



October 11, 2022

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Office of Exemption Determinations  
Employee Benefits Security Administration  
U.S. Department of Labor

Re: Comments on Proposed Amendment to Prohibited Transaction Class Exemption 84-14 (the QPAM Exemption) – Application No. D-12022, Z-RIN 1210 ZA07

Ladies and Gentlemen:

The Stable Value Investment Association (“SVIA” or the “Association”) appreciates the opportunity to comment on the Department’s proposed amendments to Prohibited Transaction Class Exemption 84-14 (the “QPAM Exemption”), as published in the *Federal Register* at 87 Fed. Reg. 45,204 on July 27, 2022. Our comments focus on the impact that the proposed amendments may have on the management of stable value investments on behalf of defined contribution plans, such as participant-directed 401(k) plans that make stable value available as an investment option to their plan participants and beneficiaries.

## **SVIA**

The SVIA is a non-profit organization dedicated to educating employers, employees, policymakers and the public about the importance of saving for retirement and the contribution stable value investment products can make toward achieving a financially secure retirement. As of December 31, 2021, the SVIA’s members managed more than \$906 billion invested in stable value investments offered in more than 206,000 defined contribution plans by more than 25 million participants. The SVIA’s 68 member companies represent all segments of the stable value community, including public and private retirement plan sponsors, insurance companies, banks, investment managers, and consultants.

## **Overview of Stable Value Investing**

“Stable value” refers to a relatively low-risk asset class that seeks to achieve consistently positive returns while providing investors with capital preservation and liquidity. In some ways, stable value funds are like certificates of deposit offered by banks and other financial institutions – both asset classes ensure protection of principal and a specified rate of return. But because of how deposited monies are reinvested, stable value funds typically have returned substantially higher yields than certificates of deposit. For these reasons, Americans who save for retirement

through employer-sponsored retirement plans have chosen to invest in stable value products in recent decades, particularly in times of uncertainty or economic distress.

Since its inception in the 1970s, stable value has become one of the most common capital preservation options available for retirement saving. According to a 2019 survey, 78% of all U.S. defined contribution plans offer stable value products. In total, U.S. savers hold more than \$906 billion in stable value funds, which in 2021 represented 10% of defined contribution plan assets.

Stable value products generally are available as investment options to individual investors through defined contribution savings plans, including 401(k) retirement plans subject to ERISA. Under the terms of the product, the plan participant receives preservation of principal and a specified rate of return. The moneys are then invested in a diversified array of assets, mostly bonds, designed to earn consistent positive returns over time. But regardless of conditions in the financial markets, individual participants' access to the principal and contracted rate of return remains protected.

This protection of principal and the rate of return is achieved through one or more investment contracts used to ensure that plan participant withdrawals can be made at the contract value, which is the participant's interest in the stable value fund<sup>1</sup> – the amount of invested principal plus the accrued interest – rather than the current market value of the portfolio. These investment contracts can take various forms, depending on the particular stable value arrangement. For example, many are so-called “wrap contracts,” which are contracts from insurance companies or banks that “wrap” a managed portfolio of fixed-income securities to ensure contract value payments to plan participants and beneficiaries even when the portfolio's market value is below its contract value. Others, such as “guaranteed investment contracts,” are issued by insurance companies and supported by the assets of the insurance company's general account. Contract value withdrawals, referred to as “benefit responsiveness,” is a characteristic unique to all stable value products and investment contracts.

The investment manager of the stable value fund is responsible for selecting and negotiating investment contracts to achieve contract value treatment for the stable value fund's fixed-income securities portfolio. To address potential prohibited transaction issues, parties entering into investment contracts commonly rely on the QPAM Exemption. The contracts that do so typically provide that if the QPAM Exemption becomes unavailable for any reason, the contract may terminate immediately unless alternative arrangements can be made, either to reestablish QPAM Exemption coverage (such as through a manager change, if needed) or to assure the investment contract provider that another exemption is available. If the investment contract is terminated, the plan participants may lose contract value treatment for their stable value fund investments, which would be reflected in the reported value of their accounts and, if they withdraw assets from the stable value fund, affect the value of the amounts they withdraw. If, at the time of withdrawal, the

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<sup>1</sup> As used herein, the term “stable value fund” may refer to a stable value investment product that is in the form of a separately managed account solely for a particular plan, or alternatively a commingled investment fund available to multiple plans, typically in the form of an insurance company pooled separate account or a bank collective investment fund.

market value of the portfolio is below what the contract value would have been, the plan participants would suffer a loss upon their withdrawal.

