THE ERISA INDUSTRY COMMITTEE
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Submitted Electronically

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Office of Exemption Determinations
Employee Benefits Security Administration
U.S. Department of Labor 200
Constitution Ave., NW
Washington, DC 20210

Re: Proposed Amendment to Prohibited Transaction Class Exemption 84-14 (the QPAM Exemption); Application No. D-12022

To Whom It May Concern:

On behalf of The ERISA Industry Committee (ERIC), thank you for the opportunity to comment on the Department of Labor's (DOL or Department) Proposed Amendment to Prohibited Transaction Class Exemption (PTE) 84-14 (Proposal).[1]

ERIC is a national nonprofit organization exclusively representing the largest employers in the United States in their capacity as sponsors of employee benefit plans for their nationwide workforces. With member companies that are leaders in every economic sector, ERIC is the voice of large employer plan sponsors on federal, state, and local public policies impacting their ability to sponsor benefit plans and to lawfully operate under the protection afforded by the Employee Retirement Incomes Security Act (ERISA) from a patchwork of different and conflicting state and local laws, in addition to federal law.

The proposed amendment would revise PTE 84-14, known as the "Qualified Professional Asset Manager" (QPAM) exemption. This exemption—which has been in place for nearly 40 years with only slight modifications—provides broad relief from the prohibited transaction rules in section 406(a) of ERISA.[2] Pursuant to the exemption, an investment fund managed by a QPAM that holds assets for an ERISA-covered plan or Individual Retirement Account and that meets a number of conditions can engage in routine transactions with parties in interest that would otherwise be prohibited. Because nearly anyone can be a party in interest, plan sponsors, fiduciaries, and service providers rely on this exemption to efficiently operate their plans and ensure that participants are not deprived of the opportunity for beneficial transactions.

[1] 87 Fed. Reg. 45204 (July 27, 2022).
[2] References to ERISA's prohibited transaction provisions include parallel provisions of section 4975 of the Internal Revenue Code. The general exemption does not extend to transactions prohibited by ERISA section 406(a)(2) or 406(b) and includes other exclusions for transactions with parties in interest that present increased risk of conflicts.

In recent years, there has been controversy surrounding the eligibility of QPAMs to maintain their exemptive relief if convicted of foreign crimes.[3] The Department's release of this proposal appears to emphasize this relatively narrow issue, even though the instances of such criminal activities are quite rare.[4]

However, the proposal has much broader implications for plans that use the QPAM exemption and will disrupt ERISA plans and their asset management contracts. **ERIC writes to emphasize that the timeframe and regulatory cost analysis for the Proposal's required changes to investment management contracts are unrealistic; the Proposal's "winding-down period" will not actually provide meaningful relief; and the proposal's amended "sole responsibility" limitation for relief is overbroad.**

<u>The Timeframe and Cost Analysis for the Proposal's Required Amendments to Investment Management Agreements Are Unrealistic</u>

The Proposal would require investment management agreements to incorporate a variety of terms, which specify that when a QPAM (or affiliate or five percent or more owner) engages in criminal conduct that results in a conviction or "ineligibility notice":

- The QPAM will not restrict the ability of a client plan to terminate or withdraw from the agreement;

- The QPAM will not impose fees, penalties, or charges in connection with terminating or withdrawing from the Investment Fund (with exceptions for certain reasonable, generally-applicable fees that meet specified conditions);

- The QPAM "agrees to indemnify, hold harmless, and promptly restore actual losses to the client Plans for any damages" arising out of the conduct that resulted in the conviction or ineligibility notice, including actual losses from unwinding transactions and excise taxes resulting from the loss of the QPAM exemption; and,

- The QPAM will not employ or knowingly engage a person convicted or the subject of an ineligibility notice.[5]

