

SUPPORTING STATEMENT
RULE 2a-5

A. JUSTIFICATION

1. Necessity for the Information Collection

Section 2(a)(41) of the Investment Company Act of 1940 (“Investment Company Act”)¹ requires funds to value their portfolio investments using the market value of their portfolio securities when market quotations for those securities are “readily available,” and, when a market quotation for a portfolio security is not readily available, by using the fair value of that security, as determined in good faith by the fund’s board.² The aggregate value of a fund’s investments is the primary determinant of the fund’s net asset value (“NAV”), which for many funds determines the price at which their shares are offered and redeemed (or repurchased).³ Accordingly, proper valuation, among other things, promotes the purchase and sale of fund shares at fair prices, and helps to avoid dilution of shareholder interests.⁴

On December 3, 2020, the Commission issued a release adopting new rule 2a-5, which will provide requirements for determining in good faith the fair value of the investments of a registered investment company or companies that have elected to be treated as business development companies under the Investment Company Act (“BDCs” and, collectively, “funds”)

¹ 15 U.S.C. 80a 1 et seq.

² 15 U.S.C. 80a-2(a)(41). *See also* 17 CFR 270.2a-4.

³ *See* 15 U.S.C. 80a-22(c) and 23(c). *See also* 17 CFR 270.22c-1(a).

⁴ *See* Investment Company Liquidity Risk Management Programs, Investment Company Act Release No. 32315 (Oct. 13, 2016) (“Liquidity Risk Management Release”) (adopting rule 22e-4 under the Investment Company Act and noting “the risk of shareholder dilution associated with improper fund pricing”). *See generally* Investment Trusts and Investment Companies: Hearings on S. 3580 Before a Subcomm. of the Senate Comm. on Banking and Currency, 76th Cong., 3d Sess. 136-38 (1940) (discussing the effect of dilution on fund shareholders).

for purposes of section 2(a)(41) of the Investment Company Act and rule 2a-4 thereunder.⁵

Under the final rule, fair value as determined in good faith will require assessing and managing material risks associated with fair value determinations; selecting, applying, and testing fair value methodologies; and overseeing and evaluating any pricing services used. The final rule also permits a fund's board to designate a "valuation designee" to perform fair value determinations. The valuation designee can be the adviser of the fund or an officer of an internally managed fund.⁶ When a board designates the performance of determinations of fair value to a valuation designee for some or all of the fund's investments under the final rule, the final rule requires the board to oversee the valuation designee's performance of fair value determinations. To facilitate such oversight, the final rule also includes certain reporting and other requirements.⁷ As relevant here, the final rule will require, if the board designates performance of fair value determinations to a valuation designee, that the valuation designee report to the board in both periodic and as needed reports on a per-fund basis.⁸

Compliance with rule 2a-5 will be mandatory for any fund that would need to determine fair value under the Act. To the extent that records will be required to be created and maintained under the rule are provided to the Commission in connection with examinations or investigations, such information would be kept confidential subject to the provisions of applicable law.

⁵ See Good Faith Determinations of Fair Value, Investment Company Act Release No. 34128 (Dec. 7, 2020) ("Adopting Release").

⁶ Rule 2a-5(e)(4).

⁷ Rule 2a-5(b).

⁸ Rule 2a-5(b).

2. Purpose and Use of the Information Collection

The purpose of the information collection requirement in rule 2a-5 is to facilitate the board's ability to oversee effectively the adviser's fair value determinations and satisfy the board's obligation under the Act.

3. Consideration Given to Information Technology

The information collected under the rule would not be submitted to the Commission. The proposed rule does not stipulate any particular method for communicating or preserving the information collected. The Electronic Signatures in Global and National Commerce Act⁹ and the conforming amendments to rules under the Investment Company Act permit funds to maintain records electronically.

4. Duplication

The Commission is not aware of any duplicate reporting requirements concerning rule 2a-5.

5. Effects on Small Entities

The Commission reviews all rules periodically, as required by the Regulatory Flexibility Act (5 U.S.C. 601 *et seq.*), to identify methods to minimize recordkeeping or reporting requirements affecting small businesses. The requirements of rule 2a-5 do not distinguish between small entities and larger entities. The burden on smaller entities may be greater than for larger entities. There are different factors that will affect whether a smaller fund incurs costs related to this requirement that are on the higher or lower end of the estimated range. For example, smaller funds – and more specifically, smaller funds that are not part of a fund complex

⁹ P.L. 106-229, 114 Stat. 464 (June 30, 2000).

– may not have an advisory agreement that has a reporting mechanism that meets all the elements that will be required under the final rule. Also, while larger funds or funds that are part of a large fund complex may incur higher costs, via increased advisory fees for valuation designees to take on this responsibility on behalf of such funds, related to this requirement in absolute terms relative to a smaller fund or a fund that is part of a smaller fund complex, a smaller fund may find it more costly, per dollar managed, to comply with the final requirement because it will not be able to benefit from a larger fund complex’s economies of scale.¹⁰

We do not believe that exempting small funds from the provisions in the rule would permit us to achieve our stated objectives, principally to protect investors from improper valuations. Further, the board reporting of the rule only affects fund boards that designate a valuation designee to perform fair value determinations, and, therefore, the rule will require funds to comply with this specific requirement only if the boards designated responsibilities to a valuation designee. However, we expect that most funds holding securities that must be fair valued will do so. Therefore if a board to a small entity does not do this and instead performs its statutory function directly, then the small entity would not be subject to this provisions of the rule.

6. Consequences of Not Conducting Collection

Less frequent information collection would be incompatible with the objectives of rule 2a-5. The requirements of the rule are necessary to facilitate the board’s ability to oversee effectively the adviser’s fair value determinations and satisfy the board’s obligation under the Act.

