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Office of Exemption Determinations
Employee Benefits Security Administration

U.S. Department of Labor
200 Constitution Avenue, NW
Washington, DC 20210

Re: EBSA-2022-0008; Proposed Amendment to Prohibited Transaction Class Exemption 84-14 (the QPAM Exemption)

Dear Mr. Khawar,

Seward & Kissel LLP is a leading U.S. law firm with offices in New York City and Washington, D.C. The firm's practice primary focuses on financial services, corporate finance and capital markets. We represent a substantial number of professional asset managers. These clients include many entities that meet the requirements of Part VI(a) of Prohibited Transaction Class Exemption 84-14 (the "QPAM Exemption").

Many of the provisions in this proposed amendment to QPAM Exemption are neither necessary nor in the interest of plans and their participants and beneficiaries. The QPAM Exemption works; it provides investment managers and the named fiduciaries who appoint them, as well as parties that transact with plans, an efficient way to assure that customary, arm's length transactions do not result in non-exempt prohibited transactions. As discussed below, the proposed amendment will burden thousands of managers, who have not engaged in any illegal activity, by requiring them to amend their investment management agreements, disclose sensitive information and assume additional liabilities if they choose to continue to rely on the QPAM Exemption. If adopted, the proposed amendment will certainly result in banks, insurance companies and investment managers ceasing to rely on the QPAM Exemption, which will limit the types of transactions and investment managers available to plans. Restricting the investment strategies available to plans and reducing the number of investment managers available to them, in order to address an infrequent problem, is not in the best interest of plans and their participants.

I. EBSA's formula for determining the number of investment managers that rely on the QPAM Exemption is seriously flawed.

EBSA estimated there are 616 potential QPAMs by approximating the total number of providers who in 2019 simultaneously provided ''Investment management'' and ''Named fiduciary''

services to at least one plan, as reported in Schedule C of the 2019 Form 5500, and then reduced that number by those who reported the NAICS codes corresponding to Finance and Insurance Institutions.

This approach ignores the fact that the vast majority of investment managers who rely on the QPAM Exemption do not act as "Named fiduciary" to the plan. Instead, EBSA's formula is more likely to only have counted those investment managers who are appointing other investment managers on behalf of the plan. Furthermore, the NAICS codes do not necessarily appear to be relevant to the determination of QPAM status and may fail to capture all entities who operate as QPAMs.

In our experience, more than 90% of investment managers investing plan assets currently rely on the QPAM Exemption. Accordingly, it is our position that EBSA should recalculate the number of investment managers relying on the QPAM Exemption by multiplying the total number of managers who are coded "#28" (i.e., "Investment management") on Schedule C of the 2019 Form 5500 by 0.90, in order to obtain a more accurate and realistic estimate of the number of plans and investment managers effected by this proposal.

II. The proposed recordkeeping requirement will reduce the number of investment strategies and managers available to plans without providing meaningful benefits to plans or plan participants.

EBSA noted in the preamble that the QPAM Exemption currently lacks a recordkeeping requirement which the Department generally includes in its administrative exemptions. The amendment would add a recordkeeping requirement to ensure QPAMs will be able to demonstrate, and the Department will be able to verify, compliance with the exemption conditions. In particular, proposed Section VI(t) would require that a QPAM maintains the records necessary to enable the Department of Labor, any federal or state regulator, as well as any fiduciary, sponsor or participant of any plan for whom the QPAM provides investment management services to determine that the conditions of the exemption are satisfied. However, fiduciaries, sponsors and participants are not authorized to examine records with privileged trade secrets or privileged commercial or financial information of the QPAM, or information identifying other individuals.

This proposed requirement is unnecessary. The reason that the current exemption contains no recordkeeping requirement is that all of the information required to verify compliance with the exemption's conditions is either publicly available or privileged financial information. In order to rely on the QPAM Exemption the investment manager must: (i) be a bank, an insurance company or a registered investment adviser; (ii) have specified assets under management as of its most recently completed fiscal year; (iii) have shareholder equity as of their most recently completed balance sheet of a specified amount; (iv) not have a plan (or group of related plans) that represents 20% or more of the investment manager total AUM; and (v) have not (nor have any affiliate or 5% owner) been disqualified under Section I(g).

As to the first requirement, this is easily found in public documents; for example, the SEC's website provides a list of all registered investment advisors. Similarly, the second requirement is

also publicly available; for example, the form ADV, required to be filed annually by registered investment advisors, is available on the SEC's website and discloses the investment advisor's discretionary assets under management. The third requirement is problematic, it would require that a bank, insurance company or investment manager turn over its balance sheet to any fiduciary, plan sponsor or participant whose assets they are managing, or argue that such information is privileged financial information. Similarly, the fourth requirement would require a bank, insurance company or investment manager to disclose the identity and investments amount of all its clients, or otherwise argue that such information was privileged commercial or financial information. With regard to the final requirement -- that the QPAM is not disqualified under Section I(g) -- it is unclear what records would be required to verify that no convictions had occurred in the last ten years by the investment manager, its affiliates or any 5% owner.

