

SUPPORTING STATEMENT
for the Paperwork Reduction Act Information Collection Submission for
“Rule 19b-5 and Form PILOT”

A. Justification

1. Necessity of Information Collection

The Securities Exchange Act of 1934, as amended (“Exchange Act”),¹ sets forth a scheme of self-regulation under which national securities exchanges, national securities associations, and registered clearing agencies have primary responsibility for regulating their members or participants. Under this scheme, the role of the Securities and Exchange Commission (“SEC”) is primarily one of oversight; the Exchange Act charges the SEC with the responsibility for assuring that each of these self-regulatory organizations (“SROs”) complies with and advances the policies of the Exchange Act. As part of its oversight responsibilities, the SEC is required to review changes in the rules of each SRO.

Section 19(b) of the Exchange Act² requires an SRO to file with the SEC a copy of any proposed amendment to its constitution, articles of incorporation, bylaws, rules, or similar instrument or any interpretation of these instruments (collectively, “rule changes”). The SEC is required to publish notice of any such filing, and when required to approve the rule change or institute proceedings to determine whether the rule change should be disapproved. Rule 19b-4 under the Exchange Act³ implements the requirements of Section 19(b) of the Act by requiring an SRO to file its rule changes on Form 19b-4 and by clarifying which actions by an SRO must be filed pursuant to Section 19(b). The SEC adopted Rule 19b-4 in 1975 pursuant to Sections 2, 3C, 6, 11A, 15A, 15B, 17, 17A, and 19 of the Exchange Act and Section 806 of the Payment, Clearing and Settlement Supervision Act.

Rule 19b-5 under the Exchange Act⁴ provides a temporary exemption from the rule-filing requirements of Section 19(b) of the Exchange Act to an SRO wishing to establish and operate a pilot trading system. An SRO that seeks to establish a pilot trading system must file a Form PILOT with the SEC. Certain provisions of Rule 19b-5 and Form PILOT contain collection of information requirements within the meaning of the Paperwork Reduction Act of 1995.⁵ Rule 19b-5 permits an SRO to develop a pilot trading system and to begin operation of such system shortly after submitting an initial report on Form PILOT to the SEC. During operation of the pilot trading system, the SRO must submit quarterly reports of the system’s operation to the SEC on Form PILOT, as well as timely amendments on Form PILOT describing any material changes to the system. After two years of operating such pilot trading system under the exemption afforded by

¹ 15 U.S.C. 78a et seq.

² 15 U.S.C. 78s(b).

³ 17 CFR 240.19b-4.

⁴ 17 CFR 240.19b-5.

⁵ 44 U.S.C. 3501 et seq.

Rule 19b-5, the SRO must submit a rule filing pursuant to Section 19(b)(2) of the Exchange Act⁶ in order to obtain permanent approval of the trading system from the SEC.

2. Purpose and Use of the Information Collection

The purpose of Rule 19b-5 is to provide a temporary exemption from the rule-filing requirements that would otherwise apply to an SRO wishing to operate a pilot trading system. In the absence of this exemption, an SRO would be required to submit a proposed rule change to the SEC pursuant to Section 19(b) of the Exchange Act and Rule 19b-4 thereunder in order to operate any new trading system. Section 19(b) of the Exchange Act generally requires an SRO to file with the SEC copies of any proposed rule or any proposed change in, addition to, or deletion from the rules of such SRO. Once a proposed rule change has been filed, the SEC must publish notice of its receipt and allow an opportunity for the public to comment on it. A proposed rule change may not take effect unless it is approved by the SEC or is otherwise permitted to become effective under Section 19(b) of the Exchange Act. In order to approve a rule change proposing a new trading system, the SEC would be required to find that, among other things, the trading system will serve to promote the public interest and help to remove impediments to a free and open securities market in accordance with the requirements of Section 6(b)(5) of the Exchange Act.⁷ Further, pursuant to Section 3(f) of the Exchange Act,⁸ the SEC would have to consider whether the proposed trading system would, in addition to the protection of investors, promote efficiency, competition, and capital formation.

Rule 19b-5 permits an SRO to operate a pilot trading system immediately, without requiring any SEC findings, provided that such system is in compliance with the conditions set forth in Rule 19b-5. For the SEC to maintain an accurate record of all new pilot trading systems operated by SROs and to determine whether an SRO has properly availed itself of the exemption afforded by Rule 19b-5, an SRO must file a Form PILOT in conjunction with the operation of a new pilot trading system, providing the SEC with at least 20 days' notice before commencing operations of the pilot trading system. In addition, for the SEC to determine whether an SRO is operating a pilot trading system in compliance with the Exchange Act and is carrying out its statutory oversight obligations under the Exchange Act, the SRO must submit quarterly reports of the system's operation and amendments describing material changes to the system to the SEC on Form PILOT. The SEC will review SRO compliance with Rule 19b-5 and other provisions of the Exchange Act through its routine inspections and examinations.

