

Regulation AC, analysts may be found to have violated the anti-fraud provisions of the federal securities laws if they make baseless recommendations or recommendations that they disbelieve.<sup>57</sup>

### *J. Performance-Based Compensation*

Commenters expressed concern that Regulation AC could be read to require disclosure of analyst compensation arrangements based on the accuracy or performance of the views expressed as to the subject company's prospects.<sup>58</sup> Commenters thought that the compensation disclosure provision should be clarified to only require disclosure of compensation that was intended to influence or induce the particular view expressed in the research report.<sup>59</sup>

In the Proposing Release, the Commission noted that Regulation AC does not preclude an analyst from providing otherwise permissible services to his or her firm's investment banking department, and it does not prohibit analysts generally from receiving compensation for covering issuers or for preparing research reports. Instead, Regulation AC focuses on disclosure where the analyst compensation that is related to the specific recommendations or views expressed by the research analyst in the research report. Regulation AC is not intended to address compensation based on the performance of the views expressed regarding the securities discussed.

### **III. Paperwork Reduction Act**

Regulation AC contains "collection of information" requirements within the meaning of the Paperwork Reduction Act of 1995 ("PRA").<sup>60</sup> We have submitted the proposal to the Office of Management and Budget ("OMB") for review in accordance with the PRA.<sup>61</sup> An agency may not conduct or sponsor, and a person is not required to respond to, an information collection unless it displays a currently valid OMB control number.

In the Proposing Release, the Commission solicited comments on the

collection of information requirements. In response to comments, the Commission has revised the estimates published in the Proposing Release regarding the collection of information burdens associated with the new rule.

#### *A. Summary of Collection of Information*

Regulation AC generally requires that research reports published, circulated, or provided by a broker or dealer or covered person contain a statement attesting that the views expressed in each research report accurately reflect the analyst's personal views and whether or not the research analyst received or will receive any compensation in connection with the views or recommendations expressed in the research report. Regulation AC also requires broker-dealers to, on a quarterly basis, make, keep, and maintain records of research analyst statements regarding whether the views expressed in public appearances accurately reflected the analyst's personal views, and whether any part of the analyst's compensation is related to the specific recommendations or views expressed in the public appearance.

#### *B. Reporting and Cost Burden Estimates*

Regulation AC provides that brokers, dealers, and covered persons must include in research reports they publish, circulate, or provide certain certifications and disclosures about the analyst's views expressed in the research reports and any relationship between the analyst's compensation and the specific recommendations or views expressed. The regulation also requires broker-dealers to periodically make, keep, and maintain records of research analyst certifications and disclosures in connection with public appearances.

The staff of the Commission believes that the average amount of time it would take to include the required certifications and disclosures in each research report is one minute per report. In the Proposing Release, the Commission staff estimated that broker-dealers publish approximately 657,000 research reports per year. One commenter provided the Commission with data in response to the Proposing Release.<sup>62</sup> After considering this

additional information, the staff of the Commission believes that broker-dealers publish approximately 1,375,865 research reports per year.<sup>63</sup> Therefore, the Commission estimates that the total annual burden in hours for broker-dealers to comply with the research report certification and disclosure requirements is approximately 22,930 hours per year ((1 minute × 1,375,865 reports)/60 minutes).

The Commission staff expects that research analysts will likely be the employees primarily charged with executing certifications and including them in research reports. According to industry sources, research analysts, on average, earn \$189,250 per year, for an hourly pay rate of approximately \$90. Including 35% overhead, Commission staff estimates that the hourly pay rate for a research analyst would be approximately \$121.50. Therefore, the Commission estimates that the total annual burden in dollars for broker-dealers to comply with the research report certification and disclosure requirements is approximately \$2,785,995.00<sup>64</sup> per year (22,930 hours × \$121.50 per hour).

Rule 501 of Regulation AC, which applies to research reports, may also impose requirements on certain entities if they are associated with a broker-dealer and meet the definition of "covered person." However, "covered persons" are not subject to Rule 502 of Regulation AC, which addresses public appearances. The Commission estimates that approximately 2,650 SEC registered investment advisers are associated with a broker-dealer. We believe that not all of these entities write research reports, and that those who do write research reports write relatively few. Of those investment advisers that are associated with a broker-dealer and that write research reports, we do not believe that all of them will meet the definition of a "covered person," as defined by

through First Call Research Direct. Thomson Financial asserted that, when these additional sell-side reports are accounted for, the total exceeds 2 million reports a year. Thomson Financial suggested that the compliance costs for sell-side firms could run as high as \$4,116,784.50.

<sup>63</sup> After further consultation with Thomson Financial, they have revised their total estimated number of research reports per year for 2001 to range between 1,375,865 and 1,540,150. The staff believes that the overall calculations are over-inclusive and possibly duplicative. As a result, we are basing our estimates on the lower-end of the range of the number of research reports per year. The staff believes that this estimate continues to be conservative.

<sup>64</sup> The estimated total annual burden in dollars for broker-dealers to comply with the research report certification and disclosure requirements would be approximately \$3,118,642.00 if calculated using the high-end of the estimated range for the number of research reports.

<sup>57</sup> See Securities Exchange Act Release No. 45908 (May 10, 2002), 67 FR 34968, 34977 (May 16, 2002); Proposing Release at 51512; *Cf. Hanly*, supra, note 13, at 597. See also *In the Matter of Robertson Stephens, Inc.*, Administrative Proceeding File No. 3-11003 (January 9, 2003) (settled fraud action against broker-dealer where Commission found that a research analyst employed by the broker-dealer issued recommendations about a public company that were inconsistent with his privately communicated beliefs about the company.)

<sup>58</sup> See, e.g., Goldman and Merrill.

<sup>59</sup> See, e.g., Cleary, SIA, SSB, and Sullivan.

<sup>60</sup> 44 U.S.C. section 3501 *et seq.*

<sup>61</sup> 44 U.S.C. section 3507(d) and 5 CFR 1320.11.

<sup>62</sup> Thomson Financial asserted in its comment letter that the Commission's cost estimate in the Proposing Release was too low. Thomson Financial noted that the Commission cited data from Thomson Financial First Call and estimated that broker-dealers publish 657,000 research reports per year. Thomson Financial asserted that, while this estimate may accurately reflect equity research on U.S. securities transmitted via First Call Notes, it did not capture fixed-income research, research on non-U.S. equities or full-text reports transmitted