becomes a client, as well as to any retail investor before such retail investor opens an account. The purpose of the information collection in rule 204-2 is to assist the Commission’s examination and oversight program in determining compliance with the Advisers Act and corresponding rules by allowing regulators to access the relationship summary during an examination. Requiring maintenance of the relationship summary as part of

² 17 CFR 275.204-2.

³ See rule 204-2(e) (17 CFR 275.204-2(e)). The standard retention period required for books and records under rule 204-2 is five years, in an easily accessible place, the first two years in an appropriate office of the investment adviser.

rule 204-2 would facilitate the Commission's ability to inspect for and enforce compliance with firms' obligations with respect to Form CRS.

The respondents to the rule are investment advisers registered with the Commission. The likely respondents for the proposed amendments to the rule would be the investment advisers registered with the Commission that would be required to prepare and deliver a relationship summary per proposed new rule 204-5 and amendments to Form ADV under the Advisers Act. Responses provided to the Commission in the context of its examination and oversight program are generally kept confidential.⁴ This collection of information is found at 17 CFR 275.204-2 and is mandatory.

3. Consideration Given to Information Technology

The Commission's use of computer technology in connection with this information collection, which has been previously approved by OMB, would not change. The Commission currently permits advisers to maintain records required by the rule through electronic media.⁵

4. Duplication

The collection of information requirements of the rule, including the proposed amendments, are not duplicated elsewhere.

5. Effect on Small Entities

The requirements of the rule are the same for all investment advisers registered with the Commission, including those that are small entities. The requirements of the proposed amendments to rule 204-2 would not distinguish between small entities and other investment

⁴ See section 210(b) of the Advisers Act [15 U.S.C. 80b-10(b)].

⁵ See Electronic Recordkeeping by Investment Companies and Investment Advisers, Investment Advisers Act Release No. 1945 (May 24, 2001) 66 FR 29224 (May 30, 2001).

advisers. OMB has previously approved the effect of this collection on all investment advisers in general, including advisers that are small entities. Moreover, it would defeat the purpose of the rule to exempt small entities from these requirements. 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

Less frequent information collection would be incompatible with the objectives of the rule and could hinder the Commission's oversight and examination program for investment advisers and thereby reduce the protection to investors.

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

The collection requirements under rule 204-2 generally require advisers to maintain documents for five years, and in some cases longer.⁶ The retention period would not be affected by the proposed amendments to the rule. Although this period exceeds the three-year guideline for most kinds of records under 5 CFR 1320.5(d)(2)(iv), OMB has previously approved the collection with this retention period. The retention periods in rule 204-2 are warranted because the recordkeeping requirements in rule 204-2 of the Advisers Act are designed to contribute 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.

8. Consultation Outside the Agency

⁶ See *supra* note 3.

In its release proposing to amend Form ADV to add a new Part 3 (the relationship summary), and to amend rule 204-2, the Commission requested public comment on the effect of information collections under these amendments. The Commission and the staff of the Division of Investment Management continue to 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 facing the industry.

9. Payment or Gift

None.

10. Confidentiality

Responses provided to the Commission pursuant to rule 204-2 in the context of the Commission's examination and oversight program are generally kept confidential.⁷

11. Sensitive Questions

No information of a sensitive nature, including social security numbers, will be required under this collection of information. The information collection collects basic Personally Identifiable Information (PII) that may include names, job titles, work addresses, and phone numbers. However, the agency has determined that the information collection does not constitute a system of record for purposes of the Privacy Act. Information is not retrieved by a personal identifier.

⁷ See *supra* note 4.

12. Burden of Information

The approved annual aggregate burden for rule 204-2 is currently 2,199,791 hours, with a total annual aggregate monetized cost burden of approximately \$130,316,112, based on an estimate of 12,024 registered advisers, or 183 hours per registered adviser.⁸ Taking into account the estimated annual burden of registered advisers that would be required to maintain records of the relationship summary, as well as the estimated annual burden of registered advisers that do not have relationship summary obligations and whose information collection burden is unchanged, the revised annual aggregate burden for all respondents to rule 204-2, under the proposed amendments, would be estimated to be 2,329,468 total hours,⁹ for a monetized cost of \$142,540,147.¹⁰

Based on Investment Adviser Registration Depository data as of December 31, 2017, there are approximately 12,721 SEC registered advisers required to maintain copies of certain books and records relating to their advisory business. This is an increase of 697 SEC registered advisers over the previously approved burden. Only those registered investment advisers offering services to retail investors would be required to prepare and file a relationship summary. We estimate that based on updated IARD data as of December 31, 2017, 7,625 investment advisers provide advice to individual high net worth and individual non-high net worth clients,

⁸ 2,199,791 hours / 12,024 registered advisers = 183 hours per adviser. *See* Form ADV and Investment Advisers Act Rules, Final Rule, Investment Advisers Act Release No. 4509 (Aug. 25, 2016) [81 FR 60418 (Sep. 1, 2016)] (“2016 Form ADV Paperwork Reduction Analysis”), at 81 FR at 60454-55.

