Family Office Insights

Family Offices and the Investment Advisers Act: Navigating the Family Office Rule and SEC Guidance

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Introduction

In managing the wealth and investments of a family, a family office frequently provides advice regarding investments in securities, manages investment portfolios, and oversees other financial matters on behalf of family members. While these activities are central to the purpose of many family offices, they may also cause a family office to fall within the broad regulatory framework of the Investment Advisers Act of 1940, as amended (Advisers Act).

The Advisers Act generally regulates people and entities that provide investment advice regarding securities for compensation. Because a family office often provides investment advice to family members and related entities, it may be considered an "investment adviser" unless it qualifies for an applicable exemption or exclusion.[1]

Historically, many family offices relied on the private adviser exemption under Section 203(b)(3) of the Advisers Act, which allowed certain advisers with fewer than 15 clients to avoid registration. The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act) eliminated that exemption and directed the Securities and Exchange Commission (SEC) to establish a separate exclusion specifically for family offices.[2]

In response, the SEC adopted Rule 202(a)(11)(G)-1 under the Advisers Act, commonly referred to as the "Family Office Rule." The rule excludes qualifying family offices from the definition of investment adviser, allowing them to avoid registration and most substantive requirements applicable to registered investment advisers.

Because the Family Office Rule provides an exclusion rather than merely an exemption from registration, understanding its requirements is essential. A family office that does not satisfy the Rule may need to restructure its operations, seek exemptive relief from the SEC, or register as an investment adviser.

The Investment Advisers Act

The Advisers Act was enacted to protect investors by establishing a regulatory framework for people and entities engaged in the business of providing investment advice. The Act imposes registration, disclosure, recordkeeping and conduct requirements intended to promote transparency and prevent fraudulent practices.

Section 202(a)(11) of the Advisers Act defines an "investment adviser" broadly as any person or firm that:

1. for compensation
2. is engaged in the business of
3. providing advice to others or issuing reports or analyses regarding securities.

A person or entity generally must satisfy all three elements to fall within the definition of "investment adviser. The term "securities" is broadly interpreted and includes common investment instruments such as stocks, bonds and other financial products. It also includes investment contracts, as described under the Howey Test.[3]

Investment advisers that fall within this definition generally must register with the SEC or applicable state securities regulators unless an exclusion or exemption applies.

1 "Institutional investment manager" is an entity that either invests in, or buys and sells, securities for its own account, and or a natural person or an entity that exercises investment discretion over the account of any other natural person or entity. Section 3(a)(9) of the Securities Exchange Act and Section 13(f)(6)(A) of the Advisers Act.

2 Section 202(a)(11)(G) of the Advisers Act.

3 *SEC v. W.J. Howey Co.*, 328 U.S. 293 (1946) (establishing the "Howey test" for determining whether a transaction constitutes an investment contract under US securities law).

Registered investment advisers are subject to ongoing obligations, including filing Form ADV; maintaining books and records; providing disclosures regarding services and conflicts of interest; and appointing a chief compliance officer to maintain compliance with rules governing advertising, custody and fiduciary obligations, to name a few.

The Advisers Act contains several exemptions from registration, including exemptions for certain venture capital advisers,[4] private fund advisers,[5] certain foreign advisers,[6] institutional investors[7], and non-US advisers with limited US activities.[8] However, these exemptions generally remove only the registration requirement and do not eliminate the adviser's status as an investment adviser or the application of other Advisers Act obligations.

Under the Family Office Rule, however, a qualifying family office is excluded from the definition of investment adviser entirely. As a result, a family office that satisfies the requirements of the rule generally avoids not only registration requirements but also most substantive provisions of the Advisers Act.

The Family Office Rule

The adoption of the Family Office Rule was largely driven by the SEC's recognition that families who establish dedicated offices to manage their own wealth are typically financially sophisticated and do not require the same regulatory protections as unrelated investors.