If EBSA clarifies that an investment manager's balance sheet and client lists are privileged, and that there are no records that are needed to verify that no disqualifying events have occurred, then the requirement does not provide any additional burden or benefit, since these records are readily available to the public. However, adding this record-keeping and disclosure condition without clarification that balance sheets and client lists are privileged and that no records are required to verify compliance with Section I(g), will result in banks, insurance companies and investment managers ceasing to rely on the QPAM Exemption, thereby limiting the types of transactions they will engage in for their plan clients or ceasing to manage plan assets entirely. Restricting the investment strategies available to plans and reducing the number of investment managers available to plans is not in the interests plans or their participants.

III. The mandated contract provisions do not provide plans with any meaningful protections; however, the ambiguity they create will reduce the number of investment strategies and managers available to plans.

The proposed amendment would require that all investment management agreements between a plan and a manager relying of the QPAM Exemption provide for: (i) immediate liquidity without penalty or fees; and (ii) an indemnity for actual losses for any damages that directly result from a violation of applicable laws, a breach of contract, or any claim arising out of the conduct that is the subject of a Criminal Conviction or Written Ineligibility Notice (as such terms would be defined in the QPAM Exemption) of the QPAM, an affiliate or an owner, direct or indirect, of a five (5) percent or more interest in the QPAM. Actual losses specified in the proposed amendment include losses and costs arising from unwinding transactions with third parties and from transitioning plan assets to an alternative asset manager. It is unclear if this would also include losses that result from a "fire sale" resulting from the plan's right to demand immediate liquidity. Requiring investment managers to assume a nonquantifiable liability for actions of an affiliate or owners with as small as a 5% interest is not in the interests plans or their participants, as it will almost certainly result in plans having fewer investment strategies available and fewer investment managers willing to manage plan assets.

Since many investment strategies have limited capacity and many of the managers with the best historical performance limit the number of investors they will take on as clients, the burdens that would be imposed by the proposed amendment will limit the investment choices available to plans. Additionally, the existing rules adequately protect the interests of plans and their

participants. When a QPAM, its affiliate or 5% owner is convicted of a listed crime, it ceases to be a QPAM and can apply to EBSA for an individual exemption. However, if the QPAM is directly involved in the suspect activity, plans typically do not wait for a conviction, but rather sue the QPAM for breaching its duties under ERISA. For example, when Allianz Global Investors directly engaged in criminal conduct with respect to its Structured Alpha product, it was promptly sued by many of its pension plan clients.

Almost all management agreements rely on Section 408(b)(2) for the receipt of fees by an investment manager. Therefore, the proposed requirements that the manager "not restrict the ability of a client plan to terminate or withdraw from its arrangement with the QPAM" and not "impose any fees, penalties, or charges on client plans in connection with the process of terminating or withdrawing from an Investment Fund managed by the QPAM…" is unnecessary and repetitive. In order to comply with Section 408(b)(2), the investment manager already must "permit termination by the plan without penalty to the plan on reasonably short notice under the circumstances to prevent the plan from becoming locked into an arrangement that has become disadvantageous." Similarly, Section 409 of ERISA already provides all plans with indemnification for any breach of the duties imposed on a fiduciary. This provision is repetitive and adds unnecessary cost without providing additional meaningful protection to ERISA plans.

EBSA should also remove the requirement that a QPAM not employ or knowingly engage any individual that participated in the conduct that is the subject of a Criminal Conviction or Written Ineligibility Notice, regardless of whether the individual is separately convicted in connection with the criminal conduct. "Participated in the conduct" is vague and difficult, if not impossible, to independently discover; if EBSA retains this condition, the exemption should specify that a representation by the potential employee that "he or she did not participate in conduct that was the subject of a Criminal Conviction or Written Ineligibility Notice" should be sufficient to satisfy this condition.

IV. The decision maker requirement proposed in Section I(c) is overbroad and will prevent many investments that benefit plan and their participants.

Notwithstanding EBSA's contention, the proposed amendment of Section I(c) is not consistent with the original intent of the QPAM Exemption. The original QPAM Exemption was clear and understood by practitioners. A named fiduciary could not appoint a QPAM to approve a pre-negotiated transaction, nor could the appointing fiduciary retain a veto or approval right over any transaction. However, as noted in the preamble to the proposed exemption, "Section I(c) of the proposal requires that the QPAM function as the decision maker of the investment fund for all covered transactions. In general, the terms of the transaction are also to be negotiated by the QPAM. However, a specific transaction may be effected by a person or entity that acts under the authority and general direction of the QPAM." In the preamble to the final QPAM Exemption, the Department stated:

> Several commentators raised the question whether the proposed exemption would apply to transactions which are subsidiary to a primary transaction, but which have not been actually negotiated by the QPAM. It was explained, for example, that a QPAM may purchase an office building from a party in interest on behalf of an

