IRISH FUNDS INDUSTRY ASSOCIATION

SUBMITTED ONLINE AT:
www.esma.europa.eu *under "Your input – Consultations"*
European Securities and Markets Authority
103, rue de Grenelle
75007 Paris
France

23 March 2012

Re: Response to ESMA Discussion Paper
"Key concepts of the Alternative Investment Fund Managers Directive and types of AIFM"

Introduction

The Irish Funds Industry Association (IFIA) is the industry association for the international investment fund community in Ireland, representing the custodians, administrators, managers, transfer agents and professional advisory firms involved in the international fund services industry in Ireland.

Ireland is a leading domicile and service location for both UCITS and a full range of non-UCITS alternative investment funds including hedge funds, private equity funds, real estate funds and other alternative investment schemes. Such non-UCITS schemes can be established in a number of legal forms, namely variable capital investment companies, unit trusts, common contractual funds and investment limited partnerships and all require authorisation by and are regulated and supervised by the Central Bank of Ireland (Central Bank). The regulatory category under which most such alternative investment schemes are authorized is the qualifying investor fund (QIF) which we consider to be exceptionally well suited as a model for the AIF under the Alternative Investment Fund Managers Directive (AIFMD).

The QIF structure has been, and is being, used on a widespread basis by asset managers from all over the globe (continental Europe, UK, USA, many Asian countries, Switzerland, South Africa etc.) and, of the current total €240 billion in assets under management within non-UCITS funds domiciled in Ireland, the QIF accounts for almost 80% of this total, at €186 billion (as of January 2012). In less than 3 years since the draft AIFMD was first published in April 2009, QIF assets have grown by more than 100% from €90 billion to €186 billion. Importantly, the QIF is a regulated vehicle and must appoint an investment manager, administrator and transfer agent, and custodian (with certain oversight obligations), each of which must themselves be regulated. In addition: the financial statements of the QIF must be audited annually; the QIF's directors must be pre-approved by the Central Bank and comply with the Central Bank's Fitness and Probity Standards; and the QIF is subject to various other legal and regulatory obligations applicable under general and sector-specific law such as data protection and anti-money laundering legislation.

In addition to the non-UCITS funds domiciled here, Ireland is established as the main centre globally for the servicing of alternative assets, with an estimated 40% of all alternative investment fund assets being serviced here.

Accordingly, all developments in the alternative investment arena are of particular importance to the IFIA which welcomes both the publication of, and the opportunity to comment on, ESMA's Discussion Paper (ESMA/2012/117) setting out ESMA's interpretation of the key concepts of the AIFMD and inviting responses from external stakeholders.

Part A - General Comments on Discussion Paper

Before responding to the specific questions raised by ESMA in the Discussion Paper, we would like to comment on a number of the other aspects of the Discussion Paper and AIFMD which are of material concern to the Irish funds industry. We should be grateful if ESMA could give consideration to these comments.

1. **Delegation of portfolio and risk management functions**

We note the statement in Paragraph 6 of the Discussion Paper that Article 6(5)(d) of the AIFMD should be interpreted as requiring an AIFM to be capable of providing, and take responsibility for, both portfolio management and risk management functions in order to obtain an AIFM authorisation in accordance with the AIFM. We have no issue in principle with this statement; however, we think that the reference to an AIFMD being "capable of providing" the portfolio and risk management functions could be expanded upon to clarify that such provision may be "either directly by itself [i.e., the AIFM] or indirectly by a delegate appointed in accordance with Article 20 of the AIFMD". This is referred to in paragraph 7 of the Discussion Paper but we think it would be helpful to consistently refer to this in any technical standards which are based on paragraph 6 of the Discussion Paper.

We do not however agree with ESMA's view as set out in Paragraph 8 which states that "[s]ubject to the requirements mentioned above [i.e., presumably the requirements referred to in paragraphs 6 and 7 of the Discussion Paper], ESMA considers that an AIFM may delegate the two functions (i.e. portfolio management or risk management) either in whole or in part, *in the understanding that an AIFM may not delegate both functions in whole at the same time."* We disagree with this statement for two reasons: (i) not only is it not supported by the wording of Article 20 of the AIFMD, which clearly contemplates the ability of AIFMs to delegate *both* portfolio management and risk management functions; (ii) it also runs contrary to the well established operating model of many funds whereby they delegate portfolio management and risk management to regulated third parties, but retain ultimate responsibility for such functions and retain sufficient resources to exercise day-to-day oversight over the delegates discharging such functions.