Under the Family Office Rule, a family office is a company, including its directors, partners, members, managers, trustees and employees acting within the scope of their employment, that satisfies three requirements:

1. The family office provides investment advice only to "family clients"
2. The family office is wholly owned by family clients and controlled exclusively by family members and/or family entities

The family office does not hold itself out to the public as an investment adviser

The SEC has emphasized that the exclusion is intended for single-family offices. A family office may not rely on the rule if it is effectively operating as a multi-family office. For example, multiple families cannot establish separate offices while sharing the same or substantially similar personnel in an effort to avoid Advisers Act regulation.

i. Family client

The requirement that a family office provide investment advice only to "family clients" is the most detailed aspect of the Family Office Rule. The definition includes several categories of individuals and entities connected to the family, including family members, former family members, key employees, former key employees, certain trusts, estates, charitable organizations and family-owned entities.

a. Family members

The definition of "family member" generally includes all lineal descendants of a designated common ancestor, whether living or deceased,[9] and their spouses or spousal equivalents, provided they are within ten generations of that common ancestor.[10]

The definition is intentionally broad and recognizes modern family structures. It includes adopted children, stepchildren and foster children, as well as spouses and spousal equivalents of qualifying family members.

The designated common ancestor determines the scope of the family for purposes of the rule. The common ancestor may be living or deceased, and the designation may be changed over time as family circumstances evolve.

However, the definition does not generally extend to in-laws. For example, a family member's sibling's spouse would not qualify solely because of that relationship. The SEC has addressed these types of situations through limited exemptive orders, discussed below, but absent such relief, providing investment advice to certain in-laws may cause a family office to lose its eligibility under the Family Office Rule.

The rule also recognizes "former family members." A former spouse, former spousal equivalent or former stepchild who was previously a family member but is no longer part of the family due to divorce or a similar event may continue to qualify as a family client.

Unlike former key employees, former family members generally may continue to make investments through the family office after the relationship ends.

b. Key employees

The Family Office Rule also permits certain key employees of the family office to qualify as family clients. This provision allows family offices to provide investment opportunities to important employees while aligning those employees' interests with the family.

4 Section 203(l) of the Advisers Act.

5 Section 203(m)(1) of the Advisers Act.

6 Section 203(a)(30) of the Advisers Act.

7 Section 202(a)(11)(A) of the Advisers Act.

8 Section 214(b) of the Advisers Act.

9 "Lineal descendants" include adopted children, stepchildren, foster children and any individual who was a minor when another family member became that individual's legal guardian.

10 "Spousal equivalent" means a cohabitant in a relationship generally equivalent to a spousal relationship. The family office later may designate a different common ancestor to maintain qualification as a family office, but such a change would alter the individuals who would then qualify as family members.

A "key employee" generally includes an executive officer, director, trustee, general partner or individual serving in a similar capacity.[11] It also includes employees who participate in the investment activities of the family office as part of their regular duties, provided they have performed those functions for at least 12 months.

The definition may also include key employees of an affiliated family office[12], as well as certain trusts established by key employees. A key employee's spouse or spousal equivalent may qualify with respect to jointly owned, community property or similar shared ownership interests.

The definition excludes employees whose responsibilities are limited to clerical, secretarial or administrative functions. Employees who do not participate in investment activities generally will not qualify simply because they hold an important role within the family office.

Former key employees may remain family clients, but their ability to participate is limited. Generally, a family office may continue providing investment advice only with respect to assets that were already managed by the family office before the employee's departure. Unlike former family members, former key employees generally cannot make new investments through the family office after leaving employment.[13]

c. Estates and trusts

The Family Office Rule includes certain estates and trusts within the definition of family client to accommodate common estate planning structures.

The estate of a current or former family member, key employee or former key employee may qualify as a family client during the period of estate administration, even if the ultimate beneficiaries are not themselves family clients.

