

**SUPPORTING STATEMENT**  
**For the Paperwork Reduction Act Information Collection Submission for**  
**Rule 17e-1**

**A. JUSTIFICATION**

**1. Necessity for the Information Collection**

Section 17(e)(2)(A) of the Investment Company Act of 1940 (the “Investment Company Act”)<sup>1</sup> limits the remuneration a broker affiliated with a registered investment company (“fund”) may receive in connection with the sale of securities to or by the fund or controlled company thereof, to no more than “the usual and customary broker’s commission if the sale is effected on a securities exchange.”<sup>2</sup> Rule 17e-1 under the Investment Company Act deems a remuneration as “not exceeding the usual and customary broker’s commission” for purposes of Section 17(e)(2)(A) if, among other things, the fund’s board of directors has adopted procedures reasonably designed to provide that the remuneration to the affiliated broker is reasonable and fair compared to that received by other brokers in connection with comparable transactions involving similar securities being purchased or sold on a securities exchange during a comparable period of time and the board makes and approves such changes as it deems necessary.<sup>3</sup> In addition, each quarter, the board must determine that all transactions effected under the rule during the preceding quarter complied with the established procedures (“review requirement”). Rule 17e-1(d) also requires the fund to (i) maintain permanently a written copy of the procedures adopted by the board for complying with the requirements of the rule; and (ii) maintain for a period of six years, the first two in an easily accessible place, a written record of each transaction subject to the rule setting forth the amount and source of the commission, fee, or

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<sup>1</sup> 15 U.S.C. 80a-1 *et seq.*

<sup>2</sup> 15. U.S.C. 80a-17(e)(2)(A).

<sup>3</sup> 17 CFR 270.17e-1.

other remuneration received; the identity of the broker; the terms of the transaction; and the materials used to determine that the transactions were effected in compliance with the procedures adopted by the board (“recordkeeping requirement”).

Rule 17e-1 conditionally exempts funds from having to comply with the review requirement and the recordkeeping requirement when an affiliated subadviser that serves as a broker is not in a position to influence the fund’s decision to participate in the transaction. To qualify for this exemption, rule 17e-1 requires, in part, that the advisory contracts of both the subadviser that enters into the transaction, and the subadviser that recommends that the fund engage in the transaction prohibit the subadvisers from consulting with one another concerning securities transactions of the fund.<sup>4</sup> The rule’s conditions are designed to limit the exemptions to those transactions in which the transacting subadviser has neither the ability nor the incentive to influence the investment decision of the participating fund.<sup>5</sup>

## **2. Purpose and Use of the Information Collection**

The recordkeeping requirements under rule 17e-1 enable the Commission to ensure that affiliated brokers receive compensation that does not exceed the usual and customary broker’s commission. Without the recordkeeping requirements, Commission inspectors would have difficulty ascertaining whether funds were complying with rule 17e-1. Commission rules also require funds to amend their subadvisory contracts before they can rely on rule 17e-1’s exemption to ensure that the subadviser that engages in the transaction does not influence the fund’s decision to participate in the transaction.

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<sup>4</sup> See 17 CFR 270.17a-10(a)(2); 17 CFR 270.17e-1(b)(3); 17 CFR 270.17e-1(d)(2).

<sup>5</sup> See Investment Company Act Release 25,888 (Jan. 14, 2003) [68 FR 3142, 3144 (Jan. 22, 2003)].

### **3. Consideration Given to Information Technology**

To the extent the rule includes recordkeeping requirements, the Electronic Signatures in Global and National Commerce Act<sup>6</sup> and the conforming amendments to recordkeeping rules under the Investment Company Act permit funds to maintain records electronically.

### **4. Duplication**

Section 31(a) of the Investment Company Act and rules 31a-1 and 31a-2 thereunder, require investment companies to maintain and preserve records similar to those required to be kept under rule 17e-1. Rule 17e-1 does not require that duplicate records be kept, but reiterates the requirement to maintain and preserve such records. The requirements regarding limitations in the subadvisers' contracts are similar to conditions in exemptive rules 10f-3,<sup>7</sup> 12d3-1,<sup>8</sup> and 17a-10.<sup>9</sup> To the extent that a fund relies on any one of these rules, its subadviser may use the same contract language to satisfy the comparable condition in the other rules.

### **5. Effect on Small Entities**

The recordkeeping requirements of rule 17e-1 apply equally to all funds subject to the rule, regardless of size. The burden on smaller investment companies may be greater than for larger investment companies. This burden includes the cost of amending subadvisory contracts, reviewing transactions, and maintaining records. 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 requirements. The Commission reviews all

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<sup>6</sup> P.L. 106-229, 114 Stat. 464 (June 30, 2000).