2. **Transitional Provisions**

While not directly related to the Discussion Paper we would, if possible, like to confirm the meaning of Article 61(1) of the AIFMD. This states that "AIFMs performing activities under this Directive before 22 July 2013 shall take all necessary measures to comply with national law stemming from this Directive and shall submit an application for authorisation within 1 year from that date".

We believe that the correct interpretation of Article 61 is that AIFMs will have twelve months (i.e., until 22 July 2014) from July 2013 to both (a) take the necessary measures to comply with the national law implementing the AIFMD; and (b) submit an application for authorisation.

We believe that this interpretation is correct for the following reasons:

(i) it is based on a literal reading of that provision;

(ii) Article 61 is headed “Transitional provisions” which supports the view that the transitional period of 12 months applies to all parts of the Article (i.e., the taking of “necessary measures” to comply with the local law implementing measures for AIFMD and the submission of an application for authorisation;

(iii) Article 6 of the AIFMD provides that “Member States shall ensure that no AIFMs manage AIFs unless they are authorised in accordance with the Directive” suggesting that authorisation, to which the transitional arrangement definitely applies, is the point key in time from which AIFMs should manage AIF in compliance with the AIFMD.

This is obviously without prejudice to the ability of AIFMs to seek authorisation from July 2013 onwards as “early adopters” of the AIFMD and the application of other provisions of the Directive which do not relate to the those AIFM which must submit an application for authorisation within the timeframe prescribed by Article 61(1).

It would also be helpful to clarify the scope of "making additional investments" within the meaning of Article 61(3) of the AIFMD and also the scope of Article 61(4). We foresee the following possible scenarios for closed-ended funds which would require the making of additional investments but possibly are not within the intended scope of the Level 1 text. All scenarios contemplate a closed-ended AIF in existence as at 22 July 2013:

- firstly, the AIF may, after 22 July 2013, need to enter into investments ancillary to the main objective and strategy, e.g., for the purposes of efficient portfolio management or hedging of existing investments;

- secondly, the AIF may have entered into legally binding commitments to acquire, finance or fund investments made prior to 22 July 2013 which were a requirement of the initial purchases and possibly conditional so that the timing of such investments can not be determined by the AIF but are binding on it prior to 22 July 2013; and

- finally, many AIFs of this closed-ended nature will enter into commitment agreements whereby investors will have made a legally binding agreement to contribute additional funds before 22 July 2013 and the call on such commitments and follow on investments (which may or may not have been indentified prior to 22 July 2013) are made after 22 July 2013.

We believe the first and second scenarios should be interpreted as falling outside the scope of Article 61(3) and the third within the meaning of Article 61(4). There is also a question as to whether the investment is deemed made once a legally binding arrangement is entered into or whether the test is based on the point in time at which the actual investment is made; and the former would give greater legal certainty.

Part B - Responses to Questions in Discussion Paper

IV. Definition of AIF

1. **Do you see merit in clarifying further the notion of family office vehicles? If yes, please clarify what you believe the notion of ‘investing the private wealth of investors without raising external capital’ should cover.**

Yes, we do see merit in this clarifying the notion of family office vehicles.

We suggest that consideration be given to the U.S. definition of a family office in the rules adopted under the Investment Advisors Act, 1940 which may be of assistance. The relevant extract is attached at Appendix 1.

2. **Do you see merit in clarifying the terms 'insurance contracts' and 'joint ventures'? If yes, please provide suggestions.**

We do see merit in clarifying the term "joint ventures" as it may be appropriate to include within this definition co-investments and other arrangements in which the AIF is an investor.

3. **Do you see merit in elaborating further on the characteristics of holding companies, based on the definition provided by Article 4(1)(o) of the AIFMD? If yes, please provide suggestions.**

We are concerned that it needs to be very clear that underlying special purpose vehicles (SPVs) and other conduit vehicles used by AIFs are not themselves considered to be AIFs within the scope of the AIFMD.

