

# CFTC, SEC Issue Guidance on the Applicability of Certain Regulations to Family Offices

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In November and December 2014, the Commodity Futures Trading Commission (the “CFTC”) and Securities and Exchange Commission (“SEC”), respectively, issued guidance regarding the applicability of certain regulations to family offices.

## CFTC Staff Provides Family Offices With No-Action Relief From Commodity Trading Advisor Registration

On November 4, 2014, the CFTC Division of Swap Dealer and Intermediary Oversight (the “CFTC Division”) issued no-action relief<sup>1</sup> from commodity trading advisor (“CTA”) registration to family offices in connection with advisory services provided to a “Family Client,” as defined by the SEC.<sup>2</sup> In order to claim this no-action relief, a family office must submit a notice to the CFTC Division.

### *Family Office No-Action Relief from CTA Registration*

The no-action letter supplements previous no-action relief the CFTC provided in November 2012, in Letter 12-37,<sup>3</sup> exempting family offices whose investment vehicles use CFTC-regulated products from registration as commodity pool operators (“CPO”). The previous no-action letter was silent as to relief from CTA registration. For a more complete discussion of the CFTC’s prior no-action relief, please see our client alert [here](#).

In granting relief from CTA registration, the CFTC Division agreed that “the arguments raised in favor of providing family offices no-action relief from registration as CPOs are equally applicable in the context of CTA registration.” The no-action letter cited Letter 12-37’s justifications for relief: Family offices are not the type of investment entities that warrant regulatory oversight given the relationship of the parties involved, the SEC has already granted relief to family offices and regulatory compliance is facilitated by creating parity between the application of SEC and CFTC regulations. The CFTC Division also noted that, in the past, the CFTC granted relief to particular family offices providing commodity trading advice from CTA registration.

A family office is eligible for relief from CTA registration if it meets the same guidelines that would make it eligible for relief from CPO registration under Letter 12-37. Both rely on the definition of “family office” in Rule 202(a)(11)(G)-1 under the Investment Advisers Act of 1940 as amended. Rule 202(a)(11)(G)-1(b) defines a family office as a company (including its directors, partners, members, trustees, etc.) that:

- (a) has no clients other than “family clients”;<sup>4</sup>
- (b) is wholly owned by family clients and exclusively controlled (directly or indirectly) by one or more “family members” and/or “family entities”;<sup>5</sup> and
- (c) does not hold itself out to the public as an investment adviser.<sup>6</sup>

<sup>1</sup> See CFTC Staff Letter No. 14-143, available [here](#).

<sup>2</sup> “Family Client” is defined in Rule 202(a)(11)(G)-1(d)(4).

<sup>3</sup> See CFTC Staff Letter No. 12-37, available [here](#).

<sup>4</sup> “Family clients” are defined in Rule 202(a)(11)(G)-1(d)(4).

<sup>5</sup> “Family members” are defined in Rule 202(a)(11)(G)-1(d)(6), and “family entities” are defined in 202(a)(11)(G)-1(d)(5).

<sup>6</sup> For a more complete discussion of the SEC’s family office exclusion, please see our client alert of September 14, 2011, “[SEC Adopts Rule Defining ‘Family Office’ Exclusion Under the Investment Advisers Act.](#)”

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An entity that is a family office under the definition of Rule 202(a)(11)(G)-1 is eligible for relief from CTA registration.

## *Procedure to Claim No-Action Relief*

Like relief from CPO registration, relief from CTA registration is not self-executing. Family offices must file a claim with the CFTC Division via email and, as long as it is materially complete, the claim will become effective upon filing. The claim must:

- (a) state the name, main business address and main business telephone number of the family office;
- (b) state the capacity of the family office (*i.e.*, acting as a CTA) with respect to the name of the “pools” for which the claim is being filed;
- (c) be electronically signed by (a person authorized to bind) the family office; and
- (d) be filed with the CFTC Division via email at [dsionoaction@cftc.gov](mailto:dsionoaction@cftc.gov) with the subject line “Family Office CTA Relief.”

