

**SUPPORTING STATEMENT FOR
PAPERWORK REDUCTION ACT SUBMISSION AMENDMENT TO
RULE 204-2**

A. JUSTIFICATION

1. Necessity for the Information Collection

Section 204 of the Investment Advisers Act of 1940 (the “Advisers Act”) provides that investment advisers required to register with the Securities and Exchange Commission (the “Commission”) must make and keep certain records for prescribed periods, and make and disseminate certain reports.¹ 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.

On November 4, 2019, the Commission proposed amendments to rules related to how advisers advertise to and solicit clients and investors⁴. The proposed amendments to the advertising rule, rule 206(4)-1⁵ under the Advisers Act, would replace the current advertising rule’s broadly drawn limitations with principles-based provisions, and the proposed amendments

¹ 15 U.S.C. 80b-4.

² 17 CFR 275.204-2.

³ *See id.* at 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.

⁴ Investment Adviser Advertisements; Compensation for Solicitations, Release No. IA-5407 (November 4, 2019) [84 FR 67518 (Dec. 10, 2019)]

⁵ 17 CFR § 275.206(4)-1.

to the Advisers Act cash solicitation rule, rule 206(4)-3,⁶ would expand the rule to cover solicitation arrangements involving all forms of compensation, rather than only cash compensation, eliminate requirements duplicative of other rules, and tailor the required disclosures solicitors would provide to investors.⁷ The Commission also proposed amendments under the Advisers Act to the books and records rule, rule 204-2, to correspond to the proposed changes to the advertising and solicitation rules.

The proposed amendments to rule 204-2 would require registered advisers to retain copies of advertisements to one or more persons,⁸ whereas the current rule requires investment advisers to retain copies of advertisements to 10 or more persons.⁹ Under the amendments to the rule, investment advisers will also be required to retain (i) for investment advisers that use a third-party rating in any advertisement, a copy of any questionnaire or survey used in preparation of the third-party rating; and, (ii) a copy of all written approvals of advertisements required under proposed rule 206(4)-1(d).¹⁰ To correspond to proposed changes to rule 206(4)-3, the Commission also proposed to amend the current books and records rule to replace the rule's requirement that investment advisers keep a record of all written acknowledgments of receipt obtained from clients pursuant to rule 206(4)-3(a)(2)(iii)(B) with the proposed requirement that

⁶ 17 CFR § 275.206(4)-3.

⁷ See Release No. IA-5407, *supra* footnote 4.

⁸ See proposed rule 204-2(a)(11); see also Release No. IA-5407, *supra* note 4, at section II.C (discussing the proposed amendments to the books and records rule).

⁹ See 17 CFR § 275.204-2.

¹⁰ See proposed rule 204-2(a)(11); see also Release No. IA-5407, *supra* note 4, at section II.C (discussing the proposed amendments to the books and records rule).

an investment adviser retain any communication or other document related to the investment adviser's determination that it has a reasonable basis for believing that any solicitor it compensates under the solicitation rule has complied with the written agreement required by the solicitation rule.¹¹

Additionally, to correspond to other proposed changes to the solicitation rule, we would amend the books and records rule to require investment advisers to make and keep records of: (i) if the adviser participates in any nonprofit program pursuant to the solicitation rule, copies of all receipts of reimbursements of payments or other compensation the adviser provides relating to its inclusion in the program; (ii) any communication or other document related to the investment adviser's determination that it has a reasonable basis for believing that any solicitor it compensates under rule 206(4)-3 is not an ineligible solicitor, and that any nonprofit program it participates in pursuant to the solicitation rule meets the requirements of the solicitation rule; and (iii) the names of all solicitors who are an adviser's partners, officers, directors or employees or other affiliates, pursuant to the solicitation rule.¹² All of these records will 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).