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[3] The Department says that it addressed this foreign crime issue "to eliminate any ambiguity" about whether certain foreign crimes are disqualifying. Proposal at 45208. *See, e.g.* Penn, Ben and Austin Ramsey, "Trump Relief for Foreign-Convicted Banks Quashed by Biden DOL" *Bloomberg Law* (Mar. 25, 2021);
but see Letter from Kate O'Scannlain, Solicitor, U.S. Dep't of Labor, to Lisa Bleier, Managing Dir. and Assoc. Gen. Counsel, Sec. Indus. and Fin. Mkts. Ass'n (Nov. 3, 2020).
[4] "US DEPARTMENT OF LABOR PROPOSES AMENDMENT TO QUALIFIED PROFESSIONAL ASSET MANAGER EXEMPTION TO PROTECT BENEFITS PLANS, PARTICIPANTS, BENEFICIARIES," Press Release, U.S. Dep't of Labor (July 26, 2022).
[5] Proposal, *supra* note 1, at 45227.

Each of these terms is to apply for "at least a period of 10 years." According to the Department's "Regulatory Impact Analysis," the only cost associated with this will be "*updating existing management agreements*."[6] In the Department's view, each highly sophisticated financial institution that relies on the QPAM will simply "send the update" to each client plan – a "single standard form with identical language." The Department believes this will take "*one hour of in-house legal professional time to update and supplement their existent standard management agreements, and two minutes of clerical time to prepare and mail a one-page addition to the agreement to each client plan*." The Department believes the total estimated cost to the entire industry will be $135,540.

This analysis is tremendously unrealistic for a number of reasons. Merely drafting revisions to management agreements by each QPAM is likely to require far more than one hour of in-house legal time. Indeed, the Department seems to presume that all of a QPAM's clients will have essentially the same template management agreement; however, many plans have their own more customized contractual documents that likely require individualized review. The Department also completely failed to consider that substantively amending a contract will also require each plan to review the proposed changes, evaluate the implications, and then likely enter into a negotiation with the QPAM for changes. Once the terms of an agreement are under discussion, the possibility for much broader negotiations exist, including pricing adjustments associated with implementing the substantive requirements of the proposal. The transaction costs of these negotiations, potential changes to pricing structures, and potential market effects (including firms potentially exiting the market given the proposed new requirements) were not analyzed by the Department.

Furthermore, the timeframe for these negotiations is highly expedited. The Proposal is to be effective within 60 days of publication of the final rule in the *Federal Register*.[7] There is no special transition period for these "updates" to existing management agreements, and so negotiations must be completed within 60 days of the final rule or reliance on the QPAM exemption will be lost. Plans may have many agreements with different QPAMs and pooled investment funds managed by QPAMs, and this will create an enormous rush for plans and QPAMs alike. For example, Plans will have to engage in a review of all investment agreements to identify which ones have terms related to the QPAM exemption. This project alone will be a substantial undertaking. **If the Department insists on requiring written contractual terms, it must delay the effective date of this requirement or provide a significant transition period for existing management agreements to be updated**.

[6] *Id.* at 45218.
[7] *Id.* at 45204.

The Proposal's "Winding-Down Period" Will Not Actually Provide Meaningful Relief

Purportedly in order to mitigate the disruption to plans of QPAM ineligibility, the Department included a one-year "winding-down period" for the plan's relationship with the QPAM. The winding-down period is subject to conditions, most notably that the relief during the winding-down period is only for transactions entered into before the QPAM's ineligibility date.[8]

The Department emphasizes that the QPAM would be prohibited from engaging in new transactions in reliance on the QPAM transaction, even for existing client plans. Nevertheless, the Department asserts that this period would provide plans with "*time to decide whether to hire an alternative discretionary asset manager that is eligible to operate as a QPAM or continue their relationship*" with the now-ineligible firm.[9]