It is common for Irish AIFs to use wholly-owned SPVs or similar vehicles through which investments are made. In other cases Irish AIFs invest alongside other investors (i.e., co-investment type arrangements) and through other non-wholly owned underlying conduit entities. The reasons for so doing can be a mixture of local legal requirements, tax requirements (including double tax treaty access), normal co-investment arrangements (very prevalent in the private equity industry) and local land holding requirements. It is important that these subsidiary/intermediate/conduit vehicles fall outside the definition of AIF under the AIFMD but can continue to be used for these legitimate purposes.

Such SPVs and conduits are not themselves funds, do not raise capital publicly and are often funded by loan/debt instruments issued to the relevant AIF.

We note in this regard that Article 26(2) of the AIFMD does not apply Section 2 ("Obligations for AIFMs managing AIFs which acquire control of Non-Listed Companies and Issuers") to SPVs "with the purpose of purchasing, holding or administering real estate". We feel that as such vehicles are not only used in connection with real estate but also for other asset classes and for the reasons set out above, it is essential that they be clearly excluded from being AIFs. In that context, it would be useful to make this clear by either including them in the definition of "holding company" or otherwise.

We believe that it should also be clarified that holding companies can be unlisted, as is frequently the case.

4. **Do you see merit in clarifying further the notion of any of the other exclusions and exemptions mentioned above in this section? If yes, please explain which other exclusions and exemptions should be further clarified and provide suggestions.**

Please see our response to question 3 above in relation to subsidiaries/intermediate/conduit vehicles used by AIF.

5. **Do you agree with the orientations set out above on the content of the criteria extracted from the definition of AIF?**

We are in broad agreement with the orientations set out in the Discussion Paper. However, please see our responses to questions 6 to 11 below.

6. **Do you have any alternative/additional suggestions on the content of these criteria?**

Raising Capital Please see response to question 7 below.

Collective Investment We agree that an entity acting for its own account, as opposed to an entity which has as its purpose the generation of a return for its investors, should not be considered to be an AIF. However, we would note in reference to paragraph 28 of the Discussion Paper that collective investment undertakings may generate a return for investors otherwise than "through the sale of its investments" (e.g., through the distribution of income received from the investments held). Furthermore, the reference to non-AIF entities whose purpose it is "to manage the underlying assets with a view to generating value during the life of the undertaking" suggests that this cannot be the purpose of an AIF. Frequently, this description could also be applied to closed-ended collective investment schemes.

We think it would be helpful if ESMA could confirm in any technical standards that "virtual pooling arrangements" do not constitute AIF. Such arrangements are commonly undertaken where a number of funds, managed accounts and/or other investors have a common investment strategy, investment manager and administrator. Virtual pooling is effectively an accounting solution whereby each pool participant (which may be a fund, a managed account or other investor) participates on a pro rata basis in a virtual asset pool. It is important to recognise that this pool does not have separate legal personality and is effectively an accounting construct. At any one time, the depositary of the pool participant is able to identify the share of the assets in the pool which are attributable to its client. The benefits of "virtual pooling" are primarily the cost savings (e.g., lower transaction costs) which result from the ability of the investment manager of the various clients to place block trades on behalf of the various pool participants rather than individual trades for each participant. While certain of the pool participants may themselves constitute AIF within the scope of AIFMD, the virtual pool itself should not be deemed to be an AIF as it does not constitute a "collective investment undertaking" within the meaning of Article 4 of the AIFMD.

Number of Investors

We think that this analysis can be broken down into three categories:-

(i) Where the AIF rules or instruments of incorporation restrict the sale to a single investor

We agree with the premise in paragraph 29 of the Discussion Paper that the reference to a "number of investors" in Article 4 of the AIFMD means that the AIF's rules or instruments of incorporation cannot contain provisions which restrict the sale of units/shares to a single investor.

(ii) Where the AIF rules or instruments of incorporation do not current restrict the sale to a single investor

We think that the concept in paragraph 29 should be expanded upon to state that the same applies where law or regulation or the prospectus, private placement memorandum, offering document or other document which specifies the terms on which an investor invests in a scheme states that the scheme may not be sold to more than one investor. In other words, if an entity is restricted by another legally binding document or legislative/regulatory provision other than the "fund rules or instruments of incorporation", it should similarly not be considered an AIF.