⁹ 7,625 registered investment advisers required to prepare relationship summary x 183.2 hours = 1,396,900 hours. 5,096 registered investment advisers not required to prepare the relationship summary x 183 hours = 932,568 hours. 1,396,900 hours + 932,568 hours = 2,329,468 hours.

¹⁰ *See infra* notes 14 and 17. \$85,476,311 + \$57,063,836 = \$142,540,147.

and would therefore be subject to the amended provisions of rule 204-2 to preserve the relationship summary as a result of the proposed new rule 204-5 and amendments to Form ADV under the Advisers Act.¹¹

We estimate that the proposed amendments to rule 204-2 would result in an increase in the collection of information burden estimate by 0.2 hours¹² for each of the estimated 7,625 registered advisers with relationship summary obligations, resulting in a total of 183.2 hours per adviser. This would yield an annual estimated aggregate burden of 1,396,900 hours under amended rule 204-2 for all registered advisers with relationship summary obligations,¹³ for a monetized cost of \$85,476,311.¹⁴ In addition, the 5,096 advisers¹⁵ not subject to the proposed

¹¹ The proposal includes amendments to Form ADV to add a new Part 3 (the firm relationship summary), and new rule 204-5 regarding delivery of the relationship summary. The hourly and cost burdens for those requirements are included in separate collections of information associated with their respective rules.

¹² In the Paperwork Reduction Act analysis for amendments to Form ADV adopted in 2016, we estimated that 1.5 hours would be required for each adviser to make and keep records relating to (i) the calculation of performance the adviser distributes to any person and (ii) all written communications received or sent relating to the adviser's performance. Because the burden of preparing of the relationship summary is already included in the collection of information estimates for Form ADV, and because the relationship is a short, standardized document, we assume that recordkeeping burden for the relationship summary would be considerably less than 1.5 hours and estimate that 0.2 hours would be appropriate.

¹³ 7,625 registered investment advisers required to prepare relationship summary x 183.2 hours = 1,396,900 hours.

¹⁴ As with our estimates relating to the previous amendments to rule 204-2 (*see* 2016 Form ADV Paperwork Reduction Analysis, *supra* note 8, at 81 FR at 60454-55, we expect that performance of this function will most likely be allocated between compliance clerks and general clerks, with compliance clerks performing 17% of the function and general clerks performing 83% of the function. Data from the SIFMA Office Salaries in the Securities Industry Report, modified to account for an 1,800-hour work year and multiplied by 2.93 to account for bonuses, firm size, employee benefits, and overhead ("SIFMA Office Salaries Report"), suggest that costs for these position are \$67 and \$60, respectively. $(17\% \times 1,396,900 \text{ hours} \times \$67) + (83\% \times 1,396,900 \text{ hours} \times \$60) = \$85,476,311$.

¹⁵ 12,721 registered investment advisers – 7,625 = 5,096 registered investment advisers not

amendments would continue to be subject to an unchanged burden of 183 hours under rule 204-2, or a total aggregate annual hour burden of 932,568,¹⁶ for a monetized cost of \$57,063,836.¹⁷

13. Cost to Respondents

There is no cost burden other than the cost of the hour burden described above.

14. Cost to the Federal Government

There are no additional costs to the federal government directly attributable to rule 204-2.

15. Changes in Burden

We estimate that the total burden hour associated with rule 204-2 will increase from 2,199,791 hours per year to 2,329,468 hours per year because of the proposed amendments to rule 204-2.¹⁸ These increases are attributable to a larger registered investment adviser population since the most recent approval and adjustments for inflation, as well as the proposed rule 204-2 amendments relating to the relationship summary.

16. Information Collection Planned for Statistical Purposes

None.

providing advice to retail investors.

¹⁶ 5,096 registered investment advisers not required to prepare the relationship summary x 183 hours = 932,568.

¹⁷ As with our estimates relating to the previous amendments to rule 204-2 (*see* 2016 Form ADV Paperwork Reduction Analysis, *supra* note 8, at 81 FR at 60454-55, we expect that performance of this function will most likely be allocated between compliance clerks and general clerks, with compliance clerks performing 17% of the function and general clerks performing 83% of the function. Data from the SIFMA Office Salaries Report suggest that costs for these position are \$67 and \$60, respectively. $(17\% \times 932,568 \text{ hours} \times \$67) + (83\% \times 932,568 \text{ hours} \times \$60) = \$57,063,836$.

¹⁸ *See supra* note 9.

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.