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

¹¹ *Id.*

¹² *Id.*

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: (i) copies of copies of advertisements to one or more persons;¹³ (ii) for investment advisers that use a third-party rating in any advertisement, a copy of any questionnaire or survey used in preparation of the third-party rating; (iii) a copy of all written approvals of advertisements required under proposed rule 206(4)-1(d); (iv) any communication or other document related to the investment adviser's determination that it has a reasonable basis for believing that any solicitor it compensates under the solicitation rule has complied with the written agreement required by the solicitation rule.¹⁴ The proposed amendments would also require registered advisers to make and keep records of: (i) if the adviser participates in any nonprofit program pursuant to the solicitation rule, copies of all receipts of reimbursements of payments or other compensation the adviser provides relating to its inclusion in the program; (ii) any communication or other document related to the investment adviser's determination that it has a reasonable basis for believing that any solicitor it compensates under rule 206(4)-3 is not an ineligible solicitor, and that any nonprofit program it participates in pursuant to the solicitation rule meets the requirements of the solicitation rule; and (iii) the names of all solicitors who are an adviser's partners, officers, directors or employees or other affiliates, pursuant to the solicitation rule. The

¹³ The current rule requires investment advisers to retail copies of advertisements to 10 or more persons. *See* 17 CFR § 275.204-2.

¹⁴ The current books and records rule requires advisers keep a record of all written acknowledgments of receipt obtained from clients pursuant to rule 206(4)-3(a)(2)(iii)(B).

purpose of the information collection in rule 204-2 is to assist the Commission's examination and oversight program. Requiring the creation, maintenance and retention of the above records as part of rule 204-2 would facilitate the Commission's ability to inspect for and enforce compliance with firms' obligations with respect to rules 206(4)-1 and 206(4)-3.

The respondents to the rule are investment advisers registered with the Commission. The likely respondents for the amendments to the rule will be the investment advisers registered with the Commission that advertise or compensate solicitors. Responses provided to the Commission in the context of its examination and oversight program are generally kept confidential.¹⁵ 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.¹⁶

4. Duplication

The collection of information requirements of the rule, including the 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 amendments to rule 204-2 will not distinguish between small entities and other investment advisers because the

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

¹⁶ See Electronic Recordkeeping by Investment Companies and Investment Advisers, Investment Advisers Act Release No. 1945 (May 24, 2001) 66 FR 29224 (May 30, 2001).

protections of the Advisers Act are intended to apply equally to retail investor clients of both large and small firms. 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 will be incompatible with the objectives of the rule and would 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. The retention period will not be affected by the 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 With Persons Outside the Agency

In its release proposing to amend the advertising, cash solicitation, and recordkeeping

rules, Commission requested public comment on the effect of information collections under these amendments. The Commission has not yet received any comments addressing the impact of the information collections.

The Commission and the staff of the Division of Investment Management also 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.

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.]

12. Burden of Information Collection

The approved annual aggregate burden for rule 204-2 is currently 2,435,364 hours, with a total annual aggregate monetized cost burden of approximately \$154,304,663, based on an

estimate of 13,299 registered advisers, or 183 hours per registered adviser.¹⁷ Based on Form ADV filings, as of September 30, 2019, 13,463 investment advisers were registered with the Commission. For the proposed recordkeeping amendments that correspond to proposed changes to the advertising rule, including the expanded definition of “advertisement,” we estimate that the proposed amendments would result in an increase in the collection of information burden estimate by 10 hours for each of the estimated 13,463 registered advisers (inclusive of the additional hours required for half of these advisers to also retain a copy of any questionnaire or survey used in the preparation of a third-party rating included or appearing in any advertisement).

