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November 16, 2010

Ms. Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

Re: Request for Comment on Proposed Rule Under the Investment Advisers Act of 1940 Regarding Defining "Family Offices"; File No. S7-25-10

Dear Ms. Murphy:

We submit this letter in response to the request of the U.S. Securities and Exchange Commission (the "Commission") in Release No. IA-3098 (the "Release")[1] for comment on proposed rule 202(a)(11)(G)-1 (the "Proposed Rule") under the Investment Advisers Act of 1940 (the "Advisers Act"),[2] which would define family offices for purposes of excluding them from the definition of "investment adviser" under the Advisers Act. Specifically the Proposed Rule would define a family office as a company that: (i) has no clients other than "family clients;"[3] (ii) is wholly-owned and controlled by "family members;"[4] and (iii) does not hold itself out to the public as an investment adviser.[5] The consequence of a family office being excluded from the definition of "investment adviser" is that it would not be subject to any of the provisions of the Advisers Act.[6]

We appreciate the opportunity to comment on the Proposed Rule and the Release. Seward & Kissel LLP has a substantial number of clients who would be affected by the adoption of the Proposed Rule. We respectfully submit the following comments and request that the

[1] Family Offices, Advisers Act Release No. IA-3098, 75 Fed. Reg. 63,753 (proposed October 12, 2010) (to be codified at 17 C.F.R. Part 275).
[2] Investment Advisers Act of 1940, 15 U.S.C. §§ 80b (2008).
[3] Proposed Rule 202(1)(11)(G)-1(b)(1).
[4] Proposed Rule 202(1)(11)(G)-1(b)(2).
[5] Proposed Rule 202(1)(11)(G)-1(b)(3).
[6] Release, at 63,755.

Commission consider them before adopting the Proposed Rule. The views we express in this letter, however, are our own and do not necessarily reflect those of our clients.

I. Background and Purpose of the Proposed Rule

Historically, family offices have been structured to rely on the current private adviser exemption from registration with the Commission for investment advisers with fewer than 15 clients (the "Private Adviser Exemption") or on exemptive orders granted by the Commission.[7] The Dodd-Frank Wall Street Reform and Consumer Protection Act[8] (the "Dodd-Frank Act") repealed the Private Adviser Exemption, but created a new exclusion from the definition of investment adviser under the Advisers Act for family offices, as defined by the Commission.[9] The Dodd-Frank Act requires the Commission to adopt a definition of family office that is consistent with its previous exemptive orders and that recognizes the range of organizational, management and employment structures and arrangements employed by family offices.[10]

According to the Release, the core policy judgment of the Proposed Rule, which formed the basis of the Commission's prior exemptive orders, was the lack of need for application of the Advisers Act to a typical single-family office.[11] The Commission explained in the Release that the Advisers Act was not designed to regulate the interactions of family members in the management of their own wealth.[12] Accordingly, most of the conditions of the Proposed Rule, like the Commission's prior exemptive orders, operate to restrict the structure and operation of a family office that would rely on the Proposed Rule to activities unlikely to involve commercial advisory activities, while permitting traditional family office activities involving charities, tax planning and pooled investing.[13] The Commission has also indicated that the Proposed Rule, consistent with its prior exemptive orders, seeks to distinguish between a "family office," that would provide investment advice to a single family, and a "family-run office" that, although owned and controlled by a single family, provides advice to a broader group of clients and much more resembles the business model common among many small investment adviser firms that are registered with the Commission or state regulatory authorities.[14]

II. The Commission Should Broaden the Definition of Founder

The Commission should broaden the definition of "founder" to allow multiple family members who are not spouses or spousal equivalents of one another to establish family offices. Under the Proposed Rule, founder means "the natural person and his or her spouse or

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[7] *Id.*, at 63,754.
[8] 10 Pub. L. 111–203, 124 Stat. 1376 (2010).
[9] *See* section 409 of the Dodd-Frank Act.
[10] *Id.*
[11] Release, at 63,755.
[12] *Id.*
[13] *Id.*
[14] *See id.*, at 63,754.

