AMERICAN INVESTMENT COUNCIL
Growth Through Long-Term Investment

October 11, 2022

VIA ELECTRONIC SUBMISSION

Ms. Lisa M. Gomez
Assistant Secretary of Labor
Office of Exemption Determinations
Employee Benefits Security Administration
U.S. Department of Labor
200 Constitution Avenue N.W., Suite 400
Washington, DC 20210

Re: Proposed Amendment to Prohibited Transaction Class Exemption 84-14 (QPAM Exemption) (RIN 1210-ZA07)

Dear Assistant Secretary Gomez:

The American Investment Council (the "AIC" or "we", as applicable) appreciates the opportunity to comment on the Proposed Amendment to Prohibited Transaction Class Exemption 84-14 (QPAM Exemption) ("Proposed Amendment") issued by the Department of Labor ("Department").[1] The Proposed Amendment would, if finalized in its current form, impose significant new requirements on asset managers, and would reduce the number of asset managers willing and able to serve as a qualified professional asset manager ("QPAM"). This would harm retirement plans and their participants as they would lose access to high-quality investment managers and to investments where counterparties are parties in interest under the Employee Retirement Income Security Act of 1974 ("ERISA"). We are, therefore, concerned that the Proposed Amendment would violate ERISA Section 408(a)(2)'s requirement, namely, that any class exemption must be "in the interests of the plan and of its participants and beneficiaries." The Proposed Amendment also raises significant concerns related to an agency's ability to create a private right of action, as well as whether the investigation and disqualification provisions provide even the minimal due process rights required under the U.S. Constitution.

The AIC is an advocacy and resource organization established to develop and provide information about the private investment industry and its contributions to the long-term growth of the U.S. economy and retirement security of American workers. Member firms of the AIC consist of the country's leading private equity and growth capital firms united by their successful partnerships with limited partners and American businesses. For further information about the AIC and its members, please visit our website at http://www.investmentcouncil.org.

Executive Summary

First, we urge the Department to withdraw the Proposed Amendment. The Department points to no basis, and offers no evidence, that the decades-long reliance by retirement plans on

[1] 87 Fed. Reg. 45204 (July 27, 2022).

Prohibited Transaction Exemption (PTE) 84-14 (the "QPAM Exemption")[2] has harmed ERISA plans or participants. Nor does the Department cite to any abusive practice or manipulation of the QPAM Exemption's protective conditions. In short, we are concerned that the Proposed Amendment represents a solution in search of a problem.

Plans and their fiduciaries have relied on the QPAM Exemption as perhaps the most efficient exemption available to invest plan assets for approximately 38 years, relying on sophisticated independent institutional asset managers, who are able to invest broadly as ERISA fiduciaries, without having to worry about potentially transacting with a party in interest. The QPAM Exemption benefits plans, and not asset managers, as it provides ERISA Section 406(a) relief only, rather than relief under ERISA Section 406(b) (which could allow a fiduciary to invest where the asset manager itself faced a conflict). Should the Department move forward and finalize the Proposed Amendment in its current form, we think there is a serious question as to whether the Department will have satisfied ERISA Section 408(a)(2)'s requirement that any class exemption must be "in the interests of the plan and of its participants and beneficiaries." We also believe that the Proposed Amendment fundamentally changes the terms and nature of the QPAM Exemption, and, as described herein, will upend longstanding relationships between plans and asset managers.

Second, the Proposed Amendment raises significant concerns related to the Department's ability to create a private right of action.[3]

Third, should the Department decide to proceed with the Proposed Amendment, we ask the Department to address seven provisions that we have identified as most troubling: (A) the proposed QPAM indemnity obligation, (B) the Department's broad discretion in determining the ineligibility of a QPAM, (C) the new winding-down process following the ineligibility of a QPAM, (D) the increased asset under management and capitalization thresholds, (E) non-prosecution/deferred prosecution agreements and other expanded bases for ineligibility, (F) more stringent rules regarding the involvement of parties in interest in investment decisions and (G) the ability of the Department and other regulators to examine the QPAM's trade secrets and confidential commercial and financial information as part of the new recordkeeping requirement.

