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Beverlye Brady, Chair
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Brig Gen (R) Edward F. Crowell (USAF)

MAILING ADDRESS
P.O. BOX 4840
MONTGOMERY, AL
36103-4840

STREET ADDRESS
RSA UNION
100 NORTH UNION STREET
SUITE 104
MONTGOMERY, AL 36104

Thomas B. Albritton
Executive Director

TELEPHONE (334) 242-2997
FAX (334) 242-0248
WEB SITE: www.ethics.alabama.gov

June 2, 2021

ADVISORY OPINION NO. 2021-05

David G. Bronner
P.O. Box 302150
Montgomery, AL 36130

Personal Gain/Confidential Information/
Investment Personnel/Retirement Systems of
Alabama

The restriction placed on RSA investment personnel regarding the trade of securities previously traded by RSA is reduced from ten days to three business days.

RSA investment personnel should not engage in any transaction with respect to any security in the RSA portfolio within three business days after any transaction by RSA with respect to that security.

Dear Dr. Bronner:

The Alabama Ethics Commission is in receipt of your request for an Advisory Opinion of this Commission, and this opinion is issued pursuant to that request.

FACTS

The facts as have been presented to this Commission are as follows:

In 1982, the Alabama Ethics Commission issued Advisory Opinion No. 673 to the Retirement Systems of Alabama (RSA) addressing two questions:

1. What limitations does the Alabama Ethics Act place upon RSA investment personnel in regard to their personal investments?
2. Under what circumstances should RSA refrain from purchasing securities identical to those held personally by an RSA employee?

In response to Question 1, the Commission determined "that RSA investment personnel should not engage in any transaction with respect to any security in the RSA portfolio within ten days after any transaction by RSA with respect to that security and further, that RSA investment personnel should not personally purchase common stock on an initial or new offering." In response to Question 2, the Commission determined that the limitations placed on RSA investment personnel regarding the purchase of securities are not to be placed on RSA investments. RSA is not prohibited "from taking advantage of an investment opportunity which might benefit the State and the members of the Retirement Systems simply because an officer or employee of the Retirement Systems happen to own some identical securities ... "

RSA now seeks an Advisory Opinion reducing the ten-day time period that RSA investment personnel are required to refrain from trading a security previously traded by RSA to a three business day time period. RSA does not seek to revise or amend Advisory Opinion No. 673 in any manner other than the reduction of the ten-day limitation to a three-business day limitation. As grounds for this request, RSA provides as follows:

The original ten-day limitation was set because RSA trades involving large amounts of securities could potentially affect the prices of those securities. It was the view at the time that ten days would be sufficient for any such potential price effect to take place. RSA investment personnel trades in such securities after the ten-day period would unlikely be viewed to have benefited from the price effect of RSA trades. However, as discussed below, there have since been significant changes in both the speed of securities transactions and the accessibility of trade data. The ten-day period should thus be shortened to reflect these changes.

In 1982, securities were traded by telephone orders and therefore, trades were executed at a slower pace making securities less liquid. Now almost 40 years later, securities are traded electronically. Trades are now executed at a much faster pace and often in real time resulting in increased liquidity.

Trades are not just executed faster than they were in 1982. They are also settled in

less time.¹ Until the early 1990s, it was market practice for trades to settle within five days of a trade being executed. In 1993, the Securities and Exchange Commission ("SEC") adopted a rule requiring that most securities transactions settle within three days of execution, shortening the so called settlement cycle from T+5 to T+3. The SEC shortened the settlement cycle primarily to reduce market risks and justified the rule by pointing to the technological capabilities of the securities industry. In 2017, the SEC further shortened the settlement cycle to T+2 and, like in 1993, said advances in technology supported a shortened settlement cycle.

Technology has also made data on market activity available significantly faster than in the early 1980s. Daily market activity is now accessible on countless websites, apps and TV channels to virtually anyone resulting in greater transparency in the market. This increased liquidity and transparency in the market makes it difficult for any organization to affect a stock's price in the overall market, thereby reducing if not eliminating any risk for front running. Thus, the drastic technological advances since 1982 in securities trading and access to market data render the ten-day limitation unnecessarily lengthy in comparison to the speed of the markets and the ease of accessibility for market participants.

