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SEC Sets Compliance Date for Pay-to-Play Rule's Ban on Third-Party Solicitation of Government Entities

July 15, 2015

On June 25, 2015, the Securities and Exchange Commission (SEC) set a compliance date of July 31, 2015 for the ban on payments to third parties for the solicitation of advisory business from any government entity under Rule 206(4)-5 of the Investment Advisers Act of 1940 (Pay-to-Play Rule). At the same time, the SEC also clarified in its Frequently Asked Questions (FAQ) on the Pay-to-Play Rule that it would not recommend enforcement action against an investment adviser or its covered associates under the Pay-to-Play Rule for payments to third-party solicitors until the Financial Industry Regulatory Authority (FINRA) and the Municipal Securities Rulemaking Board (MSRB) have adopted equivalent pay-to-play rules for broker-dealers and municipal advisers, respectively.

The Pay-to-Play Rule prohibits an investment adviser subject to the Rule and its covered associates from providing, or agreeing to provide, any direct or indirect payment to a third party for soliciting advisory business from a government entity on the adviser's behalf, unless the third party is: (i) a registered investment adviser; (ii) a registered broker or dealer subject to pay-to-play rules adopted by a national securities association (e.g., FINRA); or (iii) a registered municipal adviser subject to MSRB pay-to-play rules. The SEC must find, by order, that such FINRA and MSRB rules impose substantially equivalent or more stringent restrictions than the Pay-to-Play Rule and are consistent with its objectives.[1]

The Pay-to-Play Rule first became effective on September 13, 2010. Subsequently in a July 2012 release, the SEC extended the compliance date for the Rule's third-party solicitation ban to nine months after the compliance date of final SEC rules on municipal adviser registration. In another release on June 25, 2015, the SEC set the compliance date for the third-party solicitation ban as July 31, 2015 (nine months after the October 31, 2014 compliance date of the municipal adviser registration rules). However, as neither FINRA nor the MSRB has finalized its own pay-to-play rules,[2] the SEC also simultaneously clarified in the FAQ that it would not recommend enforcement action against an investment adviser or its covered associates for the payment to any person to solicit a government entity for investment advisory services until the later of (i) the effective date of a FINRA pay-to-play rule or (ii) the effective date of an MSRB pay-to-play rule. Thus, until both the FINRA and MSRB pay-to-play rules are in effect, investment advisers and their covered associates will not be subject to enforcement actions for third-party solicitation under the Pay-to-Play Rule.

If you have any questions on the foregoing, please contact your usual Proskauer contact or any of the lawyers listed in this alert.

[1] Please refer to our previous client alert for additional background information on the Pay-to-Play Rule.

[2] On August 18, 2014, the MSRB proposed amendments to expand its current pay-to-play rule, Rule G-37, to cover registered municipal advisers. MSRB Regulatory Notice 2014-15 is available here. FINRA released its own proposed pay-to-play rules modeled after the Pay-to-Play Rule on November 14, 2014. FINRA Regulatory Notice 14-50 is here.

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