¹⁰ See Adopting Release, *supra* footnote 5, at section III.C.1.

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

Not applicable.

8. Consultations Outside the Agency

Before adopting rule 2a-5, the Commission solicited and evaluated public comment on the collection of information requirement. Specifically, the public was given the opportunity to comment on the Commission's estimates for the burdens of rule 2a-5 as proposed. While comments were received from filers, investors and other market participants, and were considered by the Commission as discussed in the Adopting Release, most of these did not relate to the proposed burden estimates for rule 2a-5. However, specific to the proposed collection, some commenters argued that the burden estimates as proposed for this requirement were too low, arguing in particular that the cost to produce the items that would have been required on a quarterly basis as part of the proposed periodic reporting requirements would be in excess of what we had assumed due to burdens of both creating these reports and of reviewing them on the part of the board. While we clarified in the Adopting Release that certain reporting that commenters thought was suggested in the proposed rule will not be required in the final rule and made other changes to address these concerns,¹¹ we are nonetheless increasing our estimates for the final rule in consideration of these comments. We also have corrected certain estimates, specifically to include an initial burden as we believe the final rule will impose some start-up burdens and to update the wage rates for relevant personnel. We have also updated the estimated number of respondents based upon updated data.¹² Lastly, we increased the estimated amount of

¹¹ See Adopting Release, *supra* footnote 5, at Section II.B.2.

¹² See Adopting Release, *supra* footnote 5, at n. **Error! Bookmark not defined. - Error! Bookmark not defined.** and accompanying text.

external cost burden to include costs relating to both legal and accounting services as the proposed estimate only estimated external costs relating to legal expenses.

In addition, the Commission and 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 staff with a means of ascertaining and acting upon paperwork burdens that may confront the industry.

9. Payment or Gift

Not applicable.

10. Confidentiality

Not applicable.

11. Sensitive Questions

Not applicable.

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 (44 U.S.C. 3501 et seq.) and are not derived from a comprehensive or even representative survey or study of the cost of Commission rules and forms.

The table below summarizes the estimated burdens associated with the collection of information from the proposal and the final PRA estimates for internal and external burdens associated with rule 2a-5.¹³

Rule 2a-5 PRA Estimates Table

	Initial internal burden hours	Internal annual burden hours ¹		Wage rate ²	Internal time costs	Initial external cost burden	Annual external cost burden
PROPOSED ESTIMATES							
	0 hours	8 hours	×	\$329 (senior manager)	\$2,632		
Adviser written reports	0 hours	1 hour	×	\$17,860 (combined rate for 4 directors)	\$17,860	\$2,000	\$2,000
	0 hours	1 hour	×	\$365 (compliance attorney)	\$365		
Total annual burden per fund		10 hours			\$20,857	\$2,000	\$2,000
Number of funds		× 9,501			× 9,501	× 9,501	× 9,501
Total proposed burden		95,010 hours			\$198,162,357	\$19,002,000	\$19,002,000
FINAL ESTIMATES							
	12 hours	24 hours	×	\$368 (senior operations manager)	\$8,832		
Valuation designee written reports	1.5 hours	2 hours	×	\$4,770 (directors) ³	\$9,540	\$3,180	\$3,180
	6 hours	8 hours	×	\$368 (compliance attorney)	\$2,944		

¹³ The Commission's estimates of the relevant wage rates in the tables below are based on salary information for the securities industry compiled by the Securities Industry and Financial Markets Association's Office Salaries in the Securities Industry 2013. The estimated wage figures are modified by Commission staff to account for an 1,800-hour work-year and inflation, and multiplied by 5.35 for professional staff and 2.93 for clerical staff to account for bonuses, firm size, employee benefits, overhead, and adjusted to account for the effects of inflation. See Securities Industry and Financial Markets Association, Report on Management & Professional Earnings in the Securities Industry 2013 ("SIFMA Report").

Total annual burden per fund	34 hours	\$21,316	\$3,180	\$3,180
Number of funds	× 9,335	× 9,335	× 9,335	× 9,335
Total final burden	317,390 hours	\$198,984,860	\$29,685,300	\$29,685,300
TOTAL ESTIMATED BURDENS FOR BOARD REPORTING				
Proposed burden estimates	95,010 hours	\$198,162,357	\$19,002,000	\$19,002,000
Proposed total respondents	9,501			
Revised burden estimates	317,390 hours	\$198,984,860	\$29,685,300	\$29,685,300
Revised total respondents	9,335			

Notes:

1. These estimates include initial burden estimates annualized over three years.
2. See SIFMA Report, *supra* footnote 13.
3. This wage rate is not from the SIFMA Report but is a staff estimate. It is a combined cost for the entire board (not a per board member cost). This estimate assumes an average of 9 board members per board.
4. This estimated burden is based on the estimated wage rate of \$489/hour, for 4 hours, for outside legal services and of \$306/hour, for 4 hours, for outside accounting services. See *supra* footnote 13.

13. Cost to Respondents

Cost burden is the cost of goods and services purchased to collect the information required under rule 2a-5. The cost burden does not include the hour burden discussed in Item 12 above. As outlined in the table above, we estimate the total external cost burden to comply with rule 2a-5 to be \$29,685,300.

14. Cost to the Federal Government

The rule will not entail any costs on the federal government.

15. Changes in Burden

Not applicable. This is the first request for approval of a collection of information for this proposed rule.

16. Information Collection Planned for Statistical Purposes

Not applicable.

17. Approval to Omit OMB Expiration Date

Not applicable.

18. Exceptions to Certification Statement for Paperwork Reduction Act

Submission

Not applicable.

B. COLLECTION OF INFORMATION EMPLOYING STATISTICAL METHODS

Not applicable.