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Family Office Insights

Modifications to the Volcker Rule Regarding Family Wealth Management Vehicles

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In late June, five federal financial regulatory agencies (the Department of the Treasury, the Federal Reserve System, the Federal Deposit Insurance Corporation, the Commodity Futures Trading Commission, and the Securities and Exchange Commission) published the long awaited final revisions to the regulations implementing Section 13 of the Bank Holding Company Act (the "BHCA"), also known as the "Volcker Rule".

The amendments modify the Volcker Rule's prohibition on banking entities investing in or sponsoring hedge funds or private equity funds—known as "covered funds". Prior to these amendments, family wealth management vehicles (as discussed below) were included within the definition of "covered funds". Under the Volcker Rule, banking entities are generally prohibited from engaging in proprietary trading and from acquiring or retaining ownership interests in, sponsoring, or having certain relationships with covered funds.

Changes to the Volcker Rule

Effective October 1, 2020, among many other changes, the amended Volcker Rule will exclude "family wealth management vehicles" from the definition of "covered funds". This will permit banking entities to structure services or transactions for customers that are "family wealth management vehicles" without the Volcker Rule's restrictions, and to sponsor or advise those vehicles, even if the vehicle relies on Section 3(c)(1) or 3(c)(7) of the Investment Company Act or would otherwise be a covered fund under the regulations.

As defined in the Volcker Rule amendments, a "family wealth management vehicle" is (i) a trust where the grantor(s) are family customers (as defined in the Rule) or (ii) a non-trust entity in which family customers own a majority of the voting interests (directly or indirectly) as well as a majority of interests in the entity. Generally, ownership of non-trust family wealth management vehicles is limited to family customers and up to five "closely-related persons" of those family customers. However, under a *de minimis* exception in the amended Rule, one or more entities, including a banking entity, that are not family customers or closely related persons may acquire or retain up to an aggregate 0.5% interest in the family wealth management vehicle to establish corporate separateness or address bankruptcy, insolvency, or similar concerns.

For a banking entity to rely on the exclusion, there are several conditions that must be met. For example, the banking entity must provide bona fide trust, fiduciary, investment advisory, or commodity trading advisory services to the family wealth management vehicle, and the banking entity may not, directly or indirectly, guarantee, assume, or otherwise insure the obligations or performance of the family wealth management vehicle.

For family offices, the Volcker Rule amendments provide greater flexibility for banking entities to engage in transactions with family entities that qualify as "family wealth management vehicles", and should lead to broader service offerings and the availability of a wider range of potential investment and transaction structures from banking entities to family offices.

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