<sup>7</sup> 17 CFR 270.10f-3.

<sup>8</sup> 17 CFR 270.12d3-1.

<sup>9</sup> 17 CFR 270.17a-10.

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**

Rule 17e-1(c) requires the investment company to (i) maintain permanently a written copy of the procedures adopted by the board for complying with the requirements of the rule; and (ii) maintain for a period of six years a written record of each transaction subject to the rule setting forth the amount and source of the commission, fee, or other remuneration received; the identity of the broker; the terms of the transaction; and the materials used to determine that the transactions were effected in compliance with the procedures adopted by the board. Less frequent recordkeeping requirements would impair the Commission's ability to ascertain compliance with the rule. Rule 17e-1 also requires that a fund's subadvisory contract either be initially drafted or amended to qualify for the rule's exemption. This is not a recurring requirement; less frequent collection is not possible.

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

Rule 17e-1 requires funds to preserve certain records for six years and other records permanently. We believe that the long-term retention of records is necessary to carry out our examination and enforcement responsibilities, and our mandate to ensure that the Investment Company Act's provisions are legally enforceable. We periodically inspect the operations of funds to ensure compliance with the rules and regulations under the Investment Company Act; however, each fund may be inspected only at intervals of several years due to limits on our resources. Furthermore, Congress has placed no time limit on the prosecution of persons engaged in certain types of conduct that violate the securities laws. For these reasons, we often

need information relating to events or transactions that occurred years ago. In Section 31(a) of the Investment Company Act, Congress specifically authorized the Commission to require funds to maintain and preserve books and records for such periods as the Commission may prescribe by rules.<sup>10</sup> Computerized record storage has made long-term retention of records less burdensome.

#### **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 company 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. The Commission requested public comment on the collection of information requirements in rule 17e-1 before it submitted this request for extension and approval to the Office of Management and Budget. The Commission received no comments in response to this request.

#### **9. Payment or Gift**

No payment or gift to respondents was provided.

#### **10. Confidentiality**

No assurance of confidentiality was provided.

#### **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

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<sup>10</sup> 15 U.S.C. 80a-30(a).

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 following estimates of average burden hours and costs are made solely for purposes of the Paperwork Reduction Act of 1995<sup>11</sup> and are not derived from a comprehensive or even representative survey or study of the costs of Commission rules and forms.

Based on an analysis of fund filings, the staff estimates that approximately 266 funds enter into subadvisory agreements each year.<sup>12</sup> Based on discussions with industry representatives, the staff estimates that it will require approximately 3 attorney hours to draft and execute additional clauses in new subadvisory contracts in order for funds and subadvisers to be able to rely on the exemptions in rule 17e-1. Because these additional clauses are identical to the clauses that a fund would need to insert in their subadvisory contracts to rely on rules 12d3-1, 10f-3, and 17a-10, and because we believe that funds that use one such rule generally use all of these rules, we apportion this 3 hour time burden equally to all four rules. Therefore, we estimate that the burden allocated to rule 17e-1 for this contract change would be 0.75 hours.<sup>13</sup> Assuming that all 266 funds enter into new subadvisory contracts each year make the modification to their contract required by the rule, we estimate that the rule's contract

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<sup>11</sup> 4 U.S.C. 3501 *et seq.*

<sup>12</sup> Based on data from Morningstar, as of June 30, 2018, there are 12,393 registered funds (open-end funds, closed-end funds, and exchange-traded funds), 4,594 funds of which have subadvisory relationships (approximately 37%). Based on data from the 2018 ICI Factbook, 720 new funds were established in 2017 (705 open-end funds and exchange-traded funds + 15 closed-end funds (from the ICI Research Perspective, April 2018)). 720 new funds x 37% = 266 funds.

<sup>13</sup> 3 hours ÷ 4 rules = 0.75 hours.

modification requirement will result in 200 burden hours annually, with an associated cost of approximately \$80,200.<sup>14</sup>

Based on an analysis of fund filings, we estimate that approximately 1,609 funds use at least one affiliated broker. Based on staff experience and conversations with fund representatives, the staff estimates approximately 40 percent of transactions (and thus, 40% of funds) that occur under rule 17e-1 would be exempt from its recordkeeping and review requirements. This would leave approximately 965 funds<sup>15</sup> still subject to the rule's recordkeeping and review requirements. Based on staff experience and conversations with fund representatives, we estimate that the burden of compliance with rule 17e-1 is approximately 50 hours per fund per year. This time is spent, for example, reviewing the applicable transactions and maintaining records. Accordingly, we calculate the total estimated annual internal burden of complying with the review and recordkeeping requirements of rule 17e-1 to be approximately 48,250 hours.<sup>16</sup>