An SRO operating a pilot trading system pursuant to Rule 19b-5 also must notify the SEC on Form PILOT of changes to the pilot trading system and to make quarterly reports of its operations. Without such information, the SEC might not have sufficient information to ensure that the pilot trading system continued to operate in a manner consistent with the Exchange Act.

⁶ 15 U.S.C. 78s(b)(2).

⁷ 15 U.S.C. 78f(b)(5).

⁸ 15 U.S.C. 78c(f)

3. Consideration Given to Information Technology

The compilation and filing of the information required about a pilot trading system reflects the complexity of the SROs' businesses and is read and reviewed by SEC staff. Thus, improved technology would not reduce the burden.

4. Duplication

Not applicable. The SEC believes that no duplication of the requirements of Rule 19b-5 exists. Additionally, the SEC notes that Rule 17a-1 under the Exchange Act⁹ currently imposes recordkeeping requirements on SROs. Although Rule 19b-5 does not create new recordkeeping obligations for SROs, paragraph (e)(9) of Rule 19b-5¹⁰ reiterates the SROs' existing recordkeeping obligations under Rule 17a-1.

5. Effect on Small Entities

Not applicable. The SROs that are required to respond to the collection of information are not small entities.

6. Consequences of Not Conducting Collection

Rule 19b-5 requires that information describing a pilot trading system be filed prior to the SRO's operation of such system, and that subsequent information regarding the system be provided on a quarterly basis thereafter and whenever any material change is made to the system. Any less frequent collection of this information would impede the SEC's ability to fulfill its statutory obligations to maintain fair and orderly markets and protect investors.

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

There are no special circumstances. The information collection is consistent with the guidelines in 5 CFR 1320.5(d)(2).

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

Not applicable. No payments or gifts are required to be made or are made to respondents.

⁹ 17 CFR 240.17a-1.

¹⁰ 17 CFR 240.19b-5(e)(9).

10. Confidentiality

The information required by Rule 19b-5 is available only for examination by the SEC, other agencies of the federal government, and state securities authorities. Subject to the provisions of the Freedom of Information Act (“FOIA”)¹¹ and the SEC’s rules thereunder, the SEC generally will not publish or make available information contained in any 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 information of a sensitive nature, including social security numbers, are required under this collection of information. The information collection includes basic Personally Identifiable Information that may include name, job title, work address, work telephone number, and work facsimile number. However, the SEC 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. In accordance with Section 208 of the E-Government Act of 2002, the agency has determined that the information collection does not trigger the Privacy Impact Assessment requirement. The information collection is collected and maintained in paper.

12. Burden of Information Collection

Initial Reports

The SEC anticipates receiving as many as three (3) initial reports on Form PILOT each year. The SEC estimates that the reporting burden for an SRO that files an initial report on Form PILOT prior to operating a pilot trading system would be approximately 24 hours (16 hours of professional legal work and 8 hours of clerical work). Collectively, this would be an aggregate annual burden of 72 hours (3 responses x 24 hours per response) for the three respondents. The Commission estimates that the related internal compliance cost for an SRO to complete an initial report on Form PILOT would be \$7,256, calculated as follows:

16 hours of in-house professional legal work at \$422/hr ¹²	\$ 6,752
8 hours of clerical work at \$63/hr ¹³	\$ 504
	<u>\$ 7,256</u>

¹¹ 5 U.S.C. 522.

¹² \$422/hour figure for an Attorney is from the SIFMA’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.

¹³ \$63/hour figure for a General Clerk is from the SIFMA’s *Office Salaries in the Securities Industry 2013*, modified by Commission staff to account for an 1800-hour work-year and inflation and multiplied by 2.93 to account for bonuses, firm size, employee benefits, and overhead.

Thus, the aggregate annual internal cost of compliance for all SROs to file initial reports would be \$21,768 ($\$7,256 \times 3$).

Quarterly Reports

The SEC anticipates receiving as many as twelve (12) quarterly reports per year, one per quarter from each of the three estimated respondents. The SEC estimates that the reporting burden for an SRO that files a quarterly report on Form PILOT would be approximately 3 hours per report (2 hours of professional legal work and 1 hour of clerical work). Therefore, the collective annual burden would be 36 hours (12 responses \times 3 hours per response) for the three respondents. The Commission estimates that the related annual internal compliance cost for each SRO to file four quarterly reports would be \$3,628 ($\$422 \times 2 + \$63 = \907; $\$907 \times 4 = \$3,628$). Thus, the aggregate annual internal cost of compliance for all SROs to file quarterly reports would be \$10,884 ($\$3,628 \times 3$).

