

Now & Next

Securities Alert

October 21, 2026

SEC proposes to rescind advisers act pay-to-play rule

By Benedict Kwon, John Beals, John Partigan, and Elizabeth Nwabueze

Under the proposal, the federal floor may fall, but state, SRO, and contractual pay-to-play obligations would still shape public-plan fundraising.



What's the impact?

- Rule 206(4)-5 and Rule 204-2(a)(18) remain fully in force until a final rescission is adopted and takes effect. Comments on the proposal are due November 9.
- Compliance may fragment, as Advisers Act duties, SRO rules, state/local regimes, LPAs (limited partnership agreements), side letters, subscriptions, placement-agent agreements, and plan certifications may still bind.
- Investor diligence may deepen, with public plans, fund-of-funds, and others needing manager-by-manager review, especially for investment advisers subject to Section 206 but not Rules 206(4)-7 or 204A-1.

On September 3, the US Securities and Exchange Commission (SEC) proposed to rescind Rule 206(4)-5 under the Investment Advisers Act of 1940 (the investment adviser “pay-to-play” rule), together with the related recordkeeping requirements in Rule 204-2(a)(18) (Release No. IA-6994;

File No. S7-2026-31). Rule 206(4)-5 was adopted in 2010 to curb "pay-to-play," the practice of advisers, or their key people, making political contributions that could sway a state or local government's decision to hire or keep them, including decisions by public pension plans. In broad strokes, the rule does five things:

- / Imposes a two-year freeze on fees from a government client after a covered contribution to an official who can influence the hiring decision;
- / Allows for small contributions of up to \$350 per election, where the giver can vote, and \$150 where they cannot, as an exception;
- / Limits the use of paid outside solicitors and coordinated contributions;
- / Reaches private fund managers whenever a public plan invests or is approached to invest, which is why the rule can affect nearly every fundraiser; and
- / Requires advisers to keep detailed contribution records.

For managers with significant public pension relationships, rescission may not simplify pay-to-play. Rather, it could leave a more fragmented landscape governed by a patchwork of state regimes, contractual commitments, and surviving self-regulatory organization (SRO) rules.

The SEC's proposal and stated rationale

After more than 15 years, the SEC has concluded the rule is too rigid and has unintended consequences. For instance, a contribution as small as \$150 can trigger the full two-year fee ban, regardless of whether anything improper occurred, and the process for seeking relief is slow and expensive. The SEC also found that the rule is:

- / Hard to apply, with ongoing confusion over who counts as a covered "official" or "associate";
- / Discourages ordinary political participation, with roughly 12% of surveyed advisers banning all employee contributions outright;
- / Complicates hiring because a new employee's past contributions can trigger penalties; and
- / Can hurt the very pension plans it protects by limiting their choice of managers.

Chairman Paul S. Atkins called the rule "overly prescriptive," Commissioner Mark Uyeda noted that enforcement has rarely uncovered actual corruption, and Commissioner Hester Peirce framed the change as protecting political speech.

By proposing rescission, the SEC is not blessing pay-to-play. Its position is that these practices were already illegal before 2010 and would remain so under the anti-fraud and fiduciary provisions of the Advisers Act (Sections 206(1), (2), and (4)), which the SEC will continue to enforce.

If the current rule is rescinded, the SEC will likely rely on these three existing requirements:

- / The Compliance Rule (206(4)-7), which requires registered advisers to maintain tailored, annually reviewed policies covering risk assessment, pre-clearance, contribution thresholds, solicitor controls, monitoring, and remediation;
- / The Code of Ethics Rule (204A-1), which reflects advisers' fiduciary obligations;
- / The Books and Records Rule (204-2), which would drop the specific pay-to-play recordkeeping paragraph but still require core compliance, code of ethics, and government-client records. In practice, many advisers will choose to keep contribution-tracking controls as a matter of prudence, even without a specific mandate.

Status and parallel regimes

The proposal does not immediately change current law or establish a transition period, so managers should continue pre-clearance, lookback diligence, and recordkeeping. Any final rescission could face delay or legal challenge and may not eliminate the consequences of contributions made before the rule changes. The proposal has also drawn opposition, so the SEC will need to build a strong rulemaking record showing why the rule is no longer needed and addressing opponents' concerns about corruption risk.

Separately, Peirce asked whether related regimes should also be rescinded, namely Municipal Securities Rulemaking Board (MSRB) Rule G-37 (on which Rule 206(4)-5 was modeled), Exchange Act Rule 15Fh-6 (security-based swap dealers), and Financial Industry Regulatory Authority (FINRA) Rule 2030. These remain in place, and the SEC could rescind the adviser rule without touching them, so sponsors should assume that FINRA-registered placement agents, municipal advisors, affiliated broker-dealers, and swap dealer affiliates may remain subject to pay-to-play restrictions even after rescission.

