

**SUPPORTING STATEMENT**

**For the Paperwork Reduction Act Information Collection Submission for  
Amendments to Rule 204-3 under the Investment Advisers Act of 1940**

**A. JUSTIFICATION**

**1. Necessity for the Information Collection**

Rule 204-3, the “brochure rule,” requires an investment adviser to deliver its brochure and brochure supplements to its new clients or prospective clients before or at the start of the advisory relationship and to deliver annually thereafter the full updated brochure or a summary of material changes to its brochure. The rule also requires that advisers deliver an amended brochure or brochure supplement (or just a statement describing the amendment) to clients only when disciplinary information in the brochure or supplement becomes materially inaccurate. The brochure assists the client in determining whether to retain, or continue employing, the adviser. Advisers registered with the Commission are required to prepare and electronically file firm brochures through the Investment Adviser Registration Depository (“IARD”).

Rule 204-3 contains a collection of information titled “Rule 204-3 under the Investment Advisers Act of 1940,” found at 17 CFR 275.204-3, which is mandatory. Its currently approved OMB control number is 3235-0047. An agency may not sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid OMB control number. The likely respondents to this information collection are investment advisers registered or required to be registered with the Commission.

The brochure rule collection of information is necessary for several reasons. It enables the client or prospective client to evaluate the adviser's background and qualifications, and to determine whether the adviser's services and practices are appropriate for that client. It informs the client of the nature of the adviser's business, which may inform or limit the client's rights under the advisory contract. It apprises the client of situations in which the interests of the adviser may potentially be adverse to or in conflict with those of the client. Under some circumstances, it enables the client to consider the financial condition of the adviser in deciding whether to entrust funds or securities to the custody of the adviser or whether to pay large advisory fees in advance. The information that rule 204-3 requires to be contained in the brochure is also used by the Commission and staff in its enforcement, regulatory, and examination programs. Responses are not kept confidential.

On February 9, 2022, the Commission proposed rules related to cybersecurity risk management for registered investment advisers, registered investment companies, and business development companies as well as amendments to certain rules that govern investment adviser and fund disclosures under the Advisers Act and the Investment Company Act of 1940.<sup>1</sup> The Commission proposed amendments to rule 204-3 would require an adviser to deliver interim brochure amendments promptly to existing clients if the adviser adds disclosure of a cybersecurity incident to its brochure or materially revises information already disclosed in its brochure

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<sup>1</sup> 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").

about such an incident. We believe that requiring an adviser to deliver the brochure amendment promptly would enhance investor protection by enabling clients to take protective or remedial measures to the extent appropriate. It would also assist investors in determining whether their engagement of that particular adviser remains appropriate and consistent with their investment objectives.

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

Investors need accurate information about an investment adviser and its practices in order to determine whether to retain, or to continue to employ, that adviser. The Commission and staff need the information in its enforcement, regulatory, and examination programs.

## **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, has not changed. The Commission currently permits advisers to satisfy their obligations under this collection of information by delivering Part 2 of Form ADV electronically with client consent.<sup>2</sup>

## **4. Duplication**

The collection of information requirements are not duplicated elsewhere.

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<sup>2</sup> See Use of Electronic Media by Broker-Dealers, Transfer Agents, and Investment Advisers for Delivery of Information, Investment Advisers Act Release No. 1562 (May 9, 1996) (61 FR 24644 (May 15, 1996)) (publishing Commission interpretive guidance with respect to use of electronic media to fulfill investment advisers' disclosure delivery obligations).

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

The requirements of rule 204-3 are the same for all investment advisers registered with the Commission, including those that are small entities.<sup>3</sup> Some small advisers may have lesser burdens under rule 204-3. This is because small advisers usually have less complicated business practices, fewer employees, and fewer clients, and therefore their brochures and brochure supplements would be shorter, and would be delivered to fewer clients.

## **6. Consequences of Not Conducting Collection**

The collection of information required by the rule is necessary to protect investors by providing clients and potential clients with information about the adviser, its business, and its conflicts of interest. The consequences of not collecting this information would be that clients and prospective clients may not have the information they need in order to evaluate the adviser's business practices and to determine whether to select or retain that adviser and, if selected or retained, how to manage that relationship.

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

The collection of information imposes no additional requirements regarding record retention.

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<sup>3</sup> Under Advisers Act rule 0-7, for purposes of the Regulatory Flexibility Act an investment adviser generally is a small entity if it: (i) has assets under management of less than \$25 million; (ii) did not have total assets of \$5 million or more on the last day of its most recent fiscal year; and (iii) does not control, is not controlled by, and is not under common control with another investment adviser that has assets under management of \$25 million or more, or any person (other than a natural person) that had total assets of \$5 million or more on the last day of its most recent fiscal year.

## **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 adviser profession 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. In addition, the Commission has requested public comment on the proposed amendments, including the collection of information requirements resulting from the proposed amendments. 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**

None.

