

**SUPPORTING STATEMENT**  
**for the Paperwork Reduction Act Information Collection Submission for**  
**Removal of References to Credit Ratings From Regulation M: Amendments to Rule**  
**17a-4(b)(17)**

**OMB Control No. 3235-0806**

**A. JUSTIFICATION**

**1. Information Collection Necessity**

Section 939A(b) of the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”)<sup>1</sup> requires the Securities and Exchange Commission (“Commission” or “SEC”), among other things, to “remove any reference to or requirement of reliance on credit ratings” and “substitute in such regulations such standard of credit-worthiness” as the Commission determines to be appropriate for those regulations. In accordance with the requirements of Section 939A(b), the Commission adopted amendments to Rules 101 and 102 of Regulation M to remove the existing exceptions for nonconvertible debt securities, nonconvertible preferred securities, and asset-backed securities that are rated by at least one nationally recognized statistical rating organization (“NRSRO”), as that term is used in Rule 15c3-1 under the Securities Exchange Act of 1934 (“Exchange Act”), in one of its generic rating categories that signifies investment grade (“Investment Grade Exception”), and replace them with alternative standards of credit-worthiness.<sup>2</sup>

Regulation M is a set of prophylactic anti-manipulation rules that is designed to preserve the integrity of the securities trading markets as independent pricing mechanisms by prohibiting activities that could artificially influence the market for an offered security.<sup>3</sup> Rule 101 and Rule 102 of Regulation M prohibit distribution participants, their affiliated purchasers, issuers, selling security holders, and their affiliated purchasers from bidding for, purchasing, or attempting to induce any person to bid for or purchase, a covered security, during the applicable restricted period, unless an exception applies.<sup>4</sup> Prior to the Commission’s June 7, 2023, amendments, Rule 101(c)(2) and Rule 102(d)(2) excepted nonconvertible debt securities, nonconvertible preferred securities, and asset-backed securities that are rated by at least one NRSRO in one of its generic

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<sup>1</sup> See Pub. L. 111–203 sec. 939A(b), 124 Stat. 1376, 1872-90 (2010).

<sup>2</sup> See *Removal of References to Credit Ratings From Regulation M*, Exchange Act Release No. 97657 (June 7, 2023), [88 FR 39962 (June 20, 2023)] (“2023 Adopting Release”). The Commission also adopted an amendment to Rule 100 of Regulation M to provide a definition for the term “structural credit risk model,” which is used in newly adopted exceptions under Rule 101 and Rule 102 of Regulation M. This adoption follows the Commission’s publication of proposed rule amendments in March 2022. See *Removal of References to Credit Ratings From Regulation M*, Exchange Act Release No. 94499 (Mar. 22, 2022) [87 FR 18312 (Mar. 30, 2023)] (“Proposal”).

<sup>3</sup> See *Anti-manipulation Rules Concerning Securities Offerings*, Exchange Act Release No. 38067 (Dec. 20, 1996), [62 FR 520, 521 (Jan. 3, 1997)] (“Regulation M Adopting Release”).

<sup>4</sup> 17 CFR 242.101(a) (distribution participants and their affiliated purchasers), 242.102(a) (issuers, selling security holders, and their affiliated purchasers).

rating categories that signifies investment grade.<sup>5</sup> The premise of the Investment Grade Exceptions was that securities of issuers of a certain credit quality trade based on their yield and credit-worthiness and are less susceptible to the type of manipulation that Regulation M seeks to prevent.<sup>6</sup>

As discussed above, in place of the Investment Grade Exceptions in Rule 101 and Rule 102, and consistent with the Commission's original premise in excepting nonconvertible debt securities and nonconvertible preferred securities (together, "Nonconvertible Securities") of credit-worthy issuers that are less susceptible to the type of manipulation that Rule 101 and Rule 102 seek to prevent, the Commission adopted an alternative standard of credit-worthiness for distributions of Nonconvertible Securities of issuers for which the probability of default, estimated as of the sixth business day immediately preceding the determination of the offering price and over the horizon of 12 full calendar months from such day, is 0.055% or less, as determined and documented, in writing, by the distribution participant acting as the lead manager (or in a similar capacity) of a distribution, as derived from a structural credit risk model.

To facilitate Commission examinations of broker-dealers who rely on the new exception in Rule 101 or Rule 102, as applicable, for Nonconvertible Securities, the Commission adopted a new paragraph (17) of Rule 17a-4(b) that requires broker-dealers to preserve the written probability of default determination relied upon pursuant to Rule 101(c)(2)(i) or Rule 102(d)(2)(i), as applicable.

Certain provisions of the amendments impose "collection of information" requirements within the meaning of the Paperwork Reduction of 1995 ("PRA"). The title for the information collection included in this Supporting Statement is "Rule 17a-4(b)(17) Records to be Preserved by Certain Brokers and Dealers."

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

As described in the 2023 Adopting Release, the Commission believes that the information contained in the records required to be retained and kept pursuant to the amendment to Rule 17a-4 will be used to facilitate the Commission in conducting examinations of broker-dealers who rely on the new exceptions in Rule 101 and Rule 102.

