

SUPPORTING STATEMENT
For the Paperwork Reduction Act Information Collection Submission for
Rule 38a-1

A. JUSTIFICATION

1. Necessity for the Information Collection

On February 9, 2022, the Commission proposed rules related to cybersecurity risk management for registered investment advisers, as well as for registered investment companies and business development companies (together, “funds”), and also proposed amendments to certain rules that govern investment adviser and fund disclosures under the Investment Advisers Act of 1940 and the Investment Company Act of 1940 (“Investment Company Act”).¹ The proposed rules and amendments are designed to enhance the cybersecurity hygiene and preparedness of advisers and funds and improve their resilience against cybersecurity threats and attacks, while also improving the cybersecurity-related disclosures advisory clients and fund investors receive and enhancing the Commission’s ability to oversee advisers and funds and assess systemic risks.

The Commission proposed new rule 38a-2 under the Investment Company Act (“rule 38a-2”) to require funds to adopt and implement written policies and procedures reasonably designed to address cybersecurity risks. Proposed rule 38a-2 enumerates certain general elements that advisers and funds would be required to address in their cybersecurity policies and procedures including risk assessment, user security and access, information protection, threat and

¹ 15 U.S.C. 80a-1 *et seq.*; Cybersecurity Risk Governance and Incident Disclosure, Securities Act Release No. 11028 (Feb. 9, 2022) available at <https://www.sec.gov/rules/proposed/2022/33-11028.pdf> (“Cybersecurity Risk Governance and Incident Disclosure Proposal”).

vulnerability management, and cybersecurity incident response and recovery. Under the rule, a fund would also, at least annually: (1) review and assess the design and effectiveness of those policies and procedures; and (2) prepare and provide to the fund's board a written report. It would also require a fund's board of directors, including a majority of its independent directors, initially to approve the fund's cybersecurity policies and procedures, as well as to review the annual written report. Finally, a fund would need to keep records related to the policies and procedures, written reports, annual review, and any reports provided to the Commission.

2. Purpose and Use of the Information Collection

The purpose of the information collection requirements in proposed rule 38a-2 is to ensure that funds maintain comprehensive, written internal compliance programs that promote cybersecurity hygiene and preparedness. The information collections also would assist the Commission's examination staff in assessing the adequacy of funds' compliance programs.

3. Consideration Given to Information Technology

Proposed rule 38a-2 does not require the reporting of any information or the filing of any documents with the Commission. Rule 38a-2 would require that a fund maintain: (1) a copy of its cybersecurity policies and procedures that are in effect, or at any time within the last five years were in effect; (2) copies of written reports provided to its board; (3) records documenting the fund's annual review of its cybersecurity policies and procedures; (4) any report of a significant fund cybersecurity incident provided to the Commission by its adviser; (5) records documenting the occurrence of any cybersecurity incident, including any records related to any response and recovery from such an incident; and (6) records documenting the fund's cybersecurity risk assessment. These records would have to be maintained for five years, the first two years in an easily accessible place. The Electronic Signatures in Global and National

Commerce Act² and the conforming amendments to rules under the Investment Company Act permit funds to maintain records electronically.

4. Duplication

Proposed rule 38a-2 would impose a requirement that funds have in place written compliance policies and procedures on cybersecurity. Funds also are subject to certain requirements elsewhere in the federal securities laws that require them to maintain written policies and procedures, including rule 38a-1 under the Act. The staff believes, however, that any duplication of requirements is limited, as rule 38a-2 would require policies and procedures specific to cybersecurity. Moreover, rule 38a-2 would not require funds to maintain duplicate copies of records covered by these more targeted requirements, and a firm's compliance policies and procedures are not required to be maintained in a single location. The staff believes, therefore, that any duplication of regulatory requirements would not impose significant additional costs on funds. The Commission periodically evaluates rule-based recordkeeping requirements for duplication and reevaluates them whenever it proposes a rule or a change in a rule.

5. Effect on Small Entities

Funds, regardless of their size, are subject to the requirements of proposed rule 38a-2. Effective cybersecurity risk management is essential for firms of all sizes. Rule 38a-2 would afford funds the flexibility to tailor their cybersecurity risk program to the nature of their business. Small firms, which generally have less complex and more limited operations, likely need less extensive cybersecurity risk programs than their larger counterparts. Thus, rule 38a-2

² P.L. 106-229, 114 Stat. 464 (June 30, 2000).

would not inappropriately burden small entities. The Commission believes that it could not adjust the rule to lessen the burden on small entities of complying with the rule without jeopardizing the interests of investors in small funds. 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 proposed rule 38a-2. The annual reviews that would be required under rule 38a-2 are integral to detecting and correcting any gaps in the program before irrevocable or widespread harm is inflicted upon investors, and extending the time between reviews would increase the likelihood that such harm could go unchecked.

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

Proposed rule 38a-2 would require funds and advisers to maintain their internal compliance policies and procedures and documents related to the annual review of those policies and procedures for at least five years. Although this period exceeds the three-year guideline for most kinds of records under 5 CFR 1320.5(d)(2)(iv), the staff believes that this is warranted because the rule would 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

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 staff with a means of ascertaining and acting upon paperwork burdens confronting the industry. In addition, the Commission has requested public comment on proposed rule 38a-2, including the collection of information requirements resulting from the proposed rule. Before adopting these amendments, the Commission will receive and evaluate public comments on the proposed amendments and their associated collection of information requirements.

