

Pay-to-Play Spotlight: SEC Proposes Amendments to Its Recent Pay-to-Play Rule

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In November of 2010, the Securities and Exchange Commission (SEC) proposed several changes to its recent pay-to-play rule for investment advisers. These changes, if adopted, would impact both the way in which investment advisers comply with the pay-to-play rule (which becomes operational for most on March 14, 2011) and the ultimate scope of individuals covered by the rule or similar pay-to-play rules. The most important of these proposed changes is briefly discussed below.

Under the current SEC pay-to-play rule, an investment adviser is prohibited from paying a solicitor/placement agent any compensation unless the solicitor/placement agent is subject to a pertinent pay-to-play rule. Permissible solicitors/placement agents include an executive officer, general partner, managing member or employee of the investment adviser and a "regulated entity," which, in the rule currently enacted, refers to brokers regulated by the Financial Industry Regulatory Authority (FINRA). As a result, FINRA had planned to adopt its own pay-to-play rules.

Now, the SEC is proposing to change its solicitor/placement agent rules to exclude FINRA brokers from the list of permissible solicitors/placement agents and to substitute "municipal advisors" registered with the Municipal Securities Rulemaking Board (MSRB). (These municipal advisors are a new class of regulated persons created as a result of the Dodd-Frank legislation.) Thus, unless a solicitor/placement agent is related to the investment advisor as an executive officer, general partner, managing member or employee, an investment adviser would not be able to compensate a solicitor/placement agent unless the latter was a registered municipal advisor. (The MSRB is planning to apply its pay-to-play rule, Rule G-37, to such

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municipal advisors or to adopt a similar pay-to-play rule for municipal advisors.) Registration and payments under the SEC pay-to-play rule and the MSRB's municipal advisor rule become even more complex when one examines the exceptions to municipal adviser registrations related to investment advisers and their affiliated organizations.

Comments on the SEC's rulemaking are due by January 24, 2011, and the text of the proposed changes can be found here (as part of a number of proposed securities rule changes): <http://origin.www.gpo.gov/fdsys/pkg/FR-2010-12-10/pdf/2010-29956.pdf>.