We also believe that some flexibility should be provided for where a fund is in fact invested in by a single investor but does not currently contain the prescribed wording in its rules, instructions of incorporation or offering document. This flexibility could involve a grandfathering period during which such funds are afforded reasonable time to implement the changes (some of which under local law may require the shareholder's approval) to the documentation.

(iii) Where the AIF rules or instruments of incorporation restrict the sale to a single investor but there is uncertainty as to whether an investor represents a number of underlying beneficial owners

We also agree that, per paragraph 29 of the Discussion Paper, where a single investor represents a number of underlying beneficial owners (e.g., in the case of nominee arrangements), the fund should fall within the definition of AIF for the purposes of the AIFMD.

While this should also be the case for many master/feeder structures, we would note that investors in the feeder fund or fund of funds will typically not have any beneficial interest in the units of the underlying vehicle. Also, the fund of funds would itself most likely be considered to be an AIF and we would query whether it is always appropriate to designate the underlying vehicle as an AIF when the fund of funds itself will be within the scope of the AIFMD. We can think of examples where a fund of funds invests on an exclusive basis in an underlying vehicle (i.e., the fund of funds is the sole investor in the vehicle) and where that vehicle does not fulfil many of the indicia in the AIFMD to constitute an AIF. Consideration should also be given to situations in which the relevant feeder fund or fund of funds is itself a "single investor" investment fund – it follows that any underlying fund should not constitute an AIF if the feeder fund or fund of funds itself is not an AIF.

In addition, there are arrangements whereby investors in a vehicle may invest for their own account (i.e., have both the legal and beneficial interest) in the investment in the vehicle and who, in turn, may issue financial instruments which provide a return linked to the performance of the vehicle. This is often the case where insurance companies or pension funds act as investors. This may also be done via securitisation special purpose vehicles or through other structures which are not AIF and may be the subject of EU regulation under the Prospectus Directive (Directive 2003/71/EC) or MiFID regimes (Directive 2004/39/EC). In such cases, the purchasers of the financial instruments are not investing in the vehicle and so it should not be considered to be an AIF.

Owing to the wide array of investment vehicles (both collective investment undertakings and otherwise) and wide array of investor types (and differing legal natures thereof) that are in existence and the different relationships which apply between the vehicles and investors depending on the law of the jurisdiction(s) in question, we suggest that any technical standards should not seek to exhaustively define what does and does not constitute an AIF. The definition of an AIF in Article 4 of the AIFMD should always be the first point of reference when considering whether a vehicle is or is not an AIF. Ultimately, it should be a matter for the board of directors of the vehicle to determine whether an investor represents a number of underlying beneficial owners based upon:-

- information and representations received from the investor purchasing the interest in the vehicle. There are significant practical challenges in identifying whether or not an investor is investing for its own account or on behalf of a number of beneficial owners. Investment vehicles and relevant service providers (e.g., transfer agents) often rely on representations and warranties in subscription documents as to whether or not the investor is investing on its own account or on behalf of beneficial owners; and

- the legal nature of the relationship between that investor and any other persons that may be linked to such investor.

In addition, where it is not clear that a vehicle is or is not an AIF, we suggest that the facility be given to such vehicles to voluntarily choose to be designated as AIF. Naturally the vehicle should be under an obligation to notify this designation to any entity which would be considered under the AIFMD to be its AIFM.

Finally, where a single nominee invests in a vehicle on behalf of a single beneficial owner, we think it would be helpful to clarify that this does not result in the vehicle being deemed to be an AIF.

Defined Investment Policy We would agree generally with the indicative criteria set out in paragraph 31 of the Discussion Paper in determining whether or not an entity has a "defined investment policy". However, we would make a couple of observations. It should be underlined that these criteria are indicative only. In addition, the Discussion Paper states that "any change to the investment policy is disclosed to the investors and in many cases investors provide their consent to such change". We suggest that this should refer to "material changes" to investment policy, as minor changes may be made to the investment policy which do not prejudice investors and for which it is not appropriate or practicable to notify investors, at least not on an ex ante basis.

Ownership of Assets See response to question 9 below.

Control of Underlying Assets See response to question 10 below.

7. **Do you agree with the orientations set out above on the notion of raising capital? If not, please provide explanations and an alternative solution.**

We agree that investment undertaken for non-commercial purposes which are not intended to deliver an investment return or profit should not be considered to be AIF falling within the scope of AIFMD.