### **Comments on the Proposed Amendments**

The focus of our comments is on making sure that the proposed amendments do not have unintended effects on the use by defined contribution plans of stable value as an investment option for millions of plan participants and beneficiaries, or on the ability of stable value fund managers to make investments or obtain the products and services they need for purposes of managing these investment options.

A summary of SVIA's comments are as follows (note that capitalized terms refer to those terms as defined in the proposed amendments):

- *“Sole responsibility” provision (revised Section I(c))* – should be revised to clarify that the proposed changes (1) would not prevent a plan fiduciary that is independent of the QPAM and the Party in Interest engaging in a covered transaction with the plan, such as a plan sponsor, from being involved in negotiating investment guidelines with investment contract providers as part of its fiduciary oversight role, or a QPAM from otherwise coordinating with other plan fiduciaries for purposes of fulfilling its ERISA fiduciary responsibilities in managing the Investment Fund; and (2) would not prevent a Party in Interest from proposing transactions for a QPAM's consideration where the Party in Interest is not acting on behalf of the Investment Fund.
- *“Investment Fund” condition (revised Section I(c))* – should be clear that a stable value fund should be treated as an Investment Fund “established primarily for investment purposes” for purposes of the exemption.
- *Ineligibility provisions (proposed Sections I(g) through (j))*:
  - *“Actual losses”* – no indemnification or restoration of “actual losses” should be required, because of difficult questions as to what would constitute “actual losses” that could affect the allocation of risk between plans and investment managers, resulting in increased costs for plans. But if some form of this condition is maintained, it should be clarified to provide that (1) the market value-to-contract value differential in a stable value portfolio would not be treated as an “actual loss” upon a QPAM's ineligibility; (2) portfolio transition costs would not be treated as “actual losses;” and (3) “actual losses” would be limited to actual losses to portfolio investments caused directly by the inability of the QPAM to continue to rely on the QPAM Exemption.
  - *Winding-down period* – should not restrict “new” transactions during the winding-down period, and its length should take into consideration the extended termination provisions in stable value contracts that are designed to avoid adverse consequences for the plan.
  - *Written Management Agreement requirements on QPAM ineligibility* – should not require changes to written management agreements without reassessing the associated costs and benefits of doing so, and instead impose any such requirements as conditions

of the exemption only if ineligibility occurs and the stable value fund manager needs to continue to rely on the QPAM exemption.

As a general matter, the following comments are intended to highlight those issues of particular concern to the stable value industry because of the manner in which they may impact stable value products and services. The Association and its members also have concerns about several aspects of the proposed amendments that may have broader impacts not necessarily specific to stable value, as well as with regard to the anticipated costs of coming into compliance. On these matters, we refer the Department to the comments being submitted by other financial services industry firms and trade associations that deal with those matters in more detail than this letter. We also refer the Department to the threshold questions raised in other comments as to why there is a need for any amendments to the QPAM Exemption at all, given that the provisions that would be amended have worked well in their present form for over 38 years.

#### **“Sole Responsibility” Provision (Revised Section I(c))**

One of the proposed changes would revise Section I(c) of the exemption, which currently requires that the terms of the transaction be “negotiated on behalf of the investment fund by, or under the authority and general direction of, the QPAM,” to require instead that the “terms of the transaction, commitments, and investment of fund assets and any associated negotiations on behalf of the Investment Fund are the sole responsibility of the QPAM.” The amendments would further add that “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 I(c).”

