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Office of Government Ethics
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LEGAL ADVISORY

TO: Designated Agency Ethics Officials

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SUBJECT: Participation in Initial Public Offerings by Certain Employees

As you know, the Stop Trading on Congressional Knowledge Act of 2012, P.L. 112-105 (STOCK Act), established a number of new requirements for Executive Branch employees. The U.S. Office of Government Ethics (OGE) has provided guidance on many of these new requirements, including requirements for periodic transaction reporting and requirements for notification of post-employment negotiations. Recently, OGE consulted with the Office of the Ethics Counsel and the Division of Corporate Finance of the U.S. Securities and Exchange Commission (SEC) regarding section 12 of the STOCK Act, which limits the extent to which certain covered employees may participate in initial public offerings. This advisory provides guidance to agency ethics officials based on that consultation.

Section 12 of the STOCK Act, codified at section 21A(i) of the Securities Exchange Act of 1934, 15 U.S.C. § 78u-1(i) (Securities Exchange Act), provides that “[a]n individual described in section 101(f) of the Ethics in Government Act of 1978 may not purchase securities that are the subject of an initial public offering . . . in any manner other than is available to members of the public generally.” In the executive branch, individuals covered by section 101(f) are the following:

- a. the President and the Vice President;
- b. any employee who occupies a position classified above GS-15 of the General Schedule (or for which the rate of basic pay is equal to or greater than 120 percent of the minimum rate of basic pay payable for GS-15 of the General Schedule);
- c. any civilian employee in the Executive Office of the President, other than a special Government employee, who does not meet the pay threshold but who holds a commission of appointment from the President;

- d. any employee who does not meet the pay threshold but who occupies a position that OGE has determined to be of “equal classification” to positions meeting the pay threshold;
- e. any member of a uniformed service whose pay grade is at or in excess of O-7;
- f. any Administrative Law Judge appointed under 5 U.S.C. § 3105;
- g. any employee whose position is excepted from the competitive service by reason of being of a confidential or policymaking character, unless excluded from public financial disclosure filing requirements under OGE’s regulations at 5 C.F.R. § 2634.203;
- h. the Postmaster General and the Deputy Postmaster General;
- i. any member of the Board of Governors of the U.S. Postal Service and any employee of the U.S. Postal Service or the Postal Regulatory Commission who occupies a position for which the rate of basic pay is equal to or greater than 120 percent of the minimum rate of basic pay payable for GS-15 of the General Schedule; and
- j. each Designated Agency Ethics Official and OGE’s Director.

See 5 U.S.C. app. § 101(f).

Pursuant to section 21A(i) of the Securities Exchange Act, covered employees are prohibited from “purchasing” securities that are the subject of an initial public offering if done in a manner that is not available to members of the public generally. To ensure consistent advice across the Executive Branch, OGE presented the SEC staff with hypothetical scenarios illustrating when an employee would be considered to have “purchased” a security under section 21A(i) of the Securities Exchange Act. The following hypothetical scenarios therefore focus on whether the covered employee has “purchased” the securities in question.

Scenario 1

A covered employee enters Government service after terminating her previous employment with a private corporation. She continues to hold equity shares in the private corporation, which she previously received as compensation during her employment with the private corporation. A written agreement provides that her shares will convert automatically to common stock if the private corporation goes public. While she is serving in the Government, the private corporation goes public, and her shares are converted automatically to common stock.

The SEC staff explained that in its view, although this covered employee is acquiring a security that is “the subject of an initial public offering,” the employee would not be deemed to have “purchased” the shares of common stock because she received

them automatically upon conversion. Therefore, the prohibition in section 21A(i) would not apply to this scenario.

Scenario 2

A covered employee enters Government service after terminating his previous employment with a private corporation. He continues to hold equity shares in the private corporation, which he previously received as compensation during his employment with the private corporation. A written agreement provides the employee with the right to convert his shares to common stock without the payment of additional consideration if the private corporation goes public. While he is serving in the Government, the private corporation goes public. The employee subsequently elects to exercise his preexisting right to convert his shares to common stock, in accordance with the terms and limitations set forth in the agreement.

The SEC staff explained that in its view, although this covered employee is acquiring a security that is “the subject of an initial public offering,” the employee would not be deemed to have “purchased” the shares of common stock because he had a preexisting right to acquire the shares at the time of the initial public offering without the payment of additional consideration. Therefore, the prohibition in section 21(A)(i) would not apply to this scenario.

Agency ethics officials may advise employees at their agencies as to whether their positions are described in section 101(f) of the Ethics in Government Act, 5 U.S.C. app. § 101(f), which is the threshold for coverage under section 21A(i) of the Securities Exchange Act. Neither OGE nor agency ethics officials, however, will be able provide advice regarding the application of section 21A(i) of the Securities Exchange Act, which is a matter of securities law. Agency ethics officials should remind employees who are subject to section 21A(i) of the Securities Exchange Act that they are covered by the law and that they are responsible for ensuring that any purchases of securities that are the subject of an initial public offering are done in a manner that is available to the public generally. Employees should consult with their investment advisors or private attorneys to ensure that any securities they purchase meet this standard.