We would caution against stating that notion of raising capital must involve "some kind of business communication between the entity seeking capital or a person acting on its behalf with prospective investors, resulting in the transfer of cash or other assets to the AIF" as rigid language of this nature may have the unintended consequence of capturing transactions which are not capital raisings. We would also have a slight disagreement with the sentence in paragraph 27 of the Discussion Paper which says that "[i]t would not however be sufficient to say that the absence of capital raising is conclusive evidence that an entity is not an AIF". While we agree that in the example given (whereby an entity which raised capital is liquidated and its assets are transferred to a newly incorporated entity) that the newly incorporated entity could still be considered to be an AIF, notwithstanding that it didn't raise the capital itself directly. Perhaps this could be addressed by inserting the word "direct" immediately before "capital raising" in the sentence referred to.

We also suggest that subsidiaries of AIFs which are used to acquire or hold some or all of the AIF's portfolio of investments should be expressly excluded from the definition of "AIF" under the AIFMD, as these entities simply hold investments on behalf of the AIF and do not raise capital from investors. "Subsidiaries" for these purposes should also be deemed to include special purpose vehicles which issue loans or financial instruments such as profit participating notes to the AIF. See our response to question 3 above.

8. **Do you consider that any co-investment of the manager should be taken into account when determining whether or not an entity raises capital from a number of investors?**

In determining whether or not an entity raises capital from a number of investors co-investment by the AIFM, or an affiliated entity, should not be taken into account. If such an investment was to be taken into account then, for example, managed accounts and other similar arrangements that should be outside the scope of the AIFMD would be brought within its scope where there is any co-investment by the manager. In addition, this may have the unintended effect of bring joint ventures within the scope of the AIFMD where this is clearly not intended by the AIFMD. We believe that this is also consistent with the thinking behind

Recital 16 of the AIFMD which states that the AIFMD "should not apply to AIFMs in so far as they manage AIFs whose only investors are the AIFMs themselves or their parent undertakings…".

9. **Do you agree with the analysis on the ownership of the underlying assets in an AIF? Do other ownership structures exist in your jurisdiction?**

We agree in broad terms with this analysis. However, it is not clear to us what paragraph 33 of the Discussion Paper is trying to achieve as the ownership arrangements for collective investment schemes may vary greatly from jurisdiction to jurisdiction and may depend on the legal structure used and we would not have thought that technical standards based on paragraph 33 would assist in identifying whether an arrangement was an AIF.

We would note that in Ireland, for example, the common contractual fund (CCF) is a structure whereby unitholders have beneficial "co-ownership" rights in the property and assets of the CCF as represented by the units in the CCF.

In certain instances, investors will want to receive reports (for tax or accounting purposes) as if that investor owned assets in the AIF. However, the legal analysis of ownership (rather than any accounting treatment) should be the only relevant factor for the purpose of the analysis under AIFMD.

10. **Do you agree with the analysis on the absence of any investor discretion or control of the underlying assets in an AIF?**

We agree generally with the proposition in paragraph 34 of the Discussion Paper. However, we think it might be helpful to elaborate by stating that in the case of many funds, investor committees or similar arrangements are put in place whereby investors or their representatives can provide feedback and other views on the investment strategy implemented by the investment manager, the investment performance of the AIF and potential conflicts of interest. Such committees do not constitute day-to-day discretion or control over the assets of the AIF.

11. **Do you agree with the proposed definition of open-ended funds in paragraph 41? In particular, do you agree that funds offering the ability to repurchase or redeem their units at less than an annual frequency should be considered closed-ended?**

We agree that funds offering the ability to repurchase or redeem their units/shares at less than an annual frequency should be considered closed-ended for the purposes of the AIFMD provided however that this is simply for the limited purposes of the application of the provisions of the AIFMD which apply to closed-ended funds. This definition should capture "limited liquidity funds" which are a type of fund in Ireland which may have extended initial lock-up periods (of more than one year) and infrequent redemption facilities. We think it would be helpful to clarify that, while such limited liquidity funds may allow for more frequent redemption facilities during their lifetime (i.e., certain periods during which redemptions may be place on a number of dealing days more frequently than annually) this should not affect the status of the limited liquidity fund as a "closed-ended fund" under the AIFMD provided that it is prominently disclosed in the prospectus or other offering document that it is a closed-ended fund for the purposes of the AIFMD and offers limited redemption facilities. We must emphasise though that the species of limited liquidity fund used in Ireland is not a closed-ended fund in any other sense (whether under the EU Prospectus Directive, Transparency Directive or Takeovers Directive or otherwise).