Impact on alternative asset managers

For sponsors of private equity, venture, real estate, private debt, and fund-of-funds vehicles, rescission would remove the federal layer, including the restriction on paying unregulated placement agents. However, the constraints on fund formation, distribution, hiring, and contracting would largely remain because state statutes, plan policies, SRO (self-regulatory organization) rules, and investor contracts operate independently of the federal rule.

Fund formation practices and structural decisions

The strictest state and local rules apply to the pension plan's investment decisions and will continue to shape how funds are structured and marketed. For instance, New York State, New York City, and the Pennsylvania Treasury bar paid placement agents altogether, including registered broker-dealers, and New York's rule applies to capital that comes in indirectly through

feeders, fund-of-funds, and similar vehicles. New Jersey requires that fund documents give its pension fund a right to terminate the relationship if a violation occurs. Rescission would change none of this.

In practice, managers should still run separate marketing tracks for plans that ban placement agents, carve those plans out of placement agent engagements and fee arrangements, and build state-required termination rights into fund documents. These tailored terms can help preserve access to strict public plans, but managers should ensure they remain fair across the investor base and workable to administer.

Fundraising compliance obligations and placement agent arrangements

Rescission would end the federal ban on paying unregistered third parties to solicit public plans, but the relief would be uneven. Registered placement agents remain subject to their own two-year pay-to-play rules under FINRA and MSRB regulations, and several states impose independent requirements. California requires placement agents to register as lobbyists and prohibits success fees, and Connecticut and New Jersey require detailed disclosure of placement fees and solicitor payments. A placement arrangement permissible for one plan may remain prohibited or require disclosure for another, so placement agent strategy will remain investor-by-investor.

Hiring and personnel policies

The federal rule's lookback has been one of its most challenging features because a new hire's past political contribution can prevent a firm from receiving fees from a government client for two years. Removing it could widen the hiring pool, particularly for candidates with government or political backgrounds. New Jersey and Connecticut, however, have their own lookback and family-member restrictions, and many investor-specific terms agreements (commonly called "side letters") mirror the federal rule. Pre-hire contribution screening should therefore continue, but it can focus on the people and roles that actually touch public-plan capital rather than applied through blanket bans.

Limited partnership agreements, side letters, and contractual pay-to-play covenants

Many fund agreements, side letters, and pension plan certifications either refer to Rule 206(4)-5 or include their own pay-to-play commitments. Those obligations may survive rescission depending on how they are drafted.

For example, if a document incorporates the rule as it existed when the agreement was signed, that version will likely continue to bind the manager, while a reference to the rule as amended may fall away.

Managers should consider related contract and compliance risks. Most-favored-nation (MFN) provisions can extend one investor's terms to others, and breaching a firm's own policies can create regulatory exposure, even without violating the underlying rule.

Managers should also inventory their agreements with public investors; identify how each pay-to-play provision is drafted; map any notice, certification, and reporting obligations; and prepare positions for future negotiations. Public investors will likely ask for more tailored contractual protections once the uniform federal standard is gone.

Impact on institutional investors

Public pension funds, fund-of-funds, and other institutional investors have relied on Rule 206(4)-5 as a uniform federal backstop when selecting managers. Without it, more of the diligence and contracting burden shifts to investors. Today, investors can rely on a manager's certification that it follows the federal rule. Under the SEC's more flexible approach, each manager's program would differ, and investors will need to evaluate its substance. The gap is widest for exempt reporting advisers, including many venture and emerging managers, which are not required to maintain formal compliance programs or codes of ethics; the SEC itself acknowledges the loss of deterrence could be greater for them.

Investors should expect to use more detailed due diligence questionnaires, stronger contractual certifications, ongoing disclosure of political contributions and placement agent arrangements, and audit rights and remedies.

Existing and future commitments to private funds

Existing commitments are largely protected. Pay-to-play terms in current fund documents may continue to bind managers after rescission, and state requirements, such as New Jersey's termination right and Connecticut's contribution restrictions, continue for the life of the investment. Investors should check whether their side letters refer to the rule as amended, which could cause protections to lapse, and amend where needed.

Future commitments would call for more manager-by-manager judgment. Large platforms with affiliated broker-dealers may keep rigorous controls, while smaller and emerging managers may adopt lighter policies that warrant closer review, and newcomers drawn into competition for public mandates may lack established compliance infrastructure. Investors should consider making pay-to-play diligence a condition of investment approval and requiring managers to identify anyone involved in sourcing or paid in connection with the investment.

Indirect exposure through fund-of-funds and manager-of-managers structures

Investors and sponsors that invest through fund-of-funds, feeders, or manager-of-managers arrangements need to look through to the underlying managers. Some state rules reach indirect investments. New York, for example, bars placement agents for state capital whether it is invested directly or indirectly, and New Jersey requires disclosure of intermediary arrangements in indirect structures. These requirements apply regardless of the federal rule. They call for flow-down provisions, diligence on underlying managers, and certifications where the upper-tier vehicle cannot see every fundraising relationship directly.

