IPI REPORT ABSTRACT

The Dodd Frank Act: Implications for Family Offices

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The Dodd Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act") effected sweeping financial regulations including delineation of those family offices exempt from registration as a registered investment advisor ("RIA") under the Investment Advisers Act of 1940.

The old rules which exempted family offices with fewer than 15 clients under the Private Adviser Exemption or those with under $25M in assets under management were replaced with much more specific, better delineated rules (section 409) with significantly more complexity. Pursuant to these rules a family office is defined as an office which:

1. has no clients other than family clients;
2. is owned and controlled by family clients; and,
3. does not hold itself out as an investment adviser.

Further, family clients are defined as any family member, any key employee, charities funded exclusively by the family, entities owned, controlled by and for the exclusive benefit of the family, and former family members and former key employees. A key employee is defined as a natural person who is an executive director, trustee, general partner or person with similar level of function or duties who has been with the family at least 12 months.

Dodd-Frank is a global law which specifically provides for extra-territorial application and enforcement. The rules also provide that the SEC is specifically directed to share any information it discovers with other government agencies such as the IRS and Department of Justice.

Overall, the reaction of most single family offices ("SFOs") has been to undertake all possible herculean steps in order to avoid registration. This often extreme reluctance to register as an RIA stems primarily from the perception of increased costs and unwelcome administrative work, loss of privacy and confidentiality, and unwelcome government intervention into private lives. The most common approaches include jettisoning the investment function, eliminating funds and qualified plans which include non-family client investors and making contributions of non-family client funds held in foundations.

For SFOs who elected to register, the investment activity is almost always isolated in a separate RIA entity which does not perform any other family office services. In the course of conducting reviews, it became apparent that many SFOs have other financial regulatory issues which were not adequately addressed. These issues include registration as a broker-dealer, registration with the CFTC and other SEC reporting and registration obligations.

Both registered and unregistered SFOs should maintain records documenting their compliance with Dodd-Frank, including the results of any analyses undertaken. Such compliance files should be maintained on an on-going basis and updated at least

annually. Significant unanswered questions remain, particularly involving joint and collaborative investments, key employees and best practices.

It is likely that greater clarity in defining the family office exemption will result in greater scrutiny, higher levels of compliance, more onerous sanctions and more complicated family office structures. In time, this is likely to result in higher costs for SFOs which will raise the assets under management hurdle to their formation and accelerate the outsourcing trend to MFOs and other outside RIAs.