12. **Do you see merit in clarifying further the other concepts mentioned in paragraph 37 above? If so, please provide suggestions.**

Yes, the meaning of "significant size" and "employs substantial leverage" should be clarified. Significant size could be determined by reference to the net asset value of the AIF under management.

VI. **Treatment of UCITS management companies**

13. **Do you agree with the above analysis? If not, please provide explanations.**

Yes, we agree with this analysis.

VII. **Treatment of MiFID firms and Credit Institutions**

14. **Do you agree with the above analysis? If not, please provide explanations.**

We disagree with the analysis in Paragraph 54 that a firm which is authorised under MiFID cannot be the appointed AIFM for an AIF nor obtain authorisation under the AIFMD. Nothing in the text of the AIFMD prohibits an AIFM from holding at the same time an authorisation under MiFID. Article 6(4) of the AIFMD allows the AIFM to perform certain investment services which fall under MiFID. As long as the AIFM restricts itself to the services as stipulated in Article 6(4) it should be permitted to hold a MiFID authorisation.

Appendix 1
Definition of "family office" in U.S. Investment Advisors Act 1940

PART 275—RULES AND REGULATIONS, INVESTMENT ADVISERS ACT OF 1940

§ 275.202(a)(11)(G)-1 Family offices.

(a) *Exclusion.* A family office, as defined in this section, shall not be considered to be an investment adviser for purpose of the Act.

(b) *Family office.* A family office is a company (including its directors, partners, members, managers, trustees, and employees acting within the scope of their position or employment) that:

(1) Has no clients other than family clients; provided that if a person that is not a family client becomes a client of the family office as a result of the death of a family member or key employee or other involuntary transfer from a family member or key employee, that person shall be deemed to be a family client for purposes of this section for one year following the completion of the transfer of legal title to the assets resulting from the involuntary event;

(2) Is wholly owned by family clients and is exclusively controlled (directly or indirectly) by one or more family members and/or family entities; and

(3) Does not hold itself out to the public as an investment adviser.

(c) *Grandfathering.* A family office as defined in paragraph (a) of this section shall not exclude any person, who was not registered or required to be registered under the Act on January 1, 2010, solely because such person provides investment advice to, and was engaged before January 1, 2010 in providing investment advice to:

(1) Natural persons who, at the time of their applicable investment, are officers, directors, or employees of the family office who have invested with the family office before January 1, 2010 and are accredited investors, as defined in Regulation D under the Securities Act of 1933;

(2) Any company owned exclusively and controlled by one or more family members; or

(3) Any investment adviser registered under the Act that provides investment advice to the family office and who identifies investment opportunities to the family office, and invests in such transactions on substantially the same terms as the family office invests, but does not invest in other funds advised by the family office, and whose assets as to which the family office directly or indirectly provides investment advice represents, in the aggregate, not more than 5 percent of the value of the total assets as to which the family office provides investment advice; provided that a family office that would not be a family office but for this paragraph (c) shall be deemed to be an investment adviser for purposes of paragraphs (1), (2) and (4) of section 206 of the Act.

(d) *Definitions.* For *purposes* of this section:

(1) *Affiliated family office* means a family office wholly owned by family clients of another family office and that is controlled (directly or indirectly) by one or more family members of such other family office and/or family entities affiliated with such other family office and has no clients other than family clients of such other family office.

(2) *Control* means the power to exercise a controlling influence over the management or policies of a company, unless such power is solely the result of being an officer of such company.

(3) *Executive officer* means the president, any vice president in charge of a principal business unit, division or function (such as administration or finance), any other officer who performs a policy-making function, or any other person who performs similar policy-making functions, for the family office.

