

SUPPORTING STATEMENT
for the Paperwork Reduction Act New Information Collection Submission for
Rule 15g-9
OMB Control #: 3235-0385

A. JUSTIFICATION

1. Necessity of Information Collection

The Commission adopted Rule 15g-9 (17 CFR 240.15g-9) (“the Rule”) in 1989 pursuant to Section 15(c)(2) of the Securities Exchange Act of 1934 (“Exchange Act”), which authorizes the Commission to promulgate rules that prescribe means reasonably designed to prevent fraudulent, deceptive, or manipulative practices in connection with over-the-counter (“OTC”) transactions.¹ Rule 15g-9 requires broker-dealers to produce a written suitability determination for, and to obtain a written customer agreement to, certain recommended transactions in penny stocks as that term is defined in Section 3(a)(51) of the Exchange Act and Rule 3a51-1 thereunder. The Rule is necessary to prevent the indiscriminate use by broker-dealers of fraudulent, high pressure telephone sales campaigns to sell penny stocks to unsophisticated customers.

The scope of the Rule is limited in order to exclude transactions that are less likely to be subject to abusive, high-pressure sales practices. Application of the Rule is limited to transactions in penny stocks, which generally refer to non-exchange listed OTC equity securities whose issuers do not meet certain financial standards described below. In addition, exemptions are provided for: (1) transactions in which the price of the security is five dollars or more; (2) transactions in which the purchaser is an accredited investor or an established customer of the broker-dealer; (3) transactions that are not recommended by the broker-dealer; and (4) transactions by a broker-dealer who is not a market maker in the penny stock that is the subject of the transaction, and whose sales-related revenue from transactions in penny stocks does not exceed five percent of its total sales-related revenue from transactions in securities.

2. Purpose and Use of Information Collection

The Commission recognizes that only comprehensive action will successfully reduce fraud in the sale of penny stocks, and therefore has undertaken a broad-based program in this area that includes expanded enforcement efforts, a public education program, and regulatory initiatives. In adopting Rule 15g-9, the Commission sought to combat the unscrupulous, high-pressure sales tactics of certain broker-dealers by imposing objective and readily reviewable requirements that discipline the process by which new customers are induced to purchase penny stocks. The requirements were

¹ See Exchange Act Rel. No. 49037, 69 FR at 2538 n. 68 (discussing Exchange Act Rule 15c2-6). Originally adopted as Rule 15c2-6 and thereafter redesignated, the Commission responded to the widespread incidence of misconduct by some broker-dealers in connection with transactions in low-priced securities. Exchange Act Rel. No. 27160, 54 FR at 35468.

intended to assist investors in protecting themselves from fraudulent sales practices, and also to reinforce a broker-dealer's suitability obligations, which are long-standing obligations under self-regulatory organization ("SRO") rules.

An essential aspect of high-pressure "boiler-room" operations is the constant solicitation of new, and often unsophisticated, customers. The Rule reins in this process by establishing account opening procedures that must be followed before penny stocks are recommended to unsophisticated new customers. The procedures are intended to increase the likelihood that a broker-dealer will make an appropriate suitability determination by requiring the broker-dealer to obtain sufficient information concerning the customer, and to consider the customer's previous investment experience, investment objectives, and financial situation.

In addition, the Rule protects investors from fraudulent sales practices in penny stocks in two ways. First, the requirement that the customer agree in writing to penny stock purchases provides the customer with an opportunity to make an investment decision outside of a pressured telephone conversation with a salesperson. Second, the account opening procedures require the broker-dealer to provide a copy of the broker-dealer's suitability determination to the customer prior to the customer's commitment to purchase a penny stock. As a result, the customer has an opportunity to review the determination and decide whether the broker-dealer has made a good faith attempt to consider the customer's financial situation, investment experience, and investment objectives.

The consequences of not requiring the information specified in the Rule would be a substantial weakening of the Rule's effectiveness. The Commission believes that certain broker-dealers engaging in abusive sales practices in connection with penny stocks may choose to ignore the requirements of the Rule. The Rule therefore requires records to be kept that indicate their compliance with each of its provisions. This documentation enables regulatory authorities to review a broker-dealer's compliance with the Rule, and provides the basis for simple and direct enforcement actions against broker-dealers that fail to comply.

3. Consideration Given to Information Technology

No consideration was given to using information technology to reduce this burden.