We have concerns about the possible scope of “sole responsibility” requirement and of the exclusion from relief for any transaction “planned, negotiated, or initiated by a Party in Interest, in whole or in part, and presented to a QPAM for approval,” as follows:

- *Plan sponsor directions and oversight:* A stable value fund manager may often take direction from a plan sponsor (or other plan fiduciary designated as the plan’s named fiduciary for investment matters, such as a plan committee) on, for example, permissible investment guidelines for not only the stable value fund itself, but also for the stable value fund’s investment contracts, given that, for example, in the case of wrap contracts, wrap providers typically negotiate investment guidelines for the wrapped assets to reduce their risk exposure on the fixed income portfolio (as described in DOL Advisory Opinion 2011-07A, which addressed certain considerations under Section I(a) of the QPAM Exemption). Because stable value fund managers often negotiate investment contracts in reliance on QPAM Exemption relief subject to this oversight from the plan sponsor/plan fiduciaries, the question is what level of plan sponsor/plan fiduciary involvement in the process of setting the investment guidelines would be acceptable under the proposed language.

The discussion of the proposed amendments does acknowledge that “providing general investment guidelines to the QPAM” would not be inconsistent with the amended

language, as part of “oversight associated with plan transactions.” 87 Fed. Reg. at 45,213. But in context, this would appear to contemplate guidelines governing the QPAM’s management of the Investment Fund under the QPAM’s investment management agreement, thereby not necessarily addressing whether another plan fiduciary’s involvement in the QPAM’s negotiation of investment guidelines with a third party – here, the wrap provider – would go beyond the limited activities that this language contemplates.

Our view is that the plan sponsors/plan fiduciaries should be able to have meaningful involvement in the process of negotiating an investment contract’s investment guidelines without affecting the ability of the investment manager to rely on the QPAM Exemption. This involvement is not inconsistent with the goal of Section I(c), since the stable value fund manager ultimately handles the negotiations with the investment contract issuer and has the final decision-making authority over entering into the contract. Depriving the plan sponsors/plan fiduciaries of the ability to be involved in this process would interfere with their ability to fulfill their ERISA fiduciary responsibility to oversee the stable value fund manager and the terms of the stable value fund investment option. We further note that, in such situations, both the stable value manager and the plan sponsor would, in accordance with the terms of other conditions of the QPAM Exemption, be independent of, and unrelated to, the wrap provider.

A similar issue is presented by pooled stable value funds and separately managed accounts that feature tiered or multiple investment structures, which, by providing diversification among wrap providers and underlying investment managers, seek to mitigate the impact of any one wrap provider’s financial condition or single investment portfolio’s performance on overall fund returns and the ability to support benefit responsiveness. These investment structures require negotiation and coordination among the stable value fund’s overall manager and underlying managers, each of which may be a QPAM with respect to its respective investment portfolio, to make sure the investment guidelines are consistent or complementary across the stable value fund and to avoid excessive overlap among the portfolios. If this type of coordination among managers relying on the QPAM Exemption affects whether a QPAM would be treated as having “sole responsibility” over particular transactions, the effect would be to undermine a structure that has the potential to be more protective of plans than single wrap provider/manager structures, reducing choice for plans among stable value options.

If the Department continues to address Section I(c) in any final amendment, we request that the Department make clear that it does not restrict actions taken by a plan fiduciary who is independent of both the Party in Interest that would be engaging in the covered transaction with the plan, and the QPAM, for purposes of fulfilling its fiduciary responsibilities under ERISA to oversee the QPAM, or coordination by the QPAM with other fiduciaries of the plan for purposes of fulfilling such QPAM’s fiduciary responsibilities under ERISA with respect to management of the Investment Fund, so long as the QPAM has sole authority to negotiate and approve the particular transactions on behalf of the Investment Fund.