Material Systems Changes Reports

The SEC anticipates receiving as many as six (6) notices of material systems changes per year, two notices per each of the three estimated respondents. The SEC estimates that the reporting burden for an SRO that files a notice of a material systems change on Form PILOT would be approximately 3 hours per notice (2 hours of professional legal work and 1 hour of clerical work). Therefore, the collective annual burden would be 18 hours (6 responses \times 3 hours per response) for the three respondents. The Commission estimates that the related annual internal compliance cost for each SRO to file notices of material systems changes would be \$1,814 ($\$422 \times 2 + \$63 = \907; $\$907 \times 2 = \$1,814$). Thus, the aggregate annual internal cost of compliance for all SROs to file notices of material systems changes would be \$5,442 ($\$1,814 \times 3$).

Summary

There are currently 23 SROs which could avail themselves of the exemption provided by Rule 19b-5. The SEC estimates that each year, three of these SROs would avail themselves of the exemption and be required to file Form PILOT. The collective annual time burden for all three respondents would be 126 hours. As detailed above, this aggregate figure consist of: (i) 72 hours for initial reports on Form PILOT (one filing for each of the three estimated respondents requiring 24 hours of work per filing); (ii) 36 hours for quarterly reports on Form PILOT (four filings for each of the three estimated respondents requiring 3 hours of work per filing); and (iii) 18 hours for notices of material systems changes on Form PILOT (two filings for each of the three estimated respondents requiring three hours of work per filing). The estimated aggregate annual internal cost of compliance for all three respondents would be \$38,094 ($\$21,768 + \$10,884 + \$5,442$).¹⁴

¹⁴ An average of approximately \$302.333 per hour.

Below is a chart summarizing the hour burdens related to Rule 19b-5 and Form PILOT.

Respondent Type	Number of Respondents	Number of Annual Reponses Per Respondent	Time Per Response (Hours)	Total Annual Burden (Hours)
Initial Reports	3	1	24	72
Quarterly Reports	3	4	3	36
Material Systems Changes Reports	3	2	3	18
Total Annual Burden for All Respondents (Hours)				<u>126</u>

13. Costs to Respondents

The SEC estimates that the three SRO respondents would, in the aggregate, incur printing, supplies, copying, and postage expenses of \$6,101 per year for filing initial reports on Form PILOT, \$3,046 per year for filing quarterly reports on Form PILOT, and \$1,523 per year for filing notices of material systems changes on Form PILOT, for a total annual cost burden of \$10,670.

Additionally, the SEC notes that Rule 19b-5 does not in itself impose new recordkeeping burdens on SROs, though it relies on existing requirements imposed pursuant to Rule 17a-1 under the Exchange Act.

Below is a chart summarizing the cost burdens related to Rule 19b-5 and Form PILOT.

Respondent Type	Dollar Cost for Printing, Supplies, Copying, and Postage
Initial Reports	\$6,101
Quarterly Reports	\$3,046
Material Systems Changes Reports	\$1,523
Total Annual Burden for All Respondents (Dollars)	
	<u>\$10,670</u>

14. Costs to Federal Government

The SEC anticipates receiving up to three initial reports on Form PILOT per year, 12 quarterly reports on Form PILOT per year, and six notices of system changes on Form PILOT per year. The SEC estimates that the average annual cost to the SEC of processing all of these filings would be \$7,683. This aggregate figure includes the following component costs:

3 initial reports on Form PILOT per year

3 hours legal processing time at \$271/hr	\$ 813
overhead, including clerical work	<u>\$ 285</u>
	\$1098

12 quarterly reports on Form PILOT per year

12 hours legal processing time at \$271/hr	\$ 3,252
overhead, including clerical work	<u>\$ 1,138</u>
	\$ 4,390

6 notices of systems changes on Form PILOT per year

6 hours legal processing time at \$271/hr	\$ 1,626
overhead, including clerical work	<u>\$ 569</u>
	\$ 2,195

For the purposes of our estimates the SEC has valued related overhead at 35% of the value of legal and clerical time combined.

The SEC notes that, after the two-year exemption provided by Rule 19b-5 from the requirements to file proposed rule changes under Section 19(b) of the Exchange Act has expired for a given trading system operated by an SRO, the SEC staff tasked with processing the subsequent proposed rule changes for such trading system will already be familiar with that system, which could reduce the costs to the SEC of processing such proposed rule changes.

15. Changes in Burden

The estimated burden hours in item #12 did not change. The estimated costs to respondents in item #13 increased by \$623 due to inflation.

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 SEC requests authorization to omit the expiration date on the electronic version of the form. Including the expiration date on the electronic version of the form will result in increased costs, because the need to make changes to the form may not follow the application's scheduled version release dates. The OMB control number will be displayed.

18. Exceptions to Certification for Paperwork Reduction Act Submissions

This collection complies with the requirements in 5 CFR 1320.9.

B. Collection of Information Employing Statistical Methods

This collection does not involve statistical methods.