Trusts may also qualify depending on their structure. Revocable trusts established solely by family clients generally qualify as family clients. Certain irrevocable trusts may also qualify where the current beneficiaries consist solely of family clients or other permitted charitable beneficiaries. The rule also permits certain trusts established by key employees to qualify where the key employee, or a qualifying spouse or spousal equivalent, is responsible for funding and decision-making authority over the trust.

d. Charitable organizations

The definition of "family client" includes certain nonprofit organizations, charitable foundations and charitable trusts that are funded exclusively by one or more family clients. This provision allows families to continue using their family office structure to manage charitable assets.

However, the organization must remain funded exclusively by family clients. Contributions from unrelated people may cause the organization to lose its status as a family client.

e. Family entities

The Family Office Rule also includes entities wholly owned by, and operated solely for the benefit of, one or more family clients. This provision allows family offices to provide investment advice through common structures, such as holding companies and pooled investment vehicles. However, introducing a nonfamily investor into such an entity may jeopardize its eligibility under the rule.

f. Grace period for involuntary transfers

The Family Office Rule provides a limited grace period for involuntary transfers of assets. If a person who is not otherwise a family client receives assets from a family client through an involuntary transfer, such as upon the death of a family client, the recipient may be treated as a family client for one year following completion of the transfer of legal title.[14]

ii. Ownership and control requirements

In addition to limiting its services to family clients, a family office must satisfy certain ownership and control requirements to qualify for the Family Office Rule exclusion. The family office must be wholly owned by family clients and controlled exclusively by family members and/or family entities.[15] This requirement ensures that the family office remains a private structure designed to manage family wealth rather than operate as a commercial investment advisory business.

The Rule permits certain key employees to hold ownership interests in a family office, allowing families to provide incentives and retain investment professionals. However, key employees may not control the family office. Control must remain with family members or family entities.

For purposes of the Rule, "control" generally means the power to exercise a controlling influence over the management or policies of a company. Under the Advisers Act, a person is presumed to control if they directly or indirectly have the right to vote 25% or more of a class of the issuer's voting securities. Accordingly, family offices should carefully review their governing documents, voting arrangements and ownership structures to ensure that control remains consistent with the Family Office Rule.

11 An "executive officer" is the family office's president, a vice president in charge of a principal business unit, division or function (such as administration or finance), any other officer who performs a policymaking function or any other person who performs similar policymaking functions.

12 An affiliated family office is an entity wholly owned by family clients of another family office, controlled (directly or indirectly) by one or more family members of that other family office and/or family entities affiliated with the other family office, and that only serves the family clients of the other family office.

13 The family office also may advise as to investments that a former key employee was contractually obligated to make pursuant to agreements in effect before they ceased to be a key employee.

14 Family Offices, Investment Advisers Act Release No. 3225 (June 22, 2011), promulgating Advisers Act Rule 202(a)(11)(G)-1 (b)(1).

15 Under the Investment Advisers Act of 1940 (Advisers Act), the term "control" is defined in Section 202(a)(1) (15 U.S.C. § 80b2). "Control" means the power to exercise a controlling influence over the company's management or policies unless such power results solely from being a company officer. A person is presumed to control a company if they beneficially own, directly or indirectly, more than 25% of the voting securities of that company.

iii. No holding out as an investment adviser

The final requirement of the Family Office Rule is that a family office may not hold itself out to the public as an investment adviser.

This requirement reflects the SEC's view that the exclusion is intended for private offices established to manage the wealth of a single family, not commercial advisory firms providing investment services to unrelated clients.

A family office that markets investment advisory services, solicits outside investors or otherwise presents itself as available to provide investment advice to the public may no longer qualify for the Family Office Rule exclusion. In such circumstances, the family office may become subject to registration and other requirements under the Advisers Act.

However, a family office that previously registered as an investment adviser and later withdraws its registration to rely on the Family Office Rule is not automatically disqualified solely because it previously held itself out as an investment adviser while registered.

