PAY-TO-PLAY COMPLIANCE DEADLINE AROUND THE CORNER FOR INVESTMENT ADVISERS

February 10, 2011

To Our Clients and Friends:

In 2010, the Securities and Exchange Commission (the "SEC") adopted Rule 206(4)-5 (the "Pay-to-Play Rule") under the Investment Advisers Act of 1940 (the "Advisers Act"). An important compliance date for the Pay-to-Play Rule is looming: March 14, 2011. The Pay-to-Play Rule is designed to address "pay-to-play" practices in the investment advisory industry. A key fact is that it applies to both registered and unregistered investment advisers. We described this rule in a memorandum to clients and friends that you may have received last year.[1]

While many private fund advisers who relied on the "fewer than 15 clients" exemption that was repealed by the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") are busy preparing for SEC registration later this year, all private fund sponsors need to be prepared to comply with the Pay-to-Play Rule much sooner. This includes private fund advisers that may be able to rely on the exemptions from registration in the Dodd-Frank Act, and the proposed SEC implementing rules, pursuant to (i) the venture capital fund adviser exemption, (ii) the private fund adviser exemption or (iii) the foreign private adviser exemption.[2]

The Pay-to-Play Rule contains three major prohibitions. Two of these prohibitions become effective on March 14, 2011. First, the rule contains a "Two-Year Timeout" that prohibits an investment adviser from receiving compensation of any kind for providing advisory services to a state or local government client (a "Government Client") (including a Government Client that is an investor in a private fund sponsored by the adviser) for two years after the adviser or certain of its affiliates, executives or employees ("Covered Associates") make a contribution to specified types of elected officials or candidates ("Government Officials"). Second, the rule prohibits an adviser and its Covered Associates from engaging in a broad range of fundraising activities for Government Officials or political parties in the localities where the adviser is providing or seeking business from a Government Client.

---

[1] *Client Update: SEC Adopts New Pay-to-Play Rule (July 12, 2010), available at* http://www.debevoise.com/newseventspubs/publications/detail.aspx?id=8200106a-2f07-49b1-a3e6-99f1b0470e06

[2] *For more information, see Client Update: SEC Proposes Rules to Implement the Dodd-Frank Act's Advisers Act Provisions (December 22, 2010), available at* http://www.debevoise.com/newseventspubs/publications/detail.aspx?id=046b5b00-2e17-4c3a-89b7-75fc4b9793ec

All private fund sponsors should promptly adopt policies and procedures designed to assure (through pre-clearance procedures or other means) that political contributions that would trigger the Two-Year Timeout are not made and that employees are aware of the rule's other prohibitions. Advisers who are registered must be prepared to maintain certain records with respect to political contributions as well.

The third prohibition of the Pay-to-Play Rule limits the ability of an adviser and its Covered Associates to compensate a third party (such as a placement agent) to solicit advisory business or an investment from a Government Client unless the third party is a registered broker-dealer or registered investment adviser. This prohibition will become effective on September 13, 2011. The SEC recently proposed an amendment to the Rule that would require the solicitor or placement agent to be a registered municipal adviser.

* * *

Please call us if you have any questions.

Washington, D.C.

Kenneth J. Berman
+1 202 383 8050
kjberman@debevoise.com

Gregory T. Larkin
+1 202 383 8064
gtlarkin@debevoise.com

New York

Michael P. Harrell
+1 212 909 6349
mpharrell@debevoise.com

Rebecca F. Silberstein
+1 212 909 6438
rfsilberstein@debevoise.com

Frankfurt

Marcia L. MacHarg
+49 69 2097 5120
mlmacharg@debevoise.com