- *Interactions with broker-dealers:* Another question is whether this language would prevent a stable value fund manager from accepting suggestions from unrelated broker-dealers on fixed income trades. For example, the manager may deal on a regular basis with a broker-dealer who has come to know the types of securities in which the stable value fund manager generally invests on behalf of its managed accounts. If the broker-dealer notifies the stable value fund manager of a new offering of fixed income securities, or of available bonds that match the duration, interest rate and other terms the stable value fund manager may be seeking, would a subsequent trade in the particular securities with the broker-dealer be considered a transaction “planned ... or initiated by a Party in Interest, in whole or in part, and presented to a QPAM for approval?” In our view, such an interaction should not be restricted by this provision, because the broker-dealer is not acting as a fiduciary to the plan or exerting undue influence over the stable value fund manager’s investment decision, but rather providing information that is appropriate and helpful to the stable value fund manager in managing the stable value fund’s investment portfolio.

Similar issues could arise with derivative transactions, such as swaps, where a financial institution that may be a Party in Interest for unrelated reasons (for example, as a securities broker or an affiliate of a securities broker) may propose for the stable value fund manager’s consideration a certain derivatives-based investment strategy or type of financial instrument, thereby arguably “planning” or “initiating” a transaction.

This question arises particularly because of the use of the terms “planned” and “initiated” in the proposed additional language. If the Department continues to include changes to Section I(c) in any final amendment, the scope of the provision could be clarified by deleting these terms, on the basis that the reference to a transaction being “negotiated” by the Party in Interest and then “presented to a QPAM for approval” is sufficient to achieve the Department’s objective of restricting relief to transactions as to which the QPAM has ultimate discretionary authority and is not a “mere independent approver of transactions.” This can further be clarified by specifying that to be affected by this restriction, the “negotiation” must be “on behalf of the Investment Fund,” to exclude any suggestion that “negotiation” by the Party in Interest on its own behalf could potentially raise an issue, and could further specify that this is only an issue if the Party in Interest stands to benefit from the transaction, so that it does not restrict an independent party assisting in negotiations under the oversight of the QPAM. The result would still be to exclude the transactions we understand to be of concern to the Department – where a non-QPAM party that has authority over the plan, such as the employer that retains the QPAM, has negotiated all material terms on behalf of the plan before engaging a QPAM to approve the specific transaction, so that the QPAM has little to no input into the terms of the transaction. At the same time, it would not unduly restrict transactions on account of any type of participation in the transaction by a Party in Interest that has no authority over decision-making with regard to the plan’s assets or over the QPAM. Such a restriction would be unworkable and would undermine the exemption’s goal of providing broad relief for Party in Interest transactions.

We have an additional concern relating to another sentence proposed to be added to Section I(c): “The prohibited transaction relief provided under this exemption applies only in connection with an Investment Fund that is established primarily for investment purposes.” The term “Investment Fund” is defined to include “single customer and pooled separate accounts maintained by an insurance company, individual trusts and common, collective or group trusts maintained by a bank, and any other account or fund to the extent that the disposition of its assets (whether or not in the custody of the QPAM) is subject to the discretionary authority of the QPAM.” A stable value fund should readily fit within the “Investment Fund” definition and, we believe, given its function as a plan investment option, should be treated as “established primarily for investment purposes.” However, because a stable value fund also has other purposes, in particular offering benefit responsive payments for participant withdrawals through entering into investment contracts with insurance companies and banks, it would be helpful to clarify for avoidance of doubt (for illustration, through an example in the preamble) that (a) a stable value fund would be covered as an “Investment Fund” and (b) entering into guaranteed investment contracts, wrap contracts and other forms of stable value investment contracts on behalf of a stable value fund would be within the scope of relief.

### **Ineligibility Provisions (Proposed Sections I(g) through (j))**

We have concerns about the potential impact under the proposed amendments of a stable value fund manager becoming ineligible to rely on the QPAM Exemption with respect to a stable value portfolio, including with regard to the contemplated winding-down period.