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

Use of information technology could reduce regulatory burdens related to preserving the written probability of default determination under the amendments to Rule 17a-4.

## **4. Duplication**

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<sup>5</sup> 17 CFR 242.101(c)(2).

<sup>6</sup> See Regulation M Adopting Release, at 62 FR 527.

The amendments Rule 17a-4 would not result in, or require the collection of, duplicate information that is otherwise available in a similar form. The Commission’s probability of default standard and related record preservation requirement are not collected elsewhere.

## 5. Effect on Small Entities

As discussed in the 2023 Adopting Release, the Commission does not believe that any of the persons that will be impacted by the amendments are small entities under the relevant definitions. Small entities include broker-dealers with total capital (net worth plus subordinated liabilities) of less than \$500,000 on the date in the prior fiscal year as of which its audited financial statements were prepared pursuant to Rule 17a-5(d) under the Exchange Act,<sup>7</sup> or, if not required to file such statements, a broker-dealer who had total capital (net worth plus subordinated liabilities) of less than \$500,000 on the last day of the preceding fiscal year (or in the time it has been in business, if shorter), and is not affiliated with any person (other than a natural person) who is not a small business or small organization.<sup>8</sup> A small business or small organization, for purposes of “issuers” or “person” other than an investment company, is defined as a person who, on the last day of its most recent fiscal year, had total assets of \$5 million or less.<sup>9</sup>

Based on the Commission’s analysis of the existing information relating to broker-dealers who are subject to Rule 101, Rule 102, and Rule 17a-4, it is unlikely that any broker-dealer categorized as a “small business” or “small organization” under Rule 0-10<sup>10</sup> could serve as an underwriter or other distribution participant, as they would almost certainly have insufficient capital to participate in underwriting activities. In addition, the Commission continues to believe that none of the various persons affected by the amendments would qualify as a small entity under the Rule 0-10 definition as it is unlikely that any issuer of that size had investment grade securities that were eligible for the Investment Grade Exception. Accordingly, the Commission believes it is unlikely that, in the future, a small entity may become impacted by the amendments because broker-dealers who enter this market are likely to have at least \$500,000 in total capital, as described above, or to be affiliated with a person who is not a small business or small organization as defined under Rule 0–10, and because issuers of securities that are eligible for the new exceptions provided in Rule 101(c)(2) and in Rule 102(d)(2) are likely to have total assets greater than \$5 million.

For the foregoing reasons, the Commission certified, in the 2023 Adopting Release, pursuant to Section 605(b) of Title 5 of the U.S. Code, that the amendments to Rule 100, Rule 101, Rule 102, and Rule 17a-4 will not have a significant economic impact on a substantial number of small entities.

## 6. Consequences of Not Conducting Collection

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<sup>7</sup> See 17 CFR 240.17a-5(d).

<sup>8</sup> See 17 CFR 240.0-10(c).

<sup>9</sup> 17 CFR 240.0-10(a).

<sup>10</sup> 17 CFR 240.0-10.

Absent the addition of paragraph (17) to Rule 17a-4(b), which requires broker-dealers relying on the probability-of-default-based exception under Rule 101 or Rule 102 to preserve the written probability of default calculation upon which they relied, the Commission would not have the same access to necessary records in conducting examinations of broker-dealers relying on those exceptions.

#### **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 Commission issued a release soliciting comment on the new “collection of information” requirements and associated paperwork burdens.<sup>11</sup> A copy of the release is attached. Comments on the 2023 Adopting Release were received from industry groups, investors, and other market participants. In addition, the Commission and staff participated in ongoing dialogue with representatives of various market participants through meetings. Any comments received on this rulemaking are posted on the Commission’s public website, and made available through <https://www.sec.gov/comments/s7-11-22/s71122.htm>. The Commission considered all comments received prior to publishing the final rule, and explained in the Adopting Release how the final rule responded to such comments, in accordance with 5 C.F.R. 1320.11(f).

#### **9. Payment or Gift**

No payment or gift is provided to respondents.

#### **10. Confidentiality**

The Commission will not typically receive confidential information as a result of this collection of information. To the extent that the Commission receives—through its examinations or investigations, or by some other means—records or disclosures from a broker-dealer regarding probability of default determinations, such information will be kept confidential, subject to the provisions of applicable law.

#### **11. Sensitive Questions**

The Information Collection does not collect information about individuals, but rather only business contact information; therefore, a PIA, SORN, and PAS are not required.

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<sup>11</sup> See Proposal.

## 12. Information Collection Burden

The Commission estimated the hourly burden of the information collection as summarized in the chart below.

