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Office of Exemption Determinations
Employee Benefits Security Administration
U.S. Department of Labor
200 Constitution Avenue NW
Washington, D.C. 20210

Submitted electronically via the Federal eRulemaking Portal

October 11, 2022

Dear Sir or Madam,

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

The Alternative Investment Management Association (AIMA)[1] appreciates the opportunity to comment on the U.S. Department of Labor's (the "Department") proposed rule to amend the Prohibited Transaction Class Exemption 84-14, i.e., the "QPAM Exemption" (the "Proposal").[2] A number of AIMA's members are qualified professional asset managers (QPAMs) and rely on the QPAM Exemption when they manage the assets of employee benefit plans that are subject to Part 4 of Subtitle B of Title I of the Employee Retirement Income Security Act of 1974, as amended ("ERISA"), or arrangements that are described in Section 4975(e) of the Internal Revenue Code of 1986, as amended (the "Code").[3] We are concerned that the Proposal will lead to various unintended and adverse consequences, including

[1] AIMA, the Alternative Investment Management Association, is the global representative of the alternative investment industry, with around 2,100 corporate members in over 60 countries. AIMA's fund manager members collectively manage more than $2.5 trillion in hedge fund and private credit assets. AIMA draws upon the expertise and diversity of its membership to provide leadership in industry initiatives such as advocacy, policy and regulatory engagement, educational programs and sound practice guides. AIMA works to raise media and public awareness of the value of the industry. AIMA set up the Alternative Credit Council (ACC) to help firms focused in the private credit and direct lending space. The ACC currently represents over 250 members that manage $600 billion of private credit assets globally. AIMA is committed to developing skills and education standards and is a co-founder of the Chartered Alternative Investment Analyst designation (CAIA) – the first and only specialized educational standard for alternative investment specialists. AIMA is governed by its Council (Board of Directors). For further information, please visit AIMA's website, www.aima.org.

[2] Department, Proposing Release, Proposed Amendment to Prohibited Transaction Class Exemption 84-14 (the QPAM Exemption), 87 Fed. Reg. 45204 (July 27, 2022) (the "Proposing Release").

[3] In this letter, we call such employee benefit plans and arrangements "Plans".

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those set forth below, and that it will ultimately harm pensions and Plan participants more than it will help them. We believe:

- The Proposal would add unnecessary complexities to the QPAM Exemption, which are likely to harm Plan participants;
- The proposed effective date would make it impracticable, if not impossible, for QPAMs to meet the new requirements described in the Proposal;
- The Department should reconsider how it implicates QPAMs for the prohibited misconduct of an affiliate that has little to no relationship or nexus with the QPAM;
- The Department should relabel and clarify the meaning and terms of the proposed "wind-down period"; and
- The Department should permit the use of certain withdrawal-related provisions during a QPAM's wind-down period.

These points are discussed in further detail below in the attached annex with relevant data provided. We would be happy to elaborate further on any of our comments raised in this letter. For additional information, please contact Daniel Austin, Director of U.S. Policy and Regulation, by email at daustin@aima.org.

Yours sincerely,

Jiří Król
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AIMA

ANNEX

1. The Proposal would add unnecessary complexities to the QPAM Exemption, which are likely to harm Plan participants.

Currently, if Plan investors hold 25% or more of any class of the equity of a fund that is not a registered investment company (a "plan asset fund"),[4] the plan asset fund and the investment manager must comply with the fiduciary requirements of ERISA.[5] Investment advisers managing plan asset funds often rely upon the QPAM Exemption because it is considered to be the best understood and therefore the most widely accepted of the prohibited transaction class exemptions. As a result, market practice, one that has developed over the past several decades, is for investment managers and counterparties to use the QPAM Exemption to manage plan asset funds. We believe that the Proposal would disrupt this market practice because the Department is proposing several changes to the