(4) *Family client* means:

(i) Any family member;

(ii) Any former family member;

(iii) Any key employee;

(iv) Any former key employee, provided that upon the end of such individual's employment by the family office, the former key employee shall not receive investment advice from the family office (or invest additional assets with a family office-advised trust, foundation or entity) other than with respect to assets advised (directly or indirectly) by the family office immediately prior to the end of such individual's employment, except that a former key employee shall be permitted to receive investment advice from the family office with respect to additional investments that the former key employee was contractually obligated to make, and that relate to a family-office advised investment existing, in each case prior to the time the person became a former key employee.

(v) Any non-profit organization, charitable foundation, charitable trust (including charitable lead trusts and charitable remainder trusts whose only current beneficiaries are other family clients and charitable or non-profit organizations), or other charitable organization, in each case for which all the funding such foundation, trust or organization holds came exclusively from one or more other family clients;

(vi) Any estate of a family member, former family member, key employee, or, subject to the condition contained in paragraph (d)(4)(iv) of this section, former key employee;

(vii) Any irrevocable trust in which one or more other family clients are the only current beneficiaries;

(viii) Any irrevocable trust funded exclusively by one or more other family clients in which other family clients and non-profit organizations, charitable foundations, charitable trusts, or other charitable organizations are the only current beneficiaries;

(ix) Any revocable trust of which one or more other family clients are the sole grantor;

(x) 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 who, at the time of contribution, holds a joint, community property, or other similar shared ownership interest with the key employee; or

(xi) Any company wholly owned (directly or indirectly) exclusively by, and operated for the sole benefit of, one or more other family clients; provided that if any such entity is a pooled investment vehicle, it is excepted from the definition of “investment company” under the Investment Company Act of 1940.

(5) *Family entity* means any of the trusts, estates, companies or other entities set forth in paragraphs (d)(4)(v), (vi), (vii), (viii), (ix), or (xi) of this section, but excluding key employees and their trusts from the definition of family client solely for purposes of this definition.

(6) *Family member* means all lineal descendants (including by adoption, stepchildren, foster children, and individuals that were a minor when another family member became a legal guardian of that individual) of a common ancestor (who may be living or deceased), and such lineal descendants' spouses or spousal equivalents; provided that the common ancestor is no more than 10 generations removed from the youngest generation of family members.

(7) *Former family member* means a spouse, spousal equivalent, or stepchild that was a family member but is no longer a family member due to a divorce or other similar event.

(8) *Key employee* means any natural person (including any key employee's spouse or spouse equivalent who holds a joint, community property, or other similar shared ownership interest with that key employee) who is an executive officer, director, trustee, general partner, or person serving in a similar capacity of the family office or its affiliated family office or any employee of the family office or its affiliated family office (other than an employee performing solely clerical, secretarial, or administrative functions with regard to the family office) who, in connection with his or her regular functions or duties, participates in the investment activities of the family office or affiliated family office, provided that such employee has been performing such functions and duties for or on behalf of the family office or affiliated family office, or substantially similar functions or duties for or on behalf of another company, for at least 12 months.

(9) *Spousal equivalent* means a cohabitant occupying a relationship generally equivalent to that of a spouse.

(e) *Transition.* (1) Any company existing on July 21, 2011 that would qualify as a family office under this section but for it having as a client one or more non-profit organizations, charitable foundations, charitable trusts, or other charitable organizations that have received funding from one or more individuals or companies that are not family clients shall be deemed to be a family office under this section until December 31, 2013, provided that such non-profit or charitable organization(s) do not accept any additional funding from any non-family client after August 31, 2011 (other than funding received prior to December 31, 2013 and provided in fulfillment of any pledge made prior to August 31, 2011).

(2) Any company engaged in the business of providing investment advice, directly or indirectly, primarily to members of a single family on July 21, 2011, and that is not registered under the Act in reliance on section 203(b)(3) of this title on July 20, 2011, is exempt from registration as an investment adviser under this title until March 30, 2012, provided that the company:

(i) During the course of the preceding twelve months, has had fewer than fifteen clients; and

(ii) Neither holds itself out generally to the public as an investment adviser nor acts as an investment adviser to any investment company registered under the Investment Company Act of 1940 (15 U.S.C. 80a), or a company which has elected to be a business development company pursuant to section 54 of that Act (15 U.S.C. 80a–54) and has not withdrawn its election.

[76 FR 37994, June 29, 2011]