Summary of Hourly Burdens								
		A.	B.	C.	D.	E.	F.	
Rule 17a-4(b)(17) Information Collections	Type of Burden	Number of Entities Impacted	Annual Responses per Entity	Initial Burden per Entity per Response	Initial Burden Annualized per Entity per Response	Ongoing Burden per Entity per Response	Total Annual Burden Per Entity	Total Industry Burden
					[C ÷ 3 years]			
Preserving the written probability of default calculation (Rule 17a-4)—Initial	Recordkeeping	301	1	25	8.33	0	25	2,508.3
Preserving the written probability of default calculation (Rule 17a-4)—Ongoing	Recordkeeping	301	1	0	0	10	10	3,010
<b>TOTAL HOURLY BURDEN FOR ALL RESPONDENTS: 5,518.3</b>								

As described in more detail below, the amendment to Rule 17a-4 results in two new information collections. The information collections are initial and ongoing recordkeeping burdens related to preserving the written probability of default calculation pursuant to the amendments to Rule 17a-4. These information collections apply to broker-dealers that choose to rely on the exception for a distribution of Nonconvertible Securities under Rule 101 or Rule 102. These PRA burdens are distinct from the existing OMB-approved burden estimates under Rule 17a-4 because there was no related recordkeeping requirement under Rule 17a-4 in connection with reliance on the Investment Grade Exceptions.

The amendment imposes information collection burdens on broker-dealers that choose to rely on the exception for a distribution of Nonconvertible Securities. There were 201 lead managing underwriters, and 100 other non-lead manager broker-dealers of Nonconvertible Securities in 2021. Therefore, 301 respondents will be subject to PRA burdens under Rule 17a-4(b)(17). The Commission believes that this number will remain roughly consistent because of the capital, expertise, and relationships needed to underwrite a nonconvertible security. The Commission, therefore, is estimating that 301 respondents will be subject to PRA burdens under the amendment to Rule 17a-4.

### Preserving the Written Probability of Default Calculation (Rule 17a-4(b)(17))

#### i. Initial Burden

The amendment to Rule 17a-4 requires broker-dealers relying on the probability-of-default-based exception in Rule 101 or Rule 102 to preserve for a period of not less than three years, the first two years in an easily accessible place, the written probability of default determination relied upon. The burden imposed by the new requirements under Rule 17a-4 are limited to the maintenance and preservation of the written records, as the burden for creating the records is

accounted for in the PRA estimates and Supporting Statement for the amendments to Rule 101. The Commission thus estimates that the recordkeeping requirements under Rule 17a-4 will impose an initial burden of 25 hours per respondent for updating the applicable policies and systems required to account for preserving the records made pursuant to Rule 101. The Commission, therefore, estimates that **the total annual industry-wide initial burden for this requirement would be 2,508.33 hours.**<sup>12</sup>

## ii. Ongoing Burden

The Commission estimates that respondents will incur an ongoing internal annual burden of 10 hours per firm for maintaining such records, as well as to make additional updates to the applicable record preservation policies and systems to account for preserving the records pursuant to new Rule 17a-4(b)(17). The Commission, therefore, estimates that **the total annual ongoing industry-wide burden would be 3,010 hours.**<sup>13</sup>

Broker-dealers relying on the new exception in Rule 101(c)(2)(i) or Rule 102(d)(2)(i) must preserve the written probability of default determination made pursuant to Rule 101(c)(2)(i), as amended. The Commission estimates that it will take a distribution participant 25 hours to update the applicable policies and systems required to account for capturing the records made pursuant to new Rule 101(c)(2)(i), for an aggregate cost of \$2,731,575. The Commission also estimates that it will take a distribution participant 10 hours to maintain such records as well as to make additional updates to the applicable record preservation policies and systems to account for the rules. Therefore, it is estimated that annually broker-dealers will spend \$1,092,630 in the aggregate complying with this requirement.

## 13. Costs to Respondents

There are no external capital, start-up, maintenance or operational cost burdens associated with this rule.

## 14. Costs to Federal Government

The Federal government would not incur a cost in connection with the collection of this information.

## 15. Changes in Burden

There is a change in estimated burden hours for both the initial and ongoing burdens in the 2023 Adopting Release due to an increase in the estimated number of respondents from the Proposal. In the Proposal, there was an estimated 237 respondents, whereas in the 2023 Adopting Release, there was an estimated 301 respondents. The changes are described in the chart below.

<sup>12</sup> 301 respondents × 25 hours = 7,525 hours for the total initial burden. As we plan to request a three-year approval period, we divide 7,525 by 3 to get 2,508.33 hours per year.

<sup>13</sup> 301 respondents × 10 hours = 3,010 hours.

<b>Information Collection Requirement</b>	<b>Annual Industry Burden Adopted</b>	<b>Annual Industry Burden Previously Proposed</b>	<b>Change in Burden</b>	<b>Reason for Change</b>
Preserving the written probability of default calculation (Rule 17a-4)— Initial	2,508.3 hours for 301 respondents at 8.33 hours per respondent	1,975 hours for 237 respondents at 8.33 hours per respondent	1,600 hours	Increase in estimated number of respondents
Preserving the written probability of default calculation (Rule 17a-4)— Ongoing	3,010 hours for 301 respondents at 10 hours per respondent	2,370 hours for 237 respondents at 10 hours per respondent	640 hours	Increase in estimated number of respondents

#### **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.