spousal equivalent for whose benefit the family office was established and any subsequent spouse of such individuals."[15] It seems reasonable to us that other combinations of family members could establish a family office for the benefit of their family, but the definition of founder under the Proposed Rule does not allow for multiple founders who are not spouses or spousal equivalents. Under the Proposed Rule, if two siblings, for example ("Sibling-Founders"), desired to establish a family office, the Sibling-Founders would be forced to choose which Sibling-Founder (with his or her spouse or spousal equivalent) would be the founder of the family office, and, accordingly, which Sibling-Founder's spouse or spousal equivalent's parents, siblings and lineal descendants (including by adoption and stepchildren) and such lineal descendants' spouses or spousal equivalents ("In-Laws") would be permitted to invest with the family office. In order to allow both Sibling-Founders' In-Laws to invest with a family office, the Sibling-Founders would be required to establish two family offices.

Similarly, under the Proposed Rule, if a parent and a child, for example, desired to establish a family office, the parent and child would be forced to choose whether the parent or the child would be the founder of the family office, impacting the identities of the family clients. If the child was the founder, the parent's parents (*i.e.*, the child's grandparents), the parent's siblings and the parent's siblings' spouses or spousal equivalents and their lineal descendants (including by adoption and stepchildren) and such lineal descendants' spouses or spousal equivalents would not be permitted to invest with the family office. On the other hand, if the parent was the founder of the family office, the parents of the child's spouse or spousal equivalent and their respective siblings and their lineal descendants (including by adoption and stepchildren) and such lineal descendants' spouses or spousal equivalents would not be permitted to invest with the family office. To prevent anomalous and unreasonable outcomes such as these, the Commission should broaden the definition of founder to allow multiple family members who are not spouses or spousal equivalents of one another to establish family offices.

Indeed, in the *Parkland Management Company, L.L.C.* Exemptive Order[16] (the "*Parkland Order*"), the Commission issued an exemption for a family office that provided investment advice to family members with a similar relationship than that of the prohibited family-client relationships described above.[17] The family office for which the Commission granted exemptive relief in the *Parkland Order* provided investment advice to, among others, a founder's lineal descendant's spouse's sister, mother and the sister's two children.[18] Although we recognize that the Proposed Rule would not (and could not) match the exact representations, conditions or terms contained in every exemptive order, as the exemptive orders varied to accommodate the particular circumstances of each family office,[19] in the *Parkland Order*, the Commission did not impose any conditions on the provision of investment advice by the family office to the founder's lineal descendant's spouse's sister, mother and the sister's children.

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[15] Proposed Rule 202(1)(11)(G)-1(d)(5).
[16] Investment Advisers Act Release Nos. 2362 (Feb. 24, 2005) [70 FR 10155 (Mar. 2, 2005)] (notice) and 2369 (Mar. 22, 2005) (order).
[17] *See id.*
[18] *See id.*
[19] *See* Release, at 63,755.

Instead, the Commission recognized, as it should here, that families establishing family offices should be provided the flexibility to choose the appropriate person or persons to be the founders of the family office. Because of the Dodd-Frank Act's mandate that the Proposed Rule be consistent with the Commission's prior exemptive orders, and to avoid the anomalous and unreasonable results of two or more immediate family members establishing multiple family offices to provide investment advice to the same family, the Commission should broaden the definition of founder to allow multiple family members who are not spouses or spousal equivalents of one another to establish family offices.

Just as it did in the Proposed Rule for stepchildren, the Commission should broaden the definition of founder, as described above, based on its understanding of the described family members' close ties to family members who are included in the Proposed Rule, and on the fact that doing so would leave to the founders whether they wish to include such family members as part of the family office clientele.[20] Moreover, allowing family offices to provide investment advice to such family members comports with the Commission's stated policy judgment that the Advisers Act was not designed to regulate the interactions of family members in the management of their own wealth.[21] Broadening the definition of founder, as described above, would also not permit a family office to engage in commercial advisory activities, but would merely permit traditional family office activities to be conducted within an extended family. Indeed, a family office that provides investment advice to the family members described above could not fairly be characterized as a "family-run office" that resembles the business model common among many small investment adviser firms that are registered with the Commission or state regulatory authorities.[22]