## **10. Confidentiality**

The information collected pursuant to rule 204-3 is by delivery of brochures and brochure supplements to advisory clients and prospective clients. These disclosures are not kept confidential.

## **11. Sensitive Questions**

No Personally Identifiable Information (PII) collected/Not applicable.

## **12. Estimate of Hour and Cost 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>4</sup> and are not derived from a

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<sup>4</sup> 44 U.S.C. 3501 *et seq.*

comprehensive or even representative survey or study of the cost of Commission rules and forms.

The respondents to this collection of information are investment advisers registered or required to be registered with the Commission. As noted above, the collection of this information is mandatory for all registered advisers. Responses are not kept confidential. As of October 31, 2021, there were 14,774 registered advisers that would be subject to this brochure requirement. The table below summarizes the initial and ongoing annual burden and cost estimates associated with the proposed amendments to rule 204-3.

*Table 1: Rule 204-3 PRA Estimates*

	Internal initial burden hours	Internal annual burden hours		Wage rate	Internal time costs	Annual external cost burden
<b>PROPOSED ESTIMATES</b>						
Annual delivery of brochure	1.66 hours <sup>1</sup>	1.66 hours	×	\$64 (general clerk)	\$106.24	\$0
Interim delivery of updates to disciplinary action <sup>2</sup>	0.1 hour <sup>3</sup>	0.1 hour	×	\$64 (general clerk)	\$6.40	\$0
Interim delivery of updates to cybersecurity incidents	0.1 hour <sup>4</sup>	0.1 hour	x	\$64 (general clerk)	\$6.40	\$0
Supplement tracking systems <sup>5</sup>	200 hours <sup>6</sup>	200 hours	x	\$64 (general clerk)	\$12,800	\$0
Total new annual burden per adviser		201.86 hours			\$12,919.04	
Number of advisers		×14,774			×14,774	
Total new aggregate annual burden		2,982,279.64 hours			\$190,865,897	

Notes:

1. We continue to estimate that, with a bulk mailing, an adviser will require no more than 0.02 hours to send the adviser’s brochure or summary of material changes to each client, or an annual burden of 1.66 hours per adviser. (0.02 hours per client x 83 clients per adviser based on IARD data as of October 31, 2021) = approximately 1.66 hours per adviser. We note that the burden for preparing brochures is already incorporated into a separate burden estimate for Form ADV. We expect that most advisers will make their annual delivery as part of a mailing of an account statement or other periodic report they already make to clients; therefore, we estimate that the additional burden will be adding a few pages to the mailing.
2. See approved rule 204-3 PRA.
3. This is the previously approved burden estimate for interim delivery of updates to disciplinary action on Form ADV. We are not changing this estimate.
4. This relates only to the amount of time it will take advisers to deliver interim updates to clients, as required by the proposed rule amendments. The burden for preparing interim updates is already incorporated into a separate burden estimate for Form ADV. This mailing may not be included with a mailing of a statement or other periodic report; therefore, we estimate that it will take slightly more time to deliver interim updates than to deliver the annual brochure or summary of material changes.
5. We estimate that large advisers will need to design and implement systems to track changes in supervised persons providing investment advice to particular clients. We do not expect that such systems will be necessary for small advisers or medium advisers. For purposes of the estimates in this section, we have categorized small advisers as those with 10 or fewer employees, medium-sized advisers as those with between 11 and 1,000 employees, and large advisers as those with over 1,000 employees. According to IARD data, only 1.70% of medium advisers report in response to Form ADV, Part 1A, Item 5.B.(1) that more than 250 employees perform investment advisory functions.
6. See approved rule 204-3 PRA. This includes estimated time for large advisers to design and implement systems to track that the right supplements are delivered to the right clients as personnel providing investment advice to those clients change.

### 13. Cost to Respondents

Cost burden is the cost of goods and services purchased to meet the requirements of rule 204-3, 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, we estimate that the annual external cost associated with the proposed amendments to rule 204-3 is \$0.

**14. Cost to the Federal Government**

There are no costs to the government directly attributable to rule 204-3.

**15. Change in Burden**

The estimated total burden hours has increased from 49,090 to 2,982,279.64 hours per year in aggregate, representing an increase of 2,933,189.64 hours per year from the currently approved burden. The changes are due to proposed amendments, updated data, and using a new methodology for certain estimates. The estimated number of annual responses has increased from approximately 13,382 to 14,774, representing an increase of 1,392 responses from the currently approved number of responses. This revised estimate is due to, among other things, new information on the number of SEC-registered investment advisers that we obtained from Form ADVs filed through the IARD as of October 31, 2021. The external cost burden associated with rule 204-3 (\$0) has not changed.

**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. COLLECTIONS OF INFORMATION EMPLOYING STATISTICAL METHODS**

Not applicable.