

---

## Midterm Congressional Election Year Merits Extra Pay-to-Play Vigilance by Investment Advisers

FEBRUARY 5, 2018

Midterm congressional elections are expected to see a historic number of candidates competing.<sup>1</sup> The record number of candidates comes as individual races become increasingly expensive<sup>2</sup> and trends portend record spending.<sup>3</sup> All of these developments pose legal and reputational risk for regulated entities subject to pay-to-play restrictions.

The SEC actively enforces Rule 206(4)-5 under the Investment Advisers Act (the Rule).<sup>4</sup> The Rule is designed to deter investment advisers and their key personnel from participating in pay-to-play practices.<sup>5</sup> The Rule carries heavy penalties. It prohibits investment advisers from receiving any compensation from a government entity for two years after a violative contribution by the adviser or any covered employee to an official or candidate to be an official of a government entity.

A key facet of the Rule that investment advisers and their personnel may overlook is that the Rule not only covers contributions to candidates for state and local offices or incumbents in those offices running for reelection, it also covers contributions made to a candidate's campaign for federal office when that candidate holds a state or local office at the time of the contribution. This aspect of the Rule has often been the basis of SEC action under the Rule. Such a scenario accounts for one recent enforcement action and several of the exemptive applications filed under the Rule, including examples from the latest presidential campaign, where a number of sitting governors made bids for the White House. As noted above, the large number of congressional candidates in this cycle increases the likelihood of current local and state officials running for federal office. Accordingly, pay-to-play policies and procedures need to account for contributions to campaigns for federal office where the candidate is currently a state or local official.

This is a good time for advisers to review their policies and procedures to ensure that contributions to federal campaigns are highlighted as a potential trip wire. Some advisers implement preclearance for all political contributions so that compliance can review and confirm that each planned contribution is acceptable. Additionally, periodic checks of public federal campaign contribution databases for donations in states and localities where the adviser has government-entity clients would be prudent. Finally, it is worth considering supplemental training and/or

compliance alerts for personnel in order to highlight this issue. The best policies won't protect a firm if they are not effectively communicated and enforced.

Our team has experience designing and working with clients to implement effective pay-to-play policies and procedures focused on meeting the expectations of regulators.

---

<sup>1</sup> David Weigel and Michael Scherer, [The 2018 midterms are fast approaching. First up: Primary fights for both parties' future](#), *Washington Post*, PowerPost (Jan. 6, 2018).

<sup>2</sup> Elena Schneider, [Georgia special election smashes all-time spending record. It's official: It will be the most expensive House race in U.S. history](#), *Politico* (May 6, 2017).

<sup>3</sup> See generally Lesley Clark, [Coming soon to a TV or web site near you: A record-breaking, expensive 2018 election](#), *McClatchyDC* (Nov. 6, 2017).

<sup>4</sup> See Press Release, [U.S. Securities and Exchange Commission, 10 Firms Violated Pay-to-Play Rule By Accepting Pension Fund Fees Following Campaign Contributions](#) (Jan. 17, 2017).

<sup>5</sup> Political Contributions by Certain Investment Advisers, Advisers Act Release No. 3043 (July 1, 2010).

---

## Authors



**Benjamin  
Neaderland**  
PARTNER

✉ [benjamin.neaderland@wilmerhale.com](mailto:benjamin.neaderland@wilmerhale.com)

☎ +1 202 663 6340



**Joseph M. Toner**  
SPECIAL COUNSEL

✉ [joseph.toner@wilmerhale.com](mailto:joseph.toner@wilmerhale.com)

☎ +1 202 663 6188