

INSIGHTS

SEC Makes Technical Amendment to Definition of "Covered Associates" Under "Pay to Play" Rule of the Advisers Act

June 7, 2012

On June 22, 2011, the Securities and Exchange Commission (SEC) adopted rules implementing certain provisions of Title IV of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), including proposed amendments to Rule 206(4)-5, or the "pay-to-play" rules of the Investment Advisers Act of 1940 (Advisers Act) in response to changes made by the Dodd-Frank Act. The purpose of the rule is to prevent investment advisers from seeking to influence government officials' awards of advisory contracts through political contributions by prohibiting them from providing advisory services for compensation to government clients for two years after the adviser or certain of its executives or employees (covered associates) make a contribution to a public official of a government entity or a candidate for such office who is or will be in a position to influence the award of advisory business. The SEC had also extended the time period for compliance to June 13, 2012 in order to provide enough time for the MSRB and FINRA to adopt their own pay-to-play rules, and to give third-party solicitors additional time to come into compliance.

A "covered associate" of an investment adviser is defined in rule 206(4)-5(f)(2) of the Advisers Act as: (i) any general partner, managing member or executive officer, or other individual with a similar status or function; (ii) any employee who solicits a government entity for the investment adviser and any person who supervises, directly or indirectly, such employee; and (iii) any political action committee controlled by the investment adviser or by any of its covered associates.

In the June 2011 adopting release, the SEC specified in the "Discussion" section that it was **not** adopting the proposed amendment to the definition of "covered associate," which replaced the word "individual" with the word "person" such that a legal entity, and not just a natural person that is a general partner or managing member of the adviser would be considered a "covered associate." However, the final text of the rule published in the "Text of Rule and Form Amendments" section of the adopting release and in the Federal Register reflected the proposed change in error (i.e., the word "individual" was incorrectly replaced by the word "person"). The SEC is therefore making this technical amendment to the rule to correct this mistake.