II. Concerns with the Department's Proposed Amendment

A. QPAM's Indemnity Obligation

We are concerned that the Department's requirement that QPAMs contractually agree to indemnify, hold harmless, and restore actual losses (including losses and costs related to unwinding transactions and transitioning to another asset manager) to plan clients for damages directly resulting from a violation of applicable law, a breach of contract, or any claims arising out of the QPAM's ineligibility[4], will lead to fewer asset managers being willing to serve as QPAMs, as well as higher costs to plans for asset management services.

---

[2] 49 Fed. Reg. 9494 (March 13, 1984).
[3] See *Chamber of Commerce of U.S.A. v. U.S. Dep't of Labor*, 885 F.3d 360, 384-85 (5th Cir. 2018).
[4] 87 Fed. Reg. 45204, 45208; Proposed Exemption §I(g)(2)(C).

The proposed indemnity will increase costs for three reasons. First, the Proposed Amendment's indemnity obligation is excessive. Second, it is unclear whether QPAMs would be able to purchase insurance to cover the possible indemnity (and even if they could, at what cost). Third, updating agreements to provide the indemnity will be expensive as asset managers likely will need to review, negotiate and/or amend other terms in their management agreements, such as fees or scope of services.

The dollar amount associated with a QPAM's proposed indemnity obligation, especially in connection with distributing assets from fund vehicles invested in illiquid investments or paying for plan clients to conduct RFI/RFP processes for a successor manager, could be excessive, particularly when one considers that these obligations can arise when the asset manager has not even been charged with a crime. Asset managers need to be able to confidently make long-term illiquid investments for plans to help them achieve targeted risk-adjusted rates of return. Requiring indemnification that covers losses associated with "fire sales" of assets should a manager be disqualified from acting as a QPAM essentially requires managers to give plans an option to either continue to hold an illiquid asset post -disqualification or instead to receive from the manager the same amount in cash. From an asset management standpoint, the proposed indemnity will cause managers to refuse these types of investment mandates for plans or discontinue making funds that invest in these types of illiquid assets available to plans. Further, the proposed indemnity will deter managers from being willing to invest even defined benefit plan assets in less liquid investments as the manager would bear the risk that it would be providing an illiquidity premium to a plan that is not forgoing liquidity. The Proposed Amendment would appear to require a disqualified manager to bear the costs associated with replacing that manager. This too is a term that likely will result in significant fee increases. RFI and RFP costs vary; negotiating costs also vary. This provision forces asset managers to consider including in their fees the risk of disqualification and the risk that a plan would choose a very expensive replacement search if it knows that it isn't bearing the cost.

In its cost/benefit analysis, the Department concluded that the costs to update both existing and future management agreements would be nominal, estimating that it would take up to one hour to amend the agreements to include the required indemnity language and then two minutes to send the amendments to each client.[5] This conclusion is based on false assumptions and materially understates the time and cost to make these changes, including, but not limited to, the time to craft language, review agreements, amend the agreements, send notices to clients, and get necessary consent. A decision to add an indemnity to any agreement is a major negotiation point and may change the economics of the arrangement. Thus, to the extent that asset managers are willing to bear the indemnity risk, asset managers likely will negotiate other changes, including, potentially, an increase in fees charged to the plan.

B. The Department's Broad Discretion in Determining the Ineligibility of a QPAM

We are concerned that the Department's broad discretion in determining whether a QPAM might be disqualified in certain cases essentially creates a system where the Department will act as not only the judge, jury, and executioner, but also as the investigator. This hardly has

[5] 87 Fed. Reg. 45204, 45218.

the hallmarks of a fair and neutral process and, in our view, raises serious questions as to whether it would afford asset managers even basic due process required under the U.S. Constitution.[6]

This also harms plans and plan participants because it creates new uncertainty for plan fiduciaries who would like to make long-term investment decisions and delegate management to asset managers but who under the Propose Amendment would have to take into account that there is heightened risk that any long-term mandate could be shortened by an ineligibility determination.

C. Winding-down Process in the Event of QPAM Ineligibility

We are concerned that the winding-down period provides only illusory relief, and is of little or no benefit to plans and their participants. While the winding-down process is intended, in part, to provide a grace period of relief for past transactions and any on-going transactions continued during the one-year winding-down period,[7] asset managers would be able to rely on the QPAM Exemption during this period ***only*** to unwind previous transactions, and would not be able to make any new investments on behalf of plan clients.[8] If asset managers cannot deploy or redeploy existing plan clients' assets in reliance on the QPAM Exemption, it could make it extremely challenging for a plan to conclude that it is prudent to continue to rely on the QPAM or for the QPAM to satisfy its own fiduciary obligations.