III. The Commission Should Broaden the Definition of Key Employee

The Commission should broaden the definition of key employee to include all employees of the family office who are likely to be in a position or have a level of knowledge and experience in financial matters sufficient to be able to evaluate the risks of investing with the family office and take steps to protect themselves. Under the Proposed Rule, "key employee" means a natural person who is (i) an executive officer, director, trustee, general partner or person serving in similar capacity, or (ii) other employee of the family office (other than an employee performing solely clerical, secretarial or administrative functions) who, in connection with his or her regular duties, has participated in the investment activities of the family office, or similar functions or duties for or on behalf of another company, for at least 12 months.[23] The Commission indicated that its limited definition of key employee ensures that employees who participate in family office investments without the protections of the Advisers Act (or family membership) are likely to be in a position or have a level of knowledge or expertise in financial matters sufficient to be able to evaluate the risks and take steps to protect themselves. In limiting its definition to employees who are executive officers, directors, trustees, general partners or

[20] *See id.*, at 63,756.
[21] *See id.*, at 63,755.
[22] *See id.*, at 63,754.
[23] Proposed Rule 202(1)(11)(G)-1(d)(2)(iv).

other persons serving in similar capacities, the Commission ignores the existence of employees of a family office who, by virtue of their financial sophistication, experience and duration of employment at the family office, have the requisite knowledge or expertise in financial matters, but do not meet the restrictive definition of key employee.

Whether a person possesses knowledge and expertise in financial matters sufficient to be able to evaluate the risks and take steps to protect oneself is the same concern that the Commission articulated in adopting the "qualified client" standard under Rule 205-3 under the Advisers Act.[24] If an investor has sufficient knowledge and expertise to invest in a private fund relying on Section 3(c)(1) of the Investment Company Act of 1940, as amended, and/or to open a separate account and be charged a performance fee by an investment adviser, the investor most certainly has sufficient knowledge and expertise to invest in a family office at which he or she has been employed for a number of years. Accordingly, we urge the Commission to broaden the definition of key employee to include employees of the family office who are likely to be in a position or have a level of knowledge and experience in financial matters sufficient to be able to evaluate the risks of investing in the family office and take steps to protect themselves.[25]

We note that including in the definition of key employee only those employees who have been employed by the family office for a number of years would more than adequately prevent a family office from being fairly characterized as a "family-run office" that resembles the business model common among many small investment adviser firms that are registered with the Commission or state regulatory authorities.[26] Instead, our proposed definition would merely allow those long-term employees of the family office whom the Commission believes have knowledge and expertise in financial matters sufficient to able to evaluate the risks and take steps to protect themselves (*e.g.*, by virtue of their qualified client status) to invest with the family office. Additionally, the advantages that the Commission notes in the Release of allowing key employees to invest with a family office—namely, aligning the interests of the employees of the family office with the family office and enabling family offices to attract highly skilled professionals[27]—do not apply merely to the category of employees included in the Proposed Rule's definition of key employee, but apply to a broader range of employees. Accordingly, the Commission should broaden the definition of key employee to include employees of the family office who are likely to be in a position or have a level of knowledge and experience in financial matters sufficient to be able to evaluate the risks and take steps to protect themselves.

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[24] The amendments to Rule 205-3 "allow investment advisers and their clients who are financially sophisticated or have the resources to obtain sophisticated financial advice to negotiate the terms of their performance fee contracts." Exemption To Allow Investment Advisers To Charge Fees Based Upon a Share of Capital Gains Upon or Capital Appreciation of a Client's Account, Advisers Act Release No. IA-1731, [17 CFR 275.205-3 (adopted August 20, 1998)].

[25] *See Adler Management, L.L.C.*, Investment Advisers Act Release Nos. 2500 (Mar. 21, 2006) [71 FR 15498 (Mar. 28, 2006)] (notice) and 2508 (Apr. 14, 2006) (order) (permitting one particular "long-standing loyal family employee" to hold a beneficial interest in a family entity advised by the family office, but not increase his investment).

[26] *See* Release, at 63,755.

[27] *See Id.*, at 63,758.

