

intermediaries. While these benefits are not readily quantifiable in terms of dollar value, we believe that transfer agents that choose to exclusively adopt electronic or micrographic-based records systems in lieu of paper records may realize cost-savings and reduce certain risks associated with paper-based recordkeeping. For example, the use of electronic and storage media should reduce storage burdens (*e.g.*, the need for storage space) that transfer agents currently face in maintaining paper records.

Other benefits include:

- increased efficiency of recordkeeping operations by reducing the need to maintain records in hard copy format;
- reduced likelihood that documents will be lost or misfiled;
- ability to retrieve documents more quickly;
- audit trails can be automated;
- reduction of risk for natural disasters;
- file centralization is automatic (file and records need not be removed from their storage in order to reference them);
- multiple persons can view the same document simultaneously;
- access authorization can be automated;
- space required for document storage is drastically reduced;
- document indexing and cross-referencing can be automatic; and
- documents can be copied, faxed, printed, and e-mailed without the paper originals.

In addition, the proposed software escrow provision would enable transfer agents to more conveniently comply with the current Rule 17Ad-7(f)(5)(ii) requirement that a copy of the electronic storage system the transfer agent utilizes to store its records be placed in escrow with an independent third party.

The Commission requests comments on the potential benefits of electronic recordkeeping including quantitative data on the potential cost savings from eliminating hard copy records.

#### B. Costs

The amendments to Rule 17Ad-7(f) would not impose costs on any particular person or entity because compliance with this provision would apply only to those transfer agents that choose to store any of their records exclusively in electronic form. Nevertheless, transfer agents that elect to use micrographic media or electronic storage media may incur some costs in destroying or otherwise disposing hard copy records that they elect to dispose or destroy. Any costs related to the use of micrographic or electronic storage

media should be at least partly offset by the resulting elimination of the need to maintain and store records in hard copy format. This cost is likely to depend upon the volume of hard copy records needed to be disposed. We expect these costs to be relatively minimal.

We estimate that approximately 60 transfer agents<sup>12</sup> will use a third party to escrow the required source code.<sup>13</sup> Each transfer agent will evaluate the risk and cost effectiveness of its records management solution differently based upon the solution that is best for its business model, such as its business practices and volume, and that assures its ability to comply with Rule 17Ad-7. Moreover, we cannot predict the effect of future market competition and innovation on the technologies that transfer agents might employ for their recordkeeping.

In addition, there will be some cost imposed by the proposed escrow requirement amendment. However, the Commission considered these costs in the Adopting Release and any new costs associated with the escrow amendment (*i.e.*, having a third party escrow the source code on the transfer agent's behalf) would likely be included in the software contract between the parties.

The Commission requests commenters to provide cost data for switching from hard copy records to electronic recordkeeping. In particular, what would be the startup costs and annual maintenance costs?

#### VI. Consideration of Impact on the Economy

For purposes of the Small Business Regulatory Enforcement Fairness Act of 1996,<sup>14</sup> a rule is "major" if it has resulted or is likely to resort in:

- an annual effect on the economy of \$100 million or more;
- a major increase in costs or prices for consumers or individual industries; or
- significant adverse effects on competition, investment, or innovation.

We request comment regarding the potential impact of the proposed rule amendments on the economy on an

annual basis. We request that commenters provide empirical data and other factual support for their views.

#### VII. Consideration of Burden on Competition, and Promotion of Efficiency, Competition, and Capital Formation

Section 3(f) of the Act<sup>15</sup> as amended by the National Securities Markets Improvement Act of 1996<sup>16</sup> provides that whenever the Commission is engaged in rulemaking and is required to consider or determine whether an action is necessary or appropriate in the public interest, the Commission shall consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation. In addition, Section 23(a)(2) of the Act<sup>17</sup> requires the Commission, when adopting rules under the Act, to consider the anti-competitive effects of any rules it adopts.

We are considering the proposed amendments to Rule 17Ad-7(f) in light of the standards set forth in Sections 3(f) and 23(a)(2) of the Act. For the reasons stated herein, the proposed amendments (1) should promote efficiency by allowing registered transfer agents to benefit from being allowed to dispose of hard copies, (2) should not adversely affect capital formation because they relate solely to post-issuance activity, and (3) should not impose any burden on competition because they will apply equally to all registered transfer agents.

We do not anticipate that the proposed amendments would have a significant effect on competition or impose any burden on competition that is not necessary or appropriate in furtherance of the Act. Under the proposed amendments, all registered transfer agents would be permitted, though not required, to exclusively use micrographic media and electronic storage media to fulfill all of the Commission's regulatory obligations. In addition, the proposed amendments would apply equally to all registered transfer agents. However, in order to fully evaluate the effects on competition of the proposed amendments, the Commission requests commenters to provide their views and specific empirical data as to any effects on competition that might result from the Commission's proposed amendments to Rule 17Ad-7(f).

<sup>12</sup> In the adopting release to Rule 17Ad-7(f), we estimated that approximately 500 transfer agents were likely to use electronic or micrographic storage systems. During the year-and-a-half since Rule 17Ad-7(f) has been effective, however, only five transfer agents have taken advantage of the record storage alternatives provided by the rule.

<sup>13</sup> Although this estimate represents less than 10% of the number of currently-registered transfer agents, we expect that many of the largest bank, corporate, and independent transfer agents, which represent over 90% of the entire transfer agent industry volume, will eventually convert their records-management systems to electronic-based solutions.

<sup>14</sup> 5 U.S.C. 801 *et seq.*

<sup>15</sup> 15 U.S.C. 78c.

<sup>16</sup> Pub. L. No. 104-290, 110 Stat. 3416 (1996).

<sup>17</sup> 15 U.S.C. 78w(a)(2).