D. Increase of Asset Management and Capitalization Thresholds

We are concerned that the Department's proposed increase in the asset management and capitalization thresholds may create a relatively high barrier to entry in the QPAM services marketplace, which may squeeze out smaller asset managers, emerging asset managers, and startup asset managers, which are otherwise capable of providing quality QPAM services.[9] If other asset managers choose to stop providing QPAM services, the increase in these thresholds will doubly harm plans and their participants as the market for QPAMs will become increasingly concentrated. This could harm participants as less competition could lead to less diversity among management strategies or give the remaining managers significantly stronger pricing power.

Additionally, the indexing of the thresholds creates an unworkable situation where a QPAM today may no longer be one tomorrow simply due to inflation.

---

[6] Both the U.S. Federal Trade Commission and the Securities and Exchange Commission use in-house adjudicatory structures that provide for greater due process, and the Supreme Court has identified deficiencies in those structures. *Lucia v. Securities and Exchange Commission*, 138 S.Ct. 2044, 2044 (2018); *Cochran v. Securities and Exchange Commission*, 20 F.4th 194, 194 (5th Cir. 2021); *Axon Enterprise, Inc. v. Federal Trade Commission*, 986 F.3d 1173, 1173 (9th Cir. 2021).

[7] 87 Fed. Reg. 45204, 45211; Proposed Exemption §I(j).

[8] 87 Fed. Reg. 45204, 45211; Proposed Exemption §I(j).

[9] Proposed Exemption §VI(a).

E. Non-Prosecution/Deferred Prosecution Agreements and Other Expanded Bases for Ineligibility

We are concerned that the Department's expansion of QPAM ineligibility presents several material issues.[10]

First, expanding QPAM ineligibility to U.S. and foreign non-prosecution agreements and deferred prosecution agreements (collectively, "Deferred Prosecution Agreements") is at odds with recent guidance from the Department that a Deferred Prosecution Agreement would not constitute a criminal conviction that would disqualify an asset manager as a QPAM.[11] Moreover, the Department seemingly has unfettered discretion as to whether a QPAM has entered into a foreign-equivalent of a U.S. Deferred Prosecution Agreement, which raises serious questions as to whether the Department even has the necessary proficiency in, for example, criminal justice and international law, or jurisdictional authority for such purposes. We are also concerned that the expansion of ineligibility to Deferred Prosecution Agreements may tamp down on an asset manager's willingness to enter into Deferred Prosecution Agreements, thereby potentially undermining efforts of the U.S. Department of Justice ("DOJ") and other U.S. and foreign regulators and prosecutors related to Deferred Prosecution Agreements, as well as making it more challenging for asset managers to resolve legal issues with the government. This also creates Executive Branch tension where the DOJ uses deferred prosecution agreements in accordance with DOJ policy. We would hope the DOJ is aware of the Proposed Amendment's terms as the Proposed Amendment will likely substantially increase the amount of time and resources DOJ spends resolving litigation.

Second, the Proposed Amendment's ineligibility criteria sweeps up "substantially equivalent" foreign crimes. As the Department is no doubt well aware, whether a foreign crime has an analog under U.S. law, much less its "substantial equivalent," raises particularly complex questions. We are skeptical the Department has the competence and jurisdiction to fairly and accurately interpret foreign law for these purposes. We also express concern over the Department's conflicting guidance on whether foreign crimes are disqualifying conduct for purposes of the QPAM Exemption.

Third, we are also concerned that the inclusion of "engaging in a systematic pattern or practice of violating the conditions of" the QPAM Exemption as a form of prohibited misconduct may result in unwieldy, unpredictable and draconian results, particularly in light of the fact that the Proposed Amendment separately targets intentional violations of the Proposed Amendment. In today's world of atomization, a "systematic pattern" can easily result from a typo or clerical error and should not, on its own, form the basis of QPAM ineligibility.