IV. The Commission Should Allow Former Spouses to Make New Investments in a Family Office

The Commission should allow former spouses to, not only retain their existing investment in a family office, but allow them to make new investments. Under the Proposed Rule, when a spouse becomes a former family member, the individual would not be permitted to receive investment advice from the family office other than with respect to assets advised (directly or indirectly) by the family office immediately prior to the time that the individual became a former family member, except that the former family member would be permitted to receive investment advice from the family office with respect to additional investments that the former family member was contractually obligated to make, and that relate to family-office advised investments existing, in each case prior to the time the person became a former family member.[28] We question the basis of the Commission's conclusion that a former spouse would not be afforded the protections that the Commission assumes accompany family membership.[29] Former spouses often continue to play a significant role in a family, in particular when a family member and a former spouse have children for whose benefit the family office was established. Preventing a former spouse from investing his or her wealth with the family office may negatively impact those children. Finally, prohibiting former family members from making new investments with the family office improperly puts the Commission in the role of arbiter of family relations.[30] Accordingly, we urge the Commission to allow former family members to make new investments with a family office.

V. The Commission Should Broaden the Definition of Family Client to Include Trusts with Beneficiaries Other than Family Clients

Under the Proposed Rule, a family client includes any trust or estate existing for the sole benefit of one or more family clients.[31] We urge the Commission remove the "sole benefit" requirement and instead allow a trust to be considered a family client, even when a non-family member is a beneficiary, to avoid an anomalous and unreasonable result. A family trust would not be a family client under the Proposed Rule if, among beneficiaries who were otherwise exclusively family members, a charity whose donors were not exclusively family members were named as a beneficiary to the trust. To prevent this unreasonable outcome, which incidentally would serve to frustrate a family's charitable purposes,[32] the Commission should

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[28] Proposed Rule 202(1)(11)(G)-1(d)(2)(vi).

[29] Release, at 63,757 ("Our approach is designed to prevent such a separation from resulting in harmful investment or tax consequences, while also recognizing that such persons are no longer members of the family controlling the office, and thus would not be subject to the protections we assume accompany membership in a family.")

[30] *See* Release, at 63,756 ("nothing in our proposed rule would mandate that the family office provide advice to any particular family member; it simply permits such advice.")

[31] Proposed Rule 202(1)(11)(G)-1(d)(2)(iv).

[32] To allow a family-client trust to have as a beneficiary a charity whose donors were not exclusively family members, under the Proposed Rule, a family trust could name as a beneficiary a charity whose donors were exclusively family members whose sole purpose was to make a gift to the charity with non-family member donors. Accordingly, we question the effectiveness of the Proposed Rule's limited inclusion of trusts in the definition of family client, as well as its reasonableness.

include in its definition of family client, trusts established for the primary benefit of family members, and not exclude trusts solely because of a minimal or incidental benefit to a non-family member.

VI. The Commission Should Lengthen the Period of Time a Family Office is Permitted to Provide Investment Advice to Assets that Have Been Involuntarily Transferred

Under the Proposed Rule, a family office is permitted to continue to provide investment advice with respect to assets that have been involuntarily transferred by a family member or key employee for four months following the transfer of assets resulting from the involuntary event.[33] We urge the Commission to lengthen the four-month period, as we question whether such a short period of time accomplishes the Commission's goal articulated in the Release of allowing a family office to orderly transition involuntarily transferred assets to another investment adviser, seeking exemptive relief or otherwise restructuring its activities to comply with the Advisers Act. A four-month period, for example, would be potentially inadequate where involuntarily transferred assets were committed to illiquid investments that they themselves were not readily transferable. Such a scenario may have the unintended effect of a family office restricting its investment program to avoid illiquid investments. Accordingly, the Commission should lengthen the period of time a family office is permitted to provide investment advice with respect to assets that have been involuntarily transferred.

We appreciate the opportunity to comment on the Proposed Rule. If you have any questions regarding this letter, please contact the undersigned at the telephone numbers indicated below.

Very truly yours,

/s/ Patricia A. Poglinco
Patricia A. Poglinco
(212) 574-1247

and

/s/ Robert B. Van Grover
Robert B. Van Grover
(212) 574-1205

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[33] Proposed Rule 202(1)(11)(G)-1(b)(1).