SEC exemptive relief for additional family clients

Although the Family Office Rule provides detailed categories of people and entities that qualify as family clients, the SEC has recognized that certain family relationships may not fit neatly within the rule's technical definitions. As a result, the SEC has granted a limited number of exemptive orders permitting family offices to provide investment advice to certain additional family clients who would otherwise not qualify.[16]

These exemptive orders have generally involved close relatives by marriage or other individuals with longstanding familial relationships, including:

- Parents-in-law[17]
- Siblings-in-law[18]
- A sister-in-law and related irrevocable trust[19]
- A niece of a family client[20]

The SEC has emphasized that such exemptive relief is evaluated on a case-by-case basis. However, the SEC has generally considered several recurring factors when determining whether relief is appropriate, including:

- Whether the additional family clients are limited in number
- Whether the proposed arrangement would change the nature of the family office into a commercial advisory business
- Whether the additional family clients represent only a small percentage of the family office's overall assets under management
- Whether the relationship reflects an existing familial connection that has existed for a number of years[21]
- Whether the family office remains controlled by qualifying family members and family entities
- Whether there is any public interest concern requiring registration under the Advisers Act

The SEC has also examined the ownership interests of additional family clients and the percentage of assets attributable to qualifying family clients. The exemptive orders provide useful insight into the circumstances in which the SEC has been willing to provide relief.

For example, in exemptive orders involving parents-in-law, the additional family clients generally did not hold an ownership interest in the family office, and qualifying family clients represented approximately 75% to 90% of total assets for which the family office provided investment advice. [22]

Similarly, in exemptive orders involving siblings-in-law, the additional family clients generally did not hold an ownership interest in the family office, and qualifying family clients represented approximately 75% to 95% of total assets managed by the office.[23]

In one exemption involving a sister-in-law and an irrevocable trust of which she was a beneficiary, the additional family clients collectively held less than a 5% membership interest in the family office. In that case, assets beneficially owned by qualifying family clients represented at least 75% of total assets under management.[24]

The SEC has also granted relief involving a niece of a family client, where the niece held no ownership interest in the family office, and qualifying family clients represented 100% of the assets managed by the office.[25]

16 Family Offices, Investment Advisers Act Release No. 3220 (June 22, 2011).

17 See Investment Advisers Act Release No. IA-3867 and IA-4902 respectively.

18 See Investment Advisers Act Release No. IA-5602 and IA-3990 respectively.

19 See Investment Advisers Act Release No. IA-4066.

20 See Investment Advisers Act Release No. IA-5690.

21 "Nine years" was cited in one application that the SEC approved. See Investment Advisers Act Release No. IA-4066.

22 See Investment Advisers Act Release No. IA-3867 and IA-4902 respectively.

23 See Investment Advisers Act Release No. IA-5602 and IA-3990 respectively.

24 See Investment Advisers Act Release No. IA-4066.

25 See Investment Advisers Act Release No. IA-5690.

Grandfathered family offices

The Dodd-Frank Act included a limited grandfathering provision for certain family offices that were not required to register under the Advisers Act as of January 1, 2010, but would not satisfy the Family Office Rule solely because they provided investment advice to certain people.[26]

A grandfathered family office may continue operating without registration under the Advisers Act. However, unlike family offices relying on the Family Office Rule, grandfathered offices remain subject to certain anti-fraud provisions of the Advisers Act.[27]

Because this grandfathering provision is narrow, family offices should carefully evaluate whether they continue to qualify under the applicable requirements.

Other securities law considerations

Although the Family Office Rule provides significant relief from Advisers Act regulation, family offices should be aware that other federal securities laws may continue to apply.

Section 13(f) and Form 13F Reporting

One important consideration is Section 13(f) of the Securities Exchange Act of 1934, as amended (Exchange Act).