Fourth, the expansion of QPAM ineligibility renders the Proposed Amendment less administratively feasible, as it increases the frequency that asset managers will need to seek individual exemptions from the rarity it is today to some higher frequency. In this respect, we are

[10] 87 Fed. Reg. 45204, 45209.
[11] DOL Advisory Opinion 2013-05A.

deeply troubled by the Department's newly concerted effort to reduce the number of asset managers who receive, and ways in which to receive, exemptive relief.[12]

Fifth, taken as a whole, the concerns identified above make clear that the Proposed Amendment's expanded basis of ineligibility would leave ordinary people unable understand what conduct is prohibited, and could leave the Department in a position that could be perceived as leaving it free to treat QPAM's facing ineligibility differently depending on non-QPAM Exemption-related criteria. This creates serious vagueness concerns that could violate the U.S. Constitution.

F. Involvement in Investment Decisions by Parties in Interest

We are concerned that the Department's proposed requirement that the terms, commitments, investments, and associated negotiations of a transaction on behalf of plan clients must be the "sole responsibility" of the QPAM,[13] (which the Department claims is intended to prevent the QPAM from being a "mere independent approver of transactions"[14]) harms participants and plans. If a party in interest cannot present to, or initiate a transaction with, a QPAM, it might functionally mean that no one (other than, presumably, the QPAM's internal staff) could approach a QPAM with an investment idea nor could a plan committee sign off on or propose investment strategies. Where a plan fiduciary or any other party-in interest (other than the QPAM), identifies a plan investment that involves a party in interest, the plan and participants benefit from access to that investment under today's terms where an independent institutional investment manager can evaluate and make the decision on the investment so that the plan and its participants can benefit.[15]

G. Recordkeeping Requirement

We are concerned that the Department's proposed requirement, that any authorized employee of the Department, the Internal Revenue Service or other state or federal regulator will have the right to examine trade secrets or confidential commercial or financial information with respect to the QPAM and its affiliates, as part of the recordkeeping requirement set forth in Part VI(t) of the Proposed Amendment, may ultimately result in the public disclosure of such information.[16] Needless to say, the public release of such confidential, sensitive and proprietary information would cause significant financial, reputational and commercial harm to the respective asset manager.

---

[12] See, e.g., 87 Fed. Reg. 21600 (Apr. 12, 2022) ("Procedures Governing the Filing and Processing of Prohibited Transaction Exemption Applications").
[13] Proposed Exemption §I(j).
[14] 87 Fed. Reg. 45204, 45213.
[15] While we could highlight any number of transactions that could potentially run afoul of this provision and that are vital to efficient plan investment, we are highlighting two. First, when plan fiduciaries hire multiple QPAMs to act as investment manager to plans, the plan fiduciaries typically direct the QPAM to invest using specific mandates. Second, plan fiduciaries are often given notice of co-investment opportunities which are identified by asset managers and an opportunity to weigh in before a plan participates.
[16] 87 Fed. Reg. 45204, 45232.

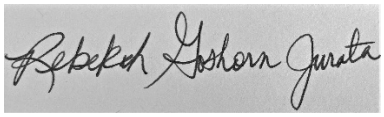
We urge the Department to expressly permit the QPAM to shield from examination by any party, including the Department and other regulators, trade secrets and other confidential commercial and financial information, for purposes of complying with the Proposed Amendment's recordkeeping requirement. Alternatively, we ask for express assurances from the Department that the trade secrets and confidential commercial and financial information, which are part of such examination, will be considered by the Department to be private and confidential for purposes of the U.S. Freedom of Information Act ("FOIA").[17]

* * *

In sum, we ask that the Department withdraw the Proposed Amendment and leave the QPAM Exemption in place in its current form. Should the Department proceed with the Proposed Amendment, we urge the Department to address the concerns raised herein.

Thank you, in advance, for your consideration.

Respectfully submitted,



Rebekah Goshorn Jurata
General Counsel

[17] 5 U.S.C.S. § 552. See, e.g., *Food Mktg. Inst. v. Argus Leader Media*, 139 S. Ct. 2356, 2366 (2019) ("At least where commercial or financial information is both customarily and actually treated as private by its owner and provided to the government under an assurance of privacy, the information is "confidential" within the meaning of [FOIA's] Exemption 4.")