

SEC Action Shows Necessity of Pay-to-Play Compliance

July 2014

On June 20, 2014, the Securities and Exchange Commission (SEC) disclosed settlements with a venture capital firm under the SEC's investment adviser pay-to-play rule. Because of 2011 contributions to a candidate for Mayor of Philadelphia and Governor of Pennsylvania by a covered associate at the firm, the firm was forced to disgorge over \$250,000 in fees for work related to city and state pension funds and pay a \$35,000 civil penalty. The relevant SEC orders can be found [here](#) and [here](#).

The facts of the case and the resulting penalty underscore the draconian effect of pay-to-play violations and how robust compliance efforts, such as a contribution preclearance program, can prevent such issues. The contributions in the case amounted to \$4,500 total, and the disgorgement may well have been higher had the firm, according to news accounts, not already been winding down its work for the investment pools related to the state and local pension funds.

Although those not in the financial service sector are not subject to the SEC rule, similar pay-to-play rules exist in states and localities around the country—such as New Jersey, Illinois, Houston, Los Angeles, and Connecticut. The crux of all of the pay-to-play rules is that contributions by contractors or prospective contractors or, in many locations, their directors, officers, or other employees (or family members) can result in fines, penalties, preclusion from future contracts, or, as in the SEC case, the disgorgement of fees from the underlying government contract. Federal, state, and local pay-to-play laws and rules are mostly strict liability prophylactic measures.

Authors

D. Mark Renaud
Partner
202.719.7405
mrenaud@wiley.law

Because of the large penalties involved (called the “death penalty” under the SEC rule), it is important for state and local contractors to have policies and procedures in place to prevent violations and to assist with reporting where required. Wiley Rein has experience establishing such compliance programs, and is available to assist with the specific questions that arise in light of the political activity proposed by directors, officers, employees, and a company's PAC.