The no-action letter does not specify whether a family office may submit a single notification to the CFTC Division for relief from both CPO and CTA registration. The CFTC Division also noted that the relief does not excuse a family office from compliance with any other applicable requirements set forth in the Commodity Exchange Act or in CFTC regulations, including antifraud provisions.

## **SEC Staff Provides Guidance on Application of the Family Office Rule to Certain Key Employee Trusts**

In December 2014, the SEC’s Division of Investment Management (the “SEC Division”) issued a guidance update (the “Update”) on the application of the Family Office Rule<sup>7</sup> (the “Rule”) of the Investment Advisers Act of 1940 as amended (the “Advisers Act”) to certain key employee trusts.<sup>8</sup>

### *Background*

The SEC adopted the Rule on June 22, 2011, under which “family offices” are excluded from the Advisers Act definition of “investment adviser” and thus not subject to the Act. The Rule is intended to provide an exclusion for investment advisers providing advice to families managing their own wealth. Under the Rule, investment

<sup>7</sup> Rule 202(a)(11)(G)-1.

<sup>8</sup> Division of Investment Management, Securities and Exchange Commission, No. 2014-13, [IM Guidance Update: Key Employee Trusts Under the Family Office Rule](#) (December 2014).

advisers are restricted to providing investment advice solely to “family clients” as defined therein.<sup>9</sup>

In order to allow family offices to attract and retain experienced investment professionals, the Rule permits family offices to include as family clients certain key employees who are not family members and certain investment entities through which key employees may invest alongside the family office.<sup>10</sup> The Update clarified the application of the Rule to certain key employee trusts that are one such type of investment entity.

The Rule defines a key employee trust as:

Any trust of which: Each trustee or other person authorized to make decisions with respect to the trust is a key employee; and each settlor or other person who has contributed assets to the trust is a key employee or the key employee’s current and/or former spouse or spousal equivalent...<sup>11</sup>

Trusts of which the key employee is the sole individual authorized to make decisions on behalf of the trust and the sole contributor to the trust are family clients under the definition.<sup>12</sup> The SEC Division released the Update in response to questions on whether: (1) decision-making powers may be bifurcated between a key employee and non-key employee, and (2) the key employee contributing assets to the trust must also be the key employee authorized to make decisions with respect to the trust.

### *Bifurcation of Decision-Making Powers Between Key Employees and Non-Key Employees*

The Update stated that it is the view of the SEC Division staff that administrative decisions may be made by a non-key employee for a key employee trust, provided that investment decisions are made by a key employee. The Division provided the following examples of purely administrative duties that do not involve investment decisions: preparing and filing taxes for the trust, keeping records for the trust and distributing periodic statements or disclosures to trust beneficiaries.

<sup>9</sup> Rule 202(a)(11)(G)-1(b)(1).

<sup>10</sup> Rule 202(a)(11)(G)-1(d)(4).

<sup>11</sup> Rule 202(a)(11)(G)-1(d)(4)(x).

<sup>12</sup> *d.* The rule also allows a settlor or other person contributing assets to be a key employee’s current and/or former spouse or spousal equivalent if, at the time of contribution, the person held a joint, community property or other similar shared ownership interest in the trust with the key employee.

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The SEC Division staff noted that the release adopting the Rule states, “it is appropriate to allow the family office to advise trusts for which the key employee is the sole person making *investment* decisions” (emphasis added).<sup>13</sup> The Update explained that the SEC drew this approach from a parallel concept in the definition of “qualified purchaser” under the Advisers Act. The approach “provides ‘consistency in entities considered not to need investor protections under our rules because *investment* decisions are made solely by individuals”<sup>14</sup> that do not require the protection of SEC regulations (emphasis added).

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<sup>13</sup>*Id.* quoting Family Offices, Investment Advisers Act Release No. 3220 at 37990 (June 22, 2011) 76 FR 37983 (June 29, 2011).

<sup>14</sup>*Id.*

## *Bifurcation of Decision-Making Powers Between Key Employees*

The Update also clarified that it is acceptable for one key employee to make investment decisions on behalf of another key employee’s trust. The SEC Division noted that such an arrangement would continue to result in all investment decisions being made solely by a key employee within the requirements of the Rule and is therefore acceptable.