Of the 48,250 hours spent annually to comply with the review and recordkeeping requirements of rule 17e-1, the Commission estimates that:

- 60 percent (28,950 hours) are spent by senior accountants, at an estimated hourly

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<sup>14</sup> These estimates are based on the following calculations: (0.75 hours × 266 funds = 200 burden hours); (\$401 per hour × 200 hours = \$80,200 total cost). The Commission's estimates concerning the wage rates for attorney time are based on salary information for the securities industry compiled by the Securities Industry and Financial Markets Association. The estimated wage figure is based on published rates for in-house attorneys, modified to account for an 1,800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits, and overhead, yielding an effective hourly rate of \$401. *See* Securities Industry and Financial Markets Association, Report on Management & Professional Earnings in the Securities Industry 2013.

<sup>15</sup> 1,609 funds × 0.6 = 965 funds.

<sup>16</sup> 965 funds × 50 hours per fund = 48,250 hours.

wage of \$209,<sup>17</sup> for a total of approximately \$6,050,550 per year;<sup>18</sup>

- 30 percent (14,475 hours) are spent by in-house attorneys at an estimated hourly wage of \$401, for a total of approximately \$5,804,475 per year;<sup>19</sup> and
- 10 percent (4,825 hours) are spent by the funds' board of directors at an hourly cost of \$4,465, for a total of approximately \$21,543,625 per year.<sup>20</sup>

Based on these estimated wage rates, the total cost to the industry of the hour burden for complying with the review and recordkeeping requirements of rule 17e-1 is approximately \$33,398,650.<sup>21</sup> Accordingly, annual burden of the rule's paperwork requirements is 48,450 hours,<sup>22</sup> at an estimated cost of \$33,478,850.<sup>23</sup>

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<sup>17</sup> The Commission's estimates concerning the allocation of burden hours and the relevant wage rates are based on consultations with industry representatives and on salary information for the securities industry compiled by the Securities Industry and Financial Markets Association. The estimated wage figures are also based on published rates for senior accountants and in-house attorneys, modified to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits, and overhead, yielding effective hourly rates of \$209 and \$401, respectively. *See* Securities Industry and Financial Markets Association, Report on Management & Professional Earnings in the Securities Industry 2013.

<sup>18</sup> 28,950 hours x \$209 per hour = \$6,050,550.

<sup>19</sup> 14,475 hours x \$401 per hour = \$5,804,475.

<sup>20</sup> 4,825 hours x \$4,465 per hour = \$21,543,625. The estimate for the cost of board time as a whole is derived from estimates made by the staff regarding typical board size and compensation that is based on information received from fund representatives and publicly available sources.

<sup>21</sup> \$6,050,550 + \$5,804,475 + \$21,543,625 = \$33,398,650.

<sup>22</sup> 200 hours + 48,250 hours = 48,450 hours.

<sup>23</sup> \$80,200 + \$33,398,650 = \$33,478,850.



**Table 1: Summary of Revised Annual Responses, Burden Hours, and Burden Hour  
Costs Estimates for Each Information Collection**

IC	IC Title	Annual No. of Responses			Annual Time Burden (Hrs.)			Cost Burden (\$)		
		<i>Previously approved</i>	<i>Requested</i>	<i>Change</i>	<i>Previously approved</i>	<i>Requested</i>	<i>Change</i>	<i>Previously approved</i>	<i>Requested</i>	<i>Change</i>
IC1	Review and Record-keeping	1,018	965	-53	50,900	48,250	-2,650	34,245,520	33,398,650	-846,870
IC2	Contractual Provisions	320	266	-54	240	200	-40	91,200	80,200	-11,000
<b>Total for all ICs</b>		1,338	1,231	-107	51,140	48,450	-2,690	34,336,720	33,478,850	-857,870

### **13. Cost to Respondents**

There is no annual cost burden associated with complying with the information collection requirements in rule 17e-1. The cost burden does not include the cost of the hour burden discussed in Item 12 above.

### **14. Cost to the Federal Government**

The rule does not require anything to be filed with the Commission. Commission staff may, in the course of routine fund inspections, monitor compliance with the rule.

### **15. Changes in Burden**

The estimated hourly burden associated with rule 17e-1 has decreased from 51,140 hours to 48,450 hours (a decrease of 2,690 hours). The net decrease is due to (i) a decrease in the number of funds estimated to enter into subadvisory agreements each year; and (ii) a decrease in the number of funds estimated to use an affiliated broker.

### **16. Information Collection Planned for Statistical Purposes**

The results of any information collected will not be published.

**17. Approval to Omit OMB Expiration Date**

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

**18. Exceptions to Certification Statement for Paperwork Reduction Act**

**Submission**

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.