> investment fund where several of the existing lessees are also parties in interest with respect to plans participating in the investment fund. Under those circumstances, the terms of the investment fund. Under those circumstances, the terms of the subsidiary transaction would not have been negotiated by the QPAM. According to the comments, the value of the exemption would be greatly diminished if it did not provide relief for such transactions. Another commentator suggested that the Department clarify the exemption to include subsidiary transactions with parties in interest where the primary transaction negotiated and approved by the QPAM involves a person who is not a party in interest. It is the view of the Department that section I(c) of the exemption will be deemed satisfied in the case of subsidiary transactions if the QPAM reviews the terms of the subsidiary transactions if the QPAM reviews the terms of the subsidiary transactions as part of its determination that the transaction, as a whole, is prudent and otherwise in the best interests of plan participants. The Department notes, however, that it does not interpret section I(c) as exempting a subsidiary transaction unless such transaction is itself subject to relief under the class exemption and the applicable conditions are otherwise met. In this regard, the Department expects that the determination of the purchase price of a building would appropriately reflect the effect on the value of the building of leases contained therein which might not contain fair market value terms due to the passage of time or changed economic conditions. In addition, the Department further wishes to emphasize that transactions which are part of a broader agreement, arrangement or understanding designed to benefit parties in interest will not be considered to be transactions for which the QPAM is the independent decision maker.

Many investment managers are presented with co-investment or participation opportunities by independent parties that: (i) manage investment funds in which the investment manager has invested; (ii) are counterparties they have dealt with in previous transactions; or (iii) know that the investment manager has capital to deploy. These investments are presented to the investment manager, with detailed disclosure of the potential investment, its risk/return profile and the terms and conditions of the transaction and investment, as an investment opportunity for the investment manager to consider for its clients. The terms of the investment have been negotiated, and while the investment manager usually is provided with consent rights, the manager runs the investment. The manager of the co-investment does not know for which clients of the investment manager, if any, the investment manager might determine the co-investment opportunity appropriate. The investment manager has absolute discretion to accept or reject the present investment. Many managers of co-investment opportunities are not registered investment advisors, and others that might be able to qualify as QPAMs are not able to rely on the QPAM Exemption since the investment manager presented with the co-investment opportunity has complete discretion to accept or reject the investment. If the investment manager determines that the co-investment is appropriate for its plan clients, the counterparties to these transactions typically rely on the QPAM Exemption to assure that no inadvertent Section 406(a) violation will occur as a result of the transaction.

Notwithstanding that the QPAM Exemption currently covers transactions effected by a person or entity that acts under the authority and general direction of the QPAM, the proposed amendment

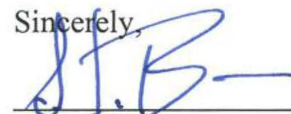
would prevent plans from participating in these types of investment opportunities. Co-investment and participations are offered to highly sophisticated investment managers who are able to weigh the risks and rewards of each opportunity as well as the terms of each transaction. These opportunities are presented by parties who have no ability to control the investment manager and who do not know which, if any, of the investment manager's clients might participate in any particular opportunity. These co-investment opportunities do not raise the "rent a QPAM" abuse the Department eliminated in the original QPAM Exemption. In these transactions, the QPAM retains all authority to make or reject the investment, retains fiduciary responsibility for the investment and retains its authority and direction over the transaction. If EBSA seeks to eliminate a category of investment opportunities available to plans, it should describe the harm it is seeking to prevent.

V. EBSA should refine the new dollar thresholds.

EBSA should clarify that the new dollar thresholds published by January 31st each year will not be applicable until January 1st of the following year. Although it is our understanding that this was the intent, clarity should be given so that investment managers are not retroactively made unable to utilize the QPAM Exemption in the first month of a particular year.

The administrative burden of yearly updates is substantial. Every QPAM will need to check for the updated dollar thresholds each year and there is little benefit to accomplishing the Department's goals to such consistent updating. EBSA noted that "The QPAM Exemption was originally granted, in part, on the premise that large financial services institutions would be able to withstand improper influence...". We understand that inflation may over time require EBSA to update such thresholds, as they did in 2005. Considering the burden on QPAMs and plans created by changing the threshold annually, we recommend EBSA update the threshold every five years. For administrative convenience, we would recommend the first such update be published by January 31, 2024, to take effect January 1, 2025. This will still limit the QPAM Exemption to large financial institutions; however, it will dramatically reduce the administrative burden of such changes upon plans and QPAMs. As proposed, if a manager is near the threshold, it must be concerned on an annual basis that it will no longer be able to utilize the QPAM Exemption and it will need to confer with plans about other potential options. If such an issue only appeared every five years, it would allow investment managers and plans to appropriately plan in advance for any concerns related to being near the minimum threshold.

Sincerely,



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