4. Duplication

Broker-dealers are not otherwise required to obtain the written agreement to purchases required by the Rule. However, responsible broker-dealers currently obtain information of substantially the same type that is required by the Rule to comply with SRO suitability rules. Although the information currently obtained by responsible broker-dealers also can be used to satisfy the Rule's requirements, the Rule does not duplicate these SRO rule requirements because the Rule contains an enhanced suitability

determination and allows for direct Commission enforcement actions in cases of non-compliance. In addition, the Rule does not duplicate any of the requirements of other rules adopted pursuant to Section 15(g) of the Exchange Act. The other rules adopted pursuant to Section 15(g) mandate that broker-dealers disclose certain information to customers about the penny stock market in general and about the particular penny stock transaction to customers with whom they do business. In contrast, the Rule requires broker-dealers who engaged in penny stock transactions with customers to obtain certain information from customers and to make a suitability determination on the basis thereof.

5. Effect on Small Entities

The statements requested are not extensive, and therefore the collection of information is not unduly burdensome for small entities.

6. Consequences of Not Conducting Collection

These statements are required only upon the occurrence of a single event. Therefore, collection could be no less frequent.

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

There are no special circumstances. This collection is consistent with the guidelines in 5 CFR 1320.5(d)(2).

8. Consultations Outside the Agency

The required Federal Register notice with a 60-day comment period soliciting comments on this collection of information was published. No public comments were received.

9. Payment or Gift

No payments or gifts are provided to any respondents.

10. Confidentiality

Not applicable.

11. Sensitive Questions

The Information Collection does not collect information about individuals, therefore, a PIA, SORN, and PAS are not required.

12. Information Collection Burden

The burden of the collection of information required under Rule 15g-9 varies widely depending on the activity and size of the broker-dealer. In this regard, the burden is the greatest on those broker-dealers whose questionable sales practice activities correspond directly to the sale of penny stocks (*i.e.* boiler-room broker-dealers), the primary type of security that the Rule addresses. The Rule is intended to rein in questionable penny stock sales practices by establishing procedures that broker-dealers follow before recommending penny stocks to unsophisticated customers. The burden of the Rule's information requirements, therefore, is triggered by the solicitation of new customers, and the greatest burden is imposed on broker-dealers who are constantly soliciting new customers for penny stock purchases.

The burden on the other broker-dealers, however, is much lower. These broker-dealers tend to concentrate on servicing existing customers. Consequently, the additional information burden for these broker-dealers is not nearly as great as for boiler-room broker-dealers, and the Rule imposes the greatest burden on those broker-dealers who employ sales practices that are the direct target of the prophylactic requirements of the Rule.

The Commission staff estimates that approximately five percent of registered broker-dealers, or 175 broker-dealers,² are subject to the Rule (5% x approximately 3,497 registered broker-dealers = 175 broker-dealers). As indicated above, the burden of the Rule on a respondent varies widely depending on the frequency with which new customers are solicited. On average, for all respondents, the staff has estimated that respondents process three new customers per week, or approximately 156 new customers requiring suitability determinations per year. We also estimate that a broker-dealer would take approximately one-half hour per new customer in obtaining, reviewing, and processing (including transmitting to the customer) the information required by Rule 15g-9, and each respondent would consequently spend 78 hours annually (156 new customers x .5 hours) obtaining the information required in the Rule. This would result in 27,300 annual responses per year for all respondents (175 respondents x 156 new customer suitability determinations per year). **We determined, based on the estimate of 175 broker-dealer respondents, that the annual hour burden of Rule 15g-9 is 13,650 hours (175 respondents x 78 hours).**

Burden type	Communication type	Number of broker-dealers	Annual number of responses	Hours per response	Total burden per communication type
Third party disclosure	Mail	175	156	1/2	13,650
<i>Total burden</i>					13,650

13. Costs to Respondents

² As of July 1, 2023, there are 3,497 registered broker-dealers. 5% of 3,497 is 174.85, rounded up to 175.

There is no cost to respondents other than the internal cost of the hours per respondent per year obtaining the information required by the rule.

14. Costs to Federal Government

There are no costs to the Federal Government. Responses submitted pursuant to Rule 15g-9 would be reviewed by existing SEC staff as part of their regular duties and does not incur capital or start-up costs to comply.

15. Changes in Burden

There was a decrease in the number of respondents affected by the rule, which impacted agency estimates. This decrease was caused by a decrease in the number of registered broker-dealers, from 182 to 175 and an estimated total burden hours from 14,196 to 13,650.

16. Information Collection Planned for Statistical Purposes

Not applicable. The information collection is not used for statistical purposes.

17. Approval to Omit OMB Expiration Date

The Commission is not seeking approval to omit the expiration date.

18. Exceptions to Certification for Paperwork Reduction Act Submissions

This collection complies with the requirements in 5 CFR 1320.9.

B. COLLECTIONS OF INFORMATION EMPLOYING STATISTICAL METHODS

This collection does not involve statistical methods.