

**SUPPORTING STATEMENT**  
**For the Paperwork Reduction Act Information Collection Submission for**  
**Rule 12d3-1**

**A. JUSTIFICATION**

**1. Necessity for the Information Collection**

Section 12(d)(3) of the Investment Company Act of 1940 (15 U.S.C. 80a-1 *et seq.*) (“Investment Company Act”) generally prohibits a registered investment company (“fund”) and companies controlled by the fund from purchasing securities issued by a registered investment adviser, broker, dealer, or underwriter (“securities-related businesses”).<sup>1</sup> Rule 12d3-1 (17 CFR 270.12d3-1) permits a fund to invest up to five percent of its assets in securities of an issuer deriving more than fifteen percent of its gross revenues from securities-related businesses, but a fund may not rely on rule 12d3-1 to acquire securities of its own investment adviser or any affiliated person of its own investment adviser.<sup>2</sup>

A fund may, however, rely on an exemption in rule 12d3-1 to acquire securities issued by its subadvisers in circumstances in which the subadviser would have little ability to take advantage of the fund, because it is not in a position to direct the fund’s securities purchases. This exemption in rule 12d3-1 is available if: (i) the subadviser is not, and is not an affiliated person of, an investment adviser that provides advice with respect to the portion of the fund that is acquiring the securities; and (ii) the advisory contracts of the subadviser, and any subadviser that is advising the purchasing portion of the fund, prohibit them from consulting with each other concerning securities transactions of the fund, and limit their responsibility in providing advice

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<sup>1</sup> 15. U.S.C. 80a-17(d)(3).<sup>2</sup> See 17 CFR 270.12d3-1(b); 17 CFR 270.12d3-1(c)(3).

<sup>2</sup> See 17 CFR 270.12d3-1(b); 17 CFR 270.12d3-1(c)(3).

to providing advice with respect to discrete portions of the fund's portfolio.<sup>3</sup>

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

The rule requires funds to amend their subadvisory contracts before they can rely on rule 12d3-1's exemption to ensure that the subadviser that engages in the transaction does not influence the fund's investment decision to engage in the transaction.

## **3. Consideration Given to Information Technology**

To the extent the rule includes recordkeeping requirements, the Electronic Signatures in Global and National Commerce Act<sup>4</sup> and the conforming amendments to recordkeeping rules under the Investment Company Act permit funds to maintain records electronically.

## **4. Duplication**

The requirement regarding limitations in the subadviser's contracts is similar to conditions in exemptive rules 10f-3<sup>5</sup> (permitting, under certain conditions, a fund to purchase securities from underwriting syndicates whose members include affiliated persons of the purchasing fund), 17a-10<sup>6</sup> (permitting a fund's subadviser to enter into certain transactions with their affiliated subadvisers), and 17e-1<sup>7</sup> (governing the receipt of compensation by a broker affiliated with a fund in connection with securities transactions by the fund). To the extent that a fund relies on more than one of these rules, its subadviser may use the same contract language to satisfy the comparable condition in the other rules.

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<sup>3</sup> See 17 CFR 270.270.12d3-1(c)(3).

<sup>4</sup> P.L. 106-229, 114 Stat. 464 (June 30, 2000).

<sup>5</sup> 17 CFR 270.10f-3.

<sup>6</sup> 17 CFR 270.17a-10.

<sup>7</sup> 17 CFR 270.17e-1.

**5. Effect on Small Entities**

Rule 12d3-1's exemptive relief is conditioned upon funds including certain provisions in their advisory contracts to ensure that fund interests are the primary consideration for otherwise prohibited transactions; these conditions apply equally to all funds, including small entities.

**6. Consequences of Not Conducting Collection**

Rule 12d3-1 requires that a fund's subadvisory contract be either initially drafted or amended to qualify for the rule's exemption. This is not a recurring requirement; less frequent collection is not possible.

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

Not applicable. The collection is not inconsistent with 5 CFR 1320.5(d)(2).

**8. Consultation Outside the Agency**

The Commission requested public comment on the collection of information requirements in rule 12d3-1 before it submitted this request for approval to the Office of Management and Budget. The Commission received no comments in response to this request.

More generally, the Commission and the staff at 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 the staff with a means of ascertaining and acting upon paperwork burdens confronting the industry.

**9. Payment or Gift**

Not applicable.

**10. Confidentiality**

Not applicable.