The wind-down period does not actually provide meaningful relief. If a plan is unable to use the now-ineligible QPAM for new transactions during the winding-down period, then the plan is still in the position of needing to find a new asset manager immediately following the ineligibility date of the QPAM, or *immediately* make the determination to retain the now-ineligible firm. Otherwise, a plan will be left unable to react to market conditions or effectively transact on behalf of participants. There is no "time to decide" actually accorded. **Therefore, plans need additional flexibility to manage the wind-down process with firms that have become ineligible, including the ability for the now-ineligible QPAM to engage in new transactions with existing clients during the winding-down period.**

Additionally, the winding-down period is not tolled while the now-ineligible QPAM seeks an individual exemption through the Department. Either the plan will be forced to switch asset managers or pursue different strategies with the same manager, perhaps in reliance on a different exemption, after the QPAM initially becomes ineligible. If the firm becomes eligible through the individual exemption process, then there could be further disruption.

There are also a number of unique practical challenges that defined contribution (DC) plans would face where an ineligible QPAM manages one or more of the plan's designated investment alternatives. If the ineligible QPAM is unable to engage in new transactions during the winding-down period, the designated investment alternative will likely be unable to achieve its investment objectives, as communicated to participants. DC plan fiduciaries and their participants would almost certainly be at increased risk to retain such a fund, even for a short time period. However, a designated investment alternative cannot be quickly removed or replaced. For example, the plan fiduciary would need time to engage in a prudent process to select a replacement fund following receipt of the QPAM's ineligibility notice. In addition, we understand that plan recordkeepers typically require at least 90 to 120 days of lead time to implement a change to a designated investment alternative.

[8] *Id.* at 45211.
[9] *Id.* at 45211.

Further complicating matters, the Department's participant disclosure regulation also requires any change to a DC plan's designated investment alternatives to be disclosed to participants at least 30 days (but not more than 90 days) in advance.[10] The plan administrator would also need to furnish a blackout notice at least 30 days (but not more than 60 days) in advance of a blackout period.[11]

It appears that the Department has not given consideration to these risks and practical limitations in proposing a winding-down period with no ability to conduct new transactions for a time period sufficient for plan fiduciaries to take prudent action that can be effectively communicated to participants and implemented by their recordkeepers.

Furthermore, there are questions left unanswered by the Proposal, such as whether the harms that the QPAM is required to indemnify include the opportunity costs of plan transactions that the QPAM would have engaged in during the one-year period after ineligibility, but for the prohibition on engaging in new transactions. Another question is whether the QPAM would have the ability to renew certain types of arrangements, such as leases, during the one-year period or if that would constitute a new transaction. These questions should be resolved by permitting the ineligible QPAM to engage in new transactions during the winding-down period.

Finally, the Department also indicates that a QPAM's failure to satisfy the conditions of the winding-down period "*would affect the availability of relief for all transactions covered by this exemption . . . includ[ing] relief for past transactions and any transaction continued during the one-year winding-down period*."[12] Retroactive loss of exemptive relief for prior transactions—particularly those entered into before a QPAM's ineligibility date—is unnecessarily disruptive. **To the extent a QPAM fails to comply with the conditions of the winding-down period, any loss of exemptive relief should be prospective only**.

<u>The Proposal's Amended "Sole Responsibility" Limitation of Relief Is Overbroad and Will Prohibit Beneficial Transactions</u>

The Department proposes to add language to the limitation of relief that is ambiguous at best; if read broadly, it could prohibit or deter a wide range of beneficial transactions and routine exchanges of information.

[10] 29 C.F.R § 2550.404a-5(c)(1)(ii). While the regulation provides an exception if the inability to provide advance notice is due to events that were unforeseeable or circumstances beyond the control of the plan administrator—in which case notice of the change must be furnished as soon as reasonably practicable—but it is unclear whether this exception would apply to a situation involving QPAM ineligibility. Failure to comply with this regulation could be deemed a fiduciary breach.
[11] 29 C.F.R. § 2520.101-3(b)(2). DOL may assess civil penalties of up to $152 per participant, per day for failure to comply with the blackout notice requirements. ERISA § 502(c)(7); 87 Fed. Reg. 2328, 2338 (Jan. 14, 2022) (stating general rule).
[12] Proposal, *supra* note 1, at 45211.