For the proposed recordkeeping amendments that correspond to proposed changes to the solicitation rule, we estimate that the proposed amendments would result in a collection of information burden estimate of 1.5 hours¹⁸ for each of the estimated 6,432 registered investment advisers that we estimate would be subject to the solicitation rule.¹⁹ We therefore estimate that the proposed amendments to both rules would result in an aggregate increase in the collection of

¹⁷ See Form ADV and Investment Advisers Act Rules, Final Rule, Release No. IA-4509 (Aug. 25, 2016) [81 FR 60418 (Sept. 1, 2016)], at 81 FR 60454-55 (“2016 Form ADV Paperwork Reduction Analysis”). There were recent revisions to the collection of information for rule 204-2 and Form ADV as a result of the following rulemakings: Form CRS Relationship Summary; Amendments to Form ADV, Release No. IA-5247 (June 5, 2019) [84 FR 33492 (Jul. 12, 2019)]; and Regulation Best Interest, Release No. 34-86031 (June 5, 2019) [84 FR 39178 (Aug. 9, 2019)].

¹⁸ This would be for advisers that would be subject to the solicitation rule, as proposed to be amended, and the corresponding amended recordkeeping requirements. We recognize that not all advisers that would be subject to the solicitation rule would be subject to all of the recordkeeping requirements related to the solicitation rule. For example, we estimate that only a few advisers would use nonprofit programs under the proposed solicitation rule and be subject to the corresponding books and records rule related to nonprofit programs. However, for purposes of the PRA, we are estimating that all advisers that would use the proposed solicitation rule would incur an estimated 1.5 hours in complying with the recordkeeping requirements related to the solicitation rule.

¹⁹ See Release No. IA-5407, *supra* note 4 at 410-414 (discussing the number of respondents that we estimate would be subject to proposed amended solicitation rule).

information burden estimate by 10.7 hours for each of the estimated 13,463 registered advisers, resulting in a total of 193.7 hours per adviser.²⁰ This would yield an annual estimated aggregate burden of 2,607,783 hours under amended rule 204-2 for all registered advisers,²¹ for a monetized cost of \$165,229,131.

The table below provides a summary of the annual burden hours.

²⁰ 10 hours (advertising rule for all advisers) + 0.7 hours (solicitation rule for 6,432 advisers [1.5 hours x 47.8%]) = 10.7 hours.

²¹ 13,463 registered investment advisers x 193.7 hours = 2,607,783 hours.

Summary of Annual Responses, Burden Hours, and Burden Hour Costs Estimates for Rule 204-2

IC	Rule 204-2 under the Investment Advisers Act of 1940	Annual No. of Responses			Annual Time Burden (Hrs.)			Monetized Time Burden (\$)		
		<i>Previously approved</i>	<i>Requested Change Due to New Statute</i>	<i>Total</i>	<i>Previously approved</i>	<i>Requested Change Due to New Statute</i>	<i>Total</i>	<i>Previously approved</i>	<i>Requested Change Due to New Statute</i>	<i>Total</i>
IC1	Recordkeeping and Record retention	13,299	164	13,469	2,435,364	172,419	2,607,783	154,304,664	10,924,467	165,229,131
Total for IC		13,299	164	13,463	2,435,364	172,419	2,607,783	154,304,664	10,924,467	165,229,131

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 2,435,364 hours per year to 2,607,783 hours per year and an increase from \$154,304,664 per year to \$165,229,131 in monetized cost,²² because of the amendments to rule 204-2. This represents an increase of 235,573²³ annual aggregate hours in the hour burden and an annual increase of \$10,924,467²⁴ from the currently approved total aggregate monetized cost for rule 204-2. These increases are attributable to a larger registered investment adviser population since the most recent approval and adjustments for inflation, as well as the rule 204-2 amendments relating to advertising and solicitation.

16. Information Collection Planned for Statistical Purposes

None.

17. Approval to Omit OMB Expiration Date

Not Applicable.

18. Exceptions to Certification Statement for Paperwork Reduction Act

Submission

Not Applicable.

²² $\$95,588,191 + \$58,716,473 = \$154,304,664$.

²³ $2,607,783 \text{ hours} - 2,435,364 \text{ hours} = 172,419 \text{ hours}$.

²⁴ $\$165,229,131 - \$154,304,664 = \$10,924,767$.

B. COLLECTION OF INFORMATION EMPLOYING STATISTICAL METHODS

Not applicable.