**11. Sensitive Questions**

No information of a sensitive nature, including social security numbers, will be 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 are made solely for the purposes of the Paperwork Reduction Act. The estimates are not derived from a comprehensive or even a representative survey or study of the costs of Commission rules.

The staff believes that all existing funds with subadvisory contracts amended those contracts to comply with the rule following amendments to rule 12d3-1 in 2002 that conditioned certain exemptions upon these contractual alterations, and that after that one-time change, there is no continuing burden for those funds. However, the staff assumes that all newly formed subadvised funds, and funds that enter into new contracts with subadvisers, will incur the one-time burden by amending their contracts to add the terms required by the rule.

Based on an analysis of fund filings, the staff estimates that approximately 285 funds enter into such new subadvisory agreements each year.<sup>8</sup> Based on discussions with industry

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<sup>8</sup> Based on data from Morningstar Direct, as of December 31, 2021, there are 14,344 registered funds (open-end funds, closed-end funds, and exchange-traded funds), 5,582 of which have subadvisory relationships (approximately 39%). 285 new funds were established in 2021 by registrants with subadvisory relationships .

representatives, the staff estimates that it will require approximately 3 attorney hours to draft and execute additional clauses in new subadvisory contracts in order for funds and subadvisers to be able to rely on the exemptions in rule 12d3-1. Because these additional clauses are identical to the clauses that a fund would need to insert in their subadvisory contracts to rely on rules 10f-3, 17a-10, and 17e-1 and because we believe that funds that use one such rule generally use all of these rules, we apportion this 3 hour time burden equally to all four rules. Therefore, we estimate that the burden allocated to rule 12d3-1 for this contract change would be 0.75 hours.<sup>9</sup> Assuming that all 285 funds that enter into new subadvisory contracts each year make the modification to their contract required by the rule, we estimate that the rule's contract modification requirement will result in 214 burden hours annually, with an associated time cost of approximately \$90,950.<sup>10</sup>

**Table 1: Summary of Revised Annual Responses, Burden Hours, and Burden Hour Costs Estimates for Each Information Collection**

Annual No. of Responses			Annual Time Burden (Hrs.)			Cost Burden (\$)		
<i>Previously approved</i>	<i>Requested</i>	<i>Change</i>	<i>Previously approved</i>	<i>Requested</i>	<i>Change</i>	<i>Previously approved</i>	<i>Requested</i>	<i>Change</i>
216	285	69	162	214	52	64,962	90,950	25,988

<sup>9</sup> This estimate is based on the following calculation (3 hours ÷ 4 rules = .75 hours).

<sup>10</sup> These estimates are based on the following calculations: (0.75 hours × 285 funds = 214 burden hours); (\$425 per hour × 214 hours = \$ 90,950 cost). The Commission's estimates concerning the wage rates for attorney time are based on salary information for the securities industry compiled by the Securities Industry and Financial Markets Association. The estimated wage figure is based on published rates for in-house attorneys, modified to account for an 1,800-hour work-year and inflation, and adjusted to account for bonuses, firm size, employee benefits, and overhead, yielding an effective hourly rate of \$425. See Securities Industry and Financial Markets Association, Report on Management & Professional Earnings in the Securities Industry 2013.

**13. Cost to Respondents**

We estimated that there is no cost burden of rule 12d3-1, other than the respondent recordkeeping burden identified in Item 12 of this Supporting Statement. Compliance with the rule is part of customary and usual investment company business practice to ensure compliance with applicable laws and regulations.

**14. Cost to the Federal Government**

The rule does not require anything to be filed with the Commission. Commission staff may, in the course of routine fund inspections, monitor compliance with the rule.

**15. Changes in Burden**

Rule 12d3-1 has a current annual burden of 162 hours and no external costs. We estimate the hour burden associated with rule 12d3-1 has increased to 214 hours since our last burden analysis due to a change in our estimate of the number of funds using subadvisers, for a total increase of 52 burden hours. The external cost burden has not changed.

**16. Information Collection Planned for Statistical Purposes**

The results of any information collected will not be published.

**17. Approval to Omit OMB Expiration Date**

The Commission is not seeking approval to not display the expiration date for OMB approval.

**18. Exceptions to Certification Statement for Paperwork Reduction Act****Submissions**

The Commission is not seeking an exception to the certification statement.

**B. COLLECTIONS OF INFORMATION EMPLOYING STATISTICAL METHODS**

Not applicable.