The Department has made clear that a QPAM must have the sole decision-making authority with respect to the relevant investments and transactions.[13] To that end, the current exemption is contingent on the QPAM making a decision "*to enter into the transaction, provided that the transaction is not part of an agreement, arrangement or understanding designed to benefit a party in interest.*" [14] However, to "eliminate any possible ambiguity," the Department proposes to change this language to add the sentence: "*No relief is provided under this exemption for any transaction that has been planned, negotiated, or initiated by a Party in Interest, in whole or in part, and presented to a QPAM for approval because the QPAM would not have sole responsibility with respect to the transaction as required by this [section].*"[15]

The phrase "planned, negotiated, or initiated" is not defined in the proposed text, nor are the words defined in the preamble. Instead, DOL states that the amendments are *"intended to make clear that a QPAM must not permit other parties in interest to make decisions regarding Plan investments under the QPAM's control*."[16] According to the Department, a "*party in interest should not be involved in any aspect of a transaction, aside from certain ministerial duties and oversight associated with plan transactions, such as providing general investment guidelines to the QPAM*."[17] And a QPAM is "*not to act as a mere independent approver of transactions. Rather the QPAM must have and exercise discretion over the commitments and investments of Plan assets and the related negotiations with respect to a fund that is established primarily for investment purposes*" in order to receive relief.[18]

Because the phrase "planned, negotiated, or initiated" is not explained, ERIC is concerned that a broad interpretation could alter how plan fiduciaries and QPAMs discuss and execute many routine transactions on behalf of the plan.

The most significant challenge is the ambiguity with the word "initiate." For example, if a party in interest proposes a transaction for the QPAM's consideration, is that "initiating" a transaction "in whole or in part"? If so, that could have drastic effects for a number of transactions regularly used by benefit plans. Similarly, if a plan sponsor makes a suggestion or provides information regarding a transaction, it is unclear whether that could be initiating a transaction "in whole or in part" for purposes of the Proposal.

The language in the preamble seems to suggest that the Department does not intend to substantively change the standards for relief, and instead merely clarify that the QPAM must have ultimate decision-making authority. **If that is true, the proposal's operative language should not use ambiguous and undefined terms like "initiate."**

[13] *Id.* at 45213.
[14] Prohibited Transaction Exemption 84-14, 49 Fed. Reg. 9494, 9504 (Mar. 13, 1984).
[15] Proposal, *supra* note 1, at 45227.
[16] *Id.* at 45213.
[17] *Id.*
[18] *Id.*

The Department's discussion of this aspect of the proposal also suggests a particular concern about transactions with parties in interest (like employers) that present an increased risk of potential conflicts. However, the QPAM exemption already incorporates protections against the types of transactions with parties in interest that are most likely to raise such concerns:

- The general exemption only provides relief for transactions prohibited by ERISA section 406(a)(1)(A) through (D) and doesn't extend to transactions prohibited by ERISA section 406(a)(2) or 406(b);

- The exemption excludes (with a limited exception for certain limited investments in pooled investment funds) transactions with parties and their affiliates that have authority to appoint or terminate the QPAM as manager of the plan assets involved in the transaction or negotiate terms of the plan's management agreement with the QPAM; [19] and,

- The exemption can't be used for transactions with the QPAM or parties related to the QPAM.

These existing limitations, combined with ERISA's stringent fiduciary standards, already substantially mitigate the concerns that the Department cites in this portion of the proposal.

Conclusion

ERIC appreciates the opportunity to provide substantive comments to the Department on the major concerns that large plan sponsors have articulated with the Proposal. Specifically, the required changes to the investment management agreements will be burdensome to undertake in the manner and timeframe the Department has proposed. Additionally, the Proposal's wind-down period will not accord meaningful relief and the amended "sole responsibility" limitation is overbroad and must be revised.

Sincerely,

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