MEMORANDUM TO CLIENTS

August 4, 2009

RE: <u>SEC Proposes Rules to Curtail "Pay to Play" by Public Plan Advisers</u>

On August 3, the Securities and Exchange Commission ("SEC") published its proposed new rules addressing so-called "pay to play" practices by investment managers and advisers seeking to manage money for state and local governments, including public pension funds and college savings plans ("529 plans"). See www.sec.gov/rules/proposed/2009/ia-2910.pdf. "Pay to play" refers to arrangements whereby investment advisers who make political contributions or other payments are rewarded with (or afforded the opportunity to compete for) contracts to manage public pension funds and other state and local government accounts. In recent years, federal and state regulators have brought both civil and criminal enforcement cases in connection with pay to play schemes involving public funds in New York, New Mexico, Connecticut, Illinois and Florida.

The proposed rules (to be issued under the Investment Advisors Act of 1940) would apply broadly to cover advisers registered by the SEC as well as certain investment advisers that are otherwise exempted from registration, including managers of hedge funds, private equity funds, and other "private" funds. Investment managers of "covered investment pools" including mutual funds and collective investment trusts would also be covered if the mutual fund or collective investment trust is selected as an investment option under a retirement plan, such as a 403(b) plan or 457 plan, or under a 529 plan for college savings.

The proposed rules would prohibit any adviser, including certain of the adviser's executives and employees, from –

- providing advisory services for compensation for two years after the adviser (or certain of its executives or employees) makes a political contribution to an elected official (including an incumbent or candidate) in a position to influence the selection of the adviser to provide advisory services for a government client (the "two year time out" provision);

- soliciting contributions on behalf of an elected official (or candidate) who can influence the selection of the adviser to provide services, or soliciting contributions for a political party in the state or locality where the adviser seeks to provide advisory services to a public fund or other government client;

- paying a third party solicitor or placement agent to solicit a government client on behalf of the investment adviser; and

- engaging in any of the prohibited "pay to play" conduct indirectly, such as by directing or funding political contributions through third parties.

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The proposed rules are modeled on rules issued by the Municipal Securities Rulemaking Board ("MSRB") that address pay to plan practices in the municipal securities markets, and are similar to rules previously proposed by the SEC in 1999 (but not finalized). As compared to the SEC's 1999 rule proposal, the proposed prohibition on payments to solicitors and placement agents is new. The 1999 proposal would not have prohibited an adviser from paying a solicitor to obtain business from a government client, but a contribution by a solicitor to a government official would have triggered the "two year time out" provisions. MSRB rules were amended in 2005 to prohibit municipal securities dealers from paying third party solicitors.

In recent months, the SEC has reportedly launched a number investigations into investment adviser pay to play practices, working in conjunction with state and local regulators. A statement issued by SEC Chairman Mary Schapiro in conjunction with the SEC's vote to propose the rules explains that criminal and regulatory actions over the past 10 years show that there is a need to address pay to play practices involving public pension and retirement funds and other government accounts. Her statement notes that public pension plans hold more than $2.2 trillion of assets – representing 1/3 of all U.S. pension assets – and that 529 plans hold another $104 billion in assets.

Comments are due on or before October 6, 2009.

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Please call one of the following, or the Groom attorney you regularly contact, if you have any questions about this or any other matter.

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