### **Indemnification for and Restoration of “Actual Losses”**

Under the proposed amendments, the QPAM would have to agree under proposed Section I(g)(2)(C), in the event of its future ineligibility, “to indemnify, hold harmless, and promptly restore actual losses to the client Plans for any damages that directly result to them 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 of the QPAM or an Affiliate (as defined in Section VI(d)) or an owner, direct or indirect, of a five (5) percent or more interest in the QPAM.” The provision adds that “Actual losses specifically include losses and costs arising from unwinding transactions with third parties and from transitioning Plan assets to an alternative asset manager as well as costs associated with any exposure to excise taxes under Code section 4975 as a result of a QPAM’s inability to rely upon the relief in the QPAM Exemption.”

SVIA’s view is that this provision should not be added to the QPAM Exemption. It raises a number of difficult questions as to what would constitute “actual losses” in particular circumstances, as described below with regard to a termination of a stable value contract. Further, it would affect the allocation of risk between the ERISA plan and the stable value fund manager, placing risks on the stable value fund manager on account of misconduct by remote affiliates over which the stable value fund manager has little or no control, with the presumed result that stable value fund managers would negotiate for increased fees to address their assumption of greater risk, in an amount that would be difficult to predict given that the scope of “actual losses” is unclear. But in the event some form of this requirement is maintained, SVIA has the following specific comments.

As indicated above, a stable value fund manager's ineligibility to continue to rely on the QPAM Exemption could, depending on the specific arrangement, result in immediate termination of a wrap or other investment contract in accordance with its terms, possibly without regard to the availability of the one-year winding-down period contemplated by the proposed amendments. The question is what could be considered "actual losses" in the event of such a contract termination. An investment contract provides for payment of plan participants' withdrawals at the contract value of their stable value fund investments, even if the market value of the stable value fund's assets wrapped by the particular contract is below the contract value covered by the investment contract. Would the differential between the market value and contract value at the time of termination be treated as a "loss"? What if the differential is never realized as a "loss" because no participant withdrawals occur before the market value increases to reach contract value? What if the market value exceeds contract value at the time of ineligibility, but declines below contract value before the plan fiduciaries are able to find a replacement manager or the stable value manager is able to enter into a replacement investment contract?

In our view, any market value-to-contract value differential should not be treated as an "actual loss" in these circumstances. Whether any payments are made to participants at a market value that is lower than contract value would depend on a number of variables that are not a direct function of the stable value fund manager becoming ineligible to use the QPAM Exemption, such as current market conditions, the timing of the plan participant withdrawals, and the diligence of the plan fiduciaries in securing replacement manager coverage or investment contract coverage. The explanation of this condition in any final amendments should provide this as an example of what should not be considered "actual losses" for this purpose.

A further possible issue is the inclusion in "actual losses" of the costs of transitioning to an alternative asset manager. These are not the types of costs normally paid for by a terminated manager, regardless of the reason for termination. It is unclear what range of costs could be covered. Would it be just the costs of transitioning investments to a new portfolio, such as the transaction costs in selling securities from the current portfolio and reinvesting in a replacement portfolio? Or would it also include the expenses of retaining a new stable value fund manager, such as the legal costs incurred in negotiating the new investment management agreement? If there are new investment contracts involved because the new manager has different investment contract provider relationships, would the costs of negotiating and entering into those contracts, and any related increase in contract fees, be covered as well?

In our view, transitioning costs should not be included within "actual losses," as it is too broad and ambiguous a category. Many of these costs may not be the direct result of the termination of the ineligible manager, but rather a function of choices made or not made by the plan fiduciaries. If the plan fiduciaries select a new manager that does not accept any existing investments, thereby requiring higher transaction costs to transition the investment portfolio, or that engages in protracted contract negotiations that increase the plan's legal costs, those should not reasonably be the responsibility of the terminated manager. In addition, there could be a concern that plan sponsors and fiduciaries would have no incentive to limit costs related to retention of a new manager, such as legal fees, if they know the plan will not be paying them. Stable value managers may seriously consider exiting the business if they are forced to take on these types of risks over



which they would have no control, with long-term adverse impacts on plans such as reduced choice and higher fees. If the “actual losses” condition continues to be included in the exemption, it should be limited to actual losses to portfolio investments caused directly by the inability of the stable value fund manager to continue to rely on the QPAM Exemption, such as early termination of a derivative contract or forced sale of a fixed income security, as those are the losses can be traced directly to the manager’s ineligibility.