Based upon these changes in trading procedures, law and technology, many retirement systems and brokerage firms now adhere to a limitation of less than ten days. See Georgia Retirement Systems (imposing a three-business day limitation for trades by the System of more than 10,000 shares); Public School and Education Employee Retirement Systems of Missouri (imposing a five-business day limitation); Tennessee Department of Treasury (imposing a one day limitation with some exceptions).²

QUESTION PRESENTED

May RSA investment personnel trade securities, which were previously traded by RSA, after a period of three business days after a transaction by RSA with respect to that security instead of a period of ten days?

¹ Trade settlement refers to the official transfer of securities to the buyer's account and the cash to seller's account.

² See Georgia Retirement Systems Internal Trading Policy § 4(b); Personal Trading Policy, The Public School and Education Employee Retirement Systems of Missouri; State of Tennessee Department of Treasury Investment Division Procedures § III. A.

ANALYSIS

A review of Advisory Opinion No. 673, considering the advancements in technology, law, and the practices of other states, indicates that the ten-day guideline is unnecessarily restrictive.

RSA investment personnel are public employees.³ They may not use their position to obtain personal gain.⁴ They may also not use confidential information obtained from their position in a way that could result in financial gain for any person or business.⁵

Since the Commission issued Advisory Opinion 1982-673, there have been advancements in securities trading: security trades are executed much faster, trade data is significantly more accessible, and the SEC has instituted a requirement that trades settle within two business days.⁶ Any advantage that an RSA employee might have from knowledge of RSA's investments regarding a security trade based on their position at RSA appears to be lost after the trade settles.

Therefore, a waiting period of three business days before engaging in a securities transaction after RSA has traded such securities will ordinarily be sufficient for RSA investment personnel to avoid using their position or confidential information for personal gain with respect to the securities transaction, absent additional facts which show use of position or confidential information. The portion of Advisory Opinion 1982-673 requiring a waiting period of ten days for RSA investment personnel to trade securities after they had been traded by RSA is overruled.

³ Ala. Code § 36-25-1(26): PUBLIC EMPLOYEE. Any person employed at the state, county, or municipal level of government or their instrumentalities, including governmental corporations and authorities, but excluding employees of hospitals or other health care corporations including contract employees of those hospitals or other health care corporations, who is paid in whole or in part from state, county, or municipal funds. For purposes of this chapter, a public employee does not include a person employed on a part-time basis whose employment is limited to providing professional services other than lobbying, the compensation for which constitutes less than 50 percent of the part-time employee's income.

⁴ Ala. Code § 36-25-5(a): No public official or public employee shall use or cause to be used his or her official position or office to obtain personal gain for himself or herself, or family member of the public employee or family member of the public official, or any business with which the person is associated unless the use and gain are otherwise specifically authorized by law. Personal gain is achieved when the public official, public employee, or a family member thereof receives, obtains, exerts control over, or otherwise converts to personal use the object constituting such personal gain.

⁵ Ala. Code § 36-25-8: No public official, public employee, former public official or former public employee, for a period consistent with the statute of limitations as contained in this chapter, shall use or disclose confidential information gained in the course of or by reason of his or her position or employment in any way that could result in financial gain other than his or her regular salary as such public official or public employee for himself or herself, a family member of the public employee or family member of the public official, or for any other person or business.

⁶ Press Release, SEC, Shortening the Trade Settlement Cycle (March 22, 2017) (on file with the SEC).

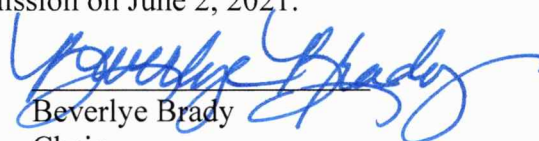
CONCLUSION

The restriction placed on RSA investment personnel regarding the trade of securities previously traded by RSA is reduced from ten days to three business days.

RSA investment personnel should not engage in any transaction with respect to any security in the RSA portfolio within three business days after any transaction by RSA with respect to that security.

AUTHORITY

By 5/0 vote of the Alabama Ethics Commission on June 2, 2021.


Beverlye Brady
Chair
Alabama Ethics Commission