Section 13(f) requires certain institutional investment managers exercising investment discretion over accounts holding at least US$100 million in specified securities to file reports with the SEC on Form 13F.[28] Importantly, these requirements apply regardless of whether an entity is registered as an investment adviser under the Advisers Act. The Family Office Rule does not provide an exclusion from Section 13(f). Accordingly, a family office may be exempt from Advisers Act registration but still be required to file Form 13F reports.[29]

Family offices should therefore evaluate whether their investment activities, particularly investments in publicly traded securities, cause them to meet the definition of institutional investment manager for purposes of Section 13(f).

Section 13(d), 13(g) and Schedule 13G or Schedule 13D

An individual, family office, trust, or pooled investment vehicle is required to file SEC Schedule 13G when it owns more than 5% of a public company's voting stock and qualifies as a passive, institutional or exempt investor under Section 13(d) and 13(g) of the Exchange Act. 13G is a short-form alternative to the more demanding Schedule 13D, and it tells the public who is quietly accumulating large stakes in US-listed companies.

Missing a Schedule 13G deadline is not a small slip. The SEC charged dozens of investors and insiders in a September 2024 sweep for late beneficial ownership filings, with penalties reaching US$750,000 per filer. According to the SEC Division of Economic and Risk Analysis, more than 25,000 Schedule 13G filings hit EDGAR every year, making it one of the most common ownership disclosures in U.S. capital markets. If these provisions are applicable, please consult with your legal adviser.

Form N-PX Reporting

Certain Form 13F filers may also be required to file annual reports on Form N-PX relating to their proxy voting activities.

These filings disclose certain voting decisions regarding executive compensation matters and other shareholder proposals. Family offices exercising voting authority over public company securities should consider whether these reporting requirements apply.

Short sale reporting requirements

Family offices should also be aware of additional reporting obligations related to short-sale activity. Under Exchange Act Rule 13f-2 and related Form SHO requirements, certain institutional investment managers may be required to report qualifying short positions exceeding specified thresholds. These obligations apply independently of Advisers Act registration status. Therefore, a family office relying on the Family Office Rule exclusion may still have reporting obligations under the Exchange Act.

26 These include the following categories of persons for whom a family office was engaged in providing advice before January 1, 2010: (i) individuals who, at the time of the applicable investment, were officers, directors or employees of the family office who invested with the family office before January 1, 2010, and are accredited investors under the Securities Act of 1933, Regulation D; (ii) any company owned exclusively and controlled by one or more family members; and (iii) any investment adviser registered under the Advisers Act that provides investment advice and identifies investment opportunities to the family office and invests in such transactions on substantially the same terms as the family office but does not invest in other funds advised by the family office, and whose assets as to which the family office directly or indirectly advises represents 5% or less of the total assets as to which the family office provides investment advice. (Of course, persons referenced in categories (i) and (ii) may also fall within the definition of "family client".)

27 Family Offices, Investment Advisers Act Release No. 3220 (June 22, 2011), promulgating Advisers Act Rule 202(a)(11)(G)-1 (b)(1).

28 Advisers Act Section 202(a)(11)(G) and Advisers Act Rule 202(a)(11)(G)-1.

29 Exchange Act Section 13(f)(6)(A).

Conclusion

Family offices frequently provide investment advice regarding securities and therefore may fall within the broad definition of investment adviser under the Advisers Act. The Family Office Rule provides an important exclusion that allows qualifying family offices to manage family wealth without becoming registered investment advisers.

However, the requirements of the Family Office Rule are highly technical. Family offices must carefully monitor their relationships with clients, ownership and governance structures, employee participation arrangements and investment activities to ensure continued compliance. The SEC's exemptive orders demonstrate that limited flexibility may be available when family offices seek to include closely connected individuals who fall outside the technical definition of family client.

Finally, family offices should remember that compliance does not end with the Advisers Act. Even a family office that qualifies for the Family Office Rule exclusion may remain subject to other federal securities law obligations, including Exchange Act reporting requirements.

A thorough understanding of the Advisers Act, the Family Office Rule and related securities law obligations is therefore essential for family offices seeking to preserve the benefits of private wealth management structures while maintaining regulatory compliance.

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