Looking ahead: State-by-state compliance remains the critical variable

Rule 206(4)-5 has functioned as a floor for pay-to-play restrictions, not a ceiling. The strictest regimes go well beyond it.

- / New York State, New York City, and the Pennsylvania Treasury impose outright placement-agent restrictions.
- / New Jersey applies a two-year contribution lookback with a lower de minimis, a 12-month pre-association lookback, mandatory fund document termination rights, bans on indirect violations, and quarterly reporting.
- / Connecticut bars state treasurer-related contributions by firm principals and their families and requires third-party fee disclosure.
- / California requires placement agent lobbyist registration, prohibits contingent fees, mandates contribution and gift disclosure, and requires annual fee and carried-interest reporting for alternative investments.

The SEC proposal does not affect any of these regimes. The Advisers Act anti-fraud and fiduciary provisions would remain, conduct unlawful before 2010 would stay unlawful, and, as the SEC and recent commentary recognize, state and local fragmentation, plan-level policies, and contractual commitments may now carry more relative weight.

Clients should therefore treat the proposed rescission not as a signal to relax compliance but as a reason to review their contractual commitments, state-level obligations, placement-agent arrangements, and investor diligence processes, and as an opportunity to rebuild policies on a risk-based foundation. The federal rule remains in effect, and even if it is rescinded, many managers may continue to be governed by state statutes, SRO rules, plan policies, and side letters.

Recommended action items

FOR ALTERNATIVE ASSET MANAGERS

- / **Maintain full compliance now.** Continue pre-clearance, lookback diligence, and Rule 204-2(a)(18) recordkeeping until any rescission is final and effective.
- / **Map the public-plan footprint.** Identify every direct and indirect governmental investor by jurisdiction, including fund-of-funds investors with New York State Common Retirement Fund or New Jersey capital and the individuals connected to each public investment.
- / **Audit fund documents.** Inventory the limited partnership agreement, side letter, and investment management agreement's pay-to-play provisions; classify each reference to Rule 206(4)-5 as static or dynamic; and map MFN exposure.
- / **Re-paper placement-agent arrangements.** Confirm carve-outs for New York State, New York City, and the Pennsylvania Treasury; California lobbyist registration and non-contingent fees; Connecticut fee affidavits; and New Jersey solicitor reporting.
- / **Recalibrate hiring protocols.** Retain pre-hire contribution vetting keyed to New Jersey's 12-month lookback, Connecticut's principal definitions, and contractual lookbacks, even if the federal lookback is eliminated.
- / **Redesign the policy, don't discard it.** Prepare a principles-based pay-to-play policy and conforming code of ethics provisions reflecting the SEC's suggested framework and applicable state law, ready to adopt upon any final rescission. In particular, exempt reporting advisers should resist retiring policies altogether.
- / **Consider commenting by November 9.** Focus comments on transition relief for existing time-outs, the treatment of exempt reporting advisers, and the interaction with FINRA Rule 2030 and MSRB Rule G-37.

FOR INSTITUTIONAL INVESTORS

- / **Review existing side letters.** Confirm that pay-to-play protections do not lapse upon rescission and seek amendments or freestanding covenants where references are dynamic.
- / **Update operational due diligence.** Revise questionnaires, certifications, and remedies to request the manager's pay-to-play policy, risk assessment, covered personnel, and contribution history, with ongoing disclosure during the commitment period.
- / **Scrutinize exempt reporting advisers.** Apply heightened diligence to exempt reporting adviser-managed vehicles, which remain subject to Advisers Act Section 206, but generally not to the Compliance Rule or Code of Ethics Rule.
- / **Strengthen flow-down provisions.** Tighten feeder, parallel, co-investment, fund-of-funds, and manager-of-managers structures to satisfy N.Y. Ret. & Soc. Sec. Law § 424-a

certifications and New Jersey intermediary-disclosure requirements.

- / **Align plan-level policies.** Coordinate with consultants and counsel to align investment policy statements and placement-agent policies to applicable state law and evaluate whether plan-level rules should be adopted or tightened if the federal rule is rescinded.
- / **Consider commenting by November 9.** Focus comments on the proposal's effect on public plan beneficiaries.

Nixon Peabody's Investment Funds practice can help managers and institutional investors evaluate the proposal, assess existing obligations, and prepare for potential changes to the pay-to-play framework. For more information on the content of this alert, please contact your Nixon Peabody attorney or:

Benedict Kwon

213.629.6164

bkwon@nixonpeabody.com

John Beals

617.345.1060

jbeals@nixonpeabody.com

John Partigan

202.585.8535

jpartigan@nixonpeabody.com

Elizabeth Nwabueze

212.940.3075

enwabueze@nixonpeabody.com