### **Winding-Down Period**

The intent of proposing a one-year winding down period following ineligibility seems to be to help mitigate consequences to plans of a QPAM’s ineligibility. However, proposed Section I(j) would not have this effect at all for the reasons discussed below.

First, the proposed provision would not permit the QPAM to engage in “new transactions” in reliance on the QPAM Exemption during the winding-down period. This raises the question of what would be considered a “new” transaction. Is the ineligible QPAM limited to permitting any past transactions to expire, or may it also take proactive steps, such as selling out of a position in particular bonds or terminating an interest-rate swap, or exercising a termination option under an investment contract that contains an automatic renewal provision?

Further, even if all of these proactive steps with respect to past transactions were permitted, the general inability of the manager to engage in new transactions during the winding-down period would still be problematic, as the ineligible manager would be required to effectively freeze the investment portfolio for the duration of the period. The implication that the Department may not grant individual exemptive relief to an ineligible manager until the end of the winding-down period, such as through the statement that a QPAM applying for an exemption must ensure it manages plan assets prudently and loyally during the winding-down period (at the end of proposed Section I(k)), further suggests that as currently drafted, this provision would not help plans.

To address these issues, the provision should be revised so that it would not restrict “new transactions” during any winding-down period.

Second, the one-year period is not sufficient to deal with certain other consequences, such as the need to fully wind down a stable value investment contract to ensure benefit responsiveness is maintained for the plan and its participants. For example, to permit termination without any adverse consequence to the plan, many wrap contracts provide an option for a phased termination over a period approximately equal to the duration of the wrapped investment portfolio, so that no securities have to be sold at a loss. To fully effectuate the intent of the winding-down provision with regard to stable value investment contracts, we propose that the winding-down period be up to the duration of the underlying investment portfolio or as otherwise provided under the terms of the contract for an extended or amortized termination.

### **Written Management Agreement Requirements**

Proposed Section I(g)(2) would require that the QPAM amend all of its Written Management Agreements with clients, to include a series of provisions addressing what would happen in the

event the QPAM becomes ineligible to rely on the QPAM Exemption. According to the Department's cost estimate, its expectation is that the related costs should be limited to one hour of in-house legal professional time to update and supplement the QPAM's 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, on the assumption that the changes could be effectuated by this mailing without any further action being required.

We believe the Department has significantly underestimated the impact of this proposed requirement. With very limited exceptions, investment management agreements typically permit amendment only through a writing signed by both parties. In the normal course, a manager's legal or contracts staff would review the agreements in need of amendment to determine the specific requirements for amendment, which could be time-consuming if the manager has used a variety of contract forms, such as legacy forms inherited as part of a merger or acquisition. A review also will be necessary to make sure that the amendment addresses any inconsistent provisions in the current agreements. If it turns out that amending the agreements requires a writing signed by both parties, the adoption of an amendment could be delayed if the client does not agree or fails to respond. The Department should not continue to impose this requirement without reassessing the associated costs and benefits in light of this information and being able to determine that the benefits outweigh the significant costs.

The correct approach would be to impose any requirements with regard to the termination of a QPAM's investment management agreement as a result of ineligibility as conditions of the exemption that need to be met only if and when ineligibility occurs, rather than requiring changes to existing contracts. The clients would be aware of these requirements through review of the terms of the exemption, and also would be receiving notice of their rights under the exemption in the event of ineligibility under proposed Section I(j)(1). The ultimate effect should be the same, with far less administrative burden on QPAMs and plan sponsors.

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SVIA appreciates the Department's consideration of these comments. The Association is available to answer any questions and to work with the Department as it moves forward.

Sincerely,

Gina Mitchell  
President