9. Payment or Gift

No payment or gift to respondents was provided.

10. Confidentiality

If information collected pursuant to proposed rule 38a-2 is reviewed by the Commission's examination staff, it would be accorded the same level of confidentiality accorded to other responses provided to the Commission in the context of its examination and oversight program.

11. Sensitive Questions

No information of a sensitive nature is required under this collection of information. The information collection does not collect personally 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 1995³ and are not derived from a comprehensive or even representative survey or study of the costs of Commission rules.

Proposed rule 38a-2 would require a fund to adopt and implement written policies and procedures reasonably designed to address cybersecurity risks. Each requirement to disclose information, offer to provide information, or to adopt policies and procedures constitutes a collection of information requirement under the Paperwork Reduction Act. The respondents to proposed rule 38a-2 would be registered investment companies and business development companies. We estimate that 14,749 funds would be subject to these proposed rule requirements.⁴ The collections of information associated with these requirements would be mandatory, and responses provided to the Commission in the context of its examination and oversight program concerning rule 38a-2 would be kept confidential subject to the provisions of applicable law. The table below summarizes the initial and ongoing annual burden and cost estimates associated with the proposed rule.

Table 1: Burden Estimates for Rule 38a-2

	Internal initial burden hours	Internal annual burden hours ¹	Wage rate ²	Internal time costs	Annual external cost burden
PROPOSED RULE 38A-2 ESTIMATES					
Adopting and implementing policies and procedures	60 hours	25 hours ³	\$425 (blended rate for compliance attorney and assistant general counsel)	\$10,625	\$5,952 ⁴

³ 44 U.S.C. 3501 et seq.

⁴ As of December 2020, we estimate 14,654 registered investment companies and 95 BDCs (totaling 14,749 funds).

			\$425		
Annual review of policies and procedures and report	9 hours	6 hours ⁵	(blended rate for compliance attorney and assistant general counsel)	\$2,550	\$992 ⁶
			\$356		
Recordkeeping	1 hour	1 hour	(blended rate for compliance attorney and senior programmer)	\$356	\$0
Total new annual burden per fund		32 hours		\$13,531	\$6,944
Number of funds		× 14,749 funds ⁷		× 14,749 funds	7,375 ⁸
Total new annual aggregate burden		471,968 hours		\$199,568,719	\$51,212,000

Notes:

1. Includes initial burden estimates annualized over a 3-year period.
2. The Commission's estimates of the relevant wage rates are based on the SIFMA Wage Report. The estimated figures are modified by firm size, employee benefits, overhead, and adjusted to account for the effects of inflation.
3. Includes initial burden estimates annualized over a three-year period, plus 5 ongoing annual burden hours. The estimate of 25 hours is based on the following calculation: ((60 initial hours / 3) + 5 additional ongoing burden hours) = 25 hours.
4. This estimated burden is based on the estimated wage rate of \$496/hour, for 12 hours, for outside legal services. The Commission's estimates of the relevant wage rates for external time costs, such as outside legal services, take into account staff experience, a variety of sources including general information websites, and adjustments for inflation.
5. Includes initial burden estimates annualized over a three-year period, plus 8 ongoing annual burden hours. The estimate of 6 hours is based on the following calculation: ((9 initial hours / 3) + 3 additional ongoing burden hours) = 6 hours.
6. This estimated burden is based on the estimated wage rate of \$496/hour, for 2 hours, for outside legal services.
7. Includes all registered investment companies, plus BDCs.
8. We estimate that 50% of funds will use outside legal services for these collections of information. This estimate takes into account that funds may elect to use outside legal services (along with in-house counsel), based on factors such as fund budget and the fund's standard practices for using outside legal services, as well as personnel availability and expertise.

13. Cost to Respondents

Cost burden is the cost of goods and services purchased to meet the requirements of proposed rule 38a-2, such as for the services of outside counsel. The cost burden does not include the hour burden discussed in Item 12 above. Estimates are based on the Commission's experience.

As summarized in Table 1 above, Commission staff estimates that the annual cost of outside services associated with rule 38a-2 would be approximately \$6,944 per fund and the total annual external cost burden for rule 38a-2 would be \$51,212,000.⁵

14. Cost to the Federal Government

Proposed rule 38a-2 would not impose a cost on the federal government. Rule 38a-2 would not require funds to file any documents with the Commission. However, the Commission staff may records produced pursuant to the rule in order to assist the Commission in carrying out its examination and oversight program.

15. Change in Burden

New collection.

16. Information Collection Planned for Statistical Purposes

The results of any information collection will not be published.

17. Approval to Omit OMB Expiration Date

The Commission is not seeking approval to omit 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. COLLECTION OF INFORMATION EMPLOYING STATISTICAL METHODS

The collection of information will not employ statistical methods.

⁵ This estimate is based on the following calculation: 7,375 funds x \$6,944 = \$51,212,000.