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It's Election Season: Investment Advisers Beware of the SEC Pay-to-Play Rule

With highly contested midterm elections less than three months away, investment advisers must be aware of, and pay close attention to, the Securities and Exchange Commission's (SEC) pay-to-play rule governing their business, SEC Rule 206(4)-5. The rule provides that when investment advisory firms and their covered associates make political contributions to certain candidates, the firms are prohibited from providing services for compensation to the governmental entities that the candidates can control or exert influence over. The rule also prohibits solicitations of contributions to these candidates and political parties, the violation of which is subject to substantial penalties. This article focuses on the key aspects of SEC Rule 206(4)-5, whose application to the rough and tumble world of political fundraising is notoriously complex.

Those who work in the financial industry should also be aware of the following additional four pay-to-play rules, which are similar to SEC Rule 206(4)-5:

1. Municipal Securities Rulemaking Board Rule G-37, which applies to brokers, dealers, municipal securities dealers, and municipal advisers.
2. Financial Industry Regulatory Authority Rule 2030, which applies to covered members of FINRA that are broker-dealers acting as placement agents for an investment adviser.
3. Commodity Futures Trading Commission Rule 23.451, which applies to non-security-based swap dealers.
4. SEC Rule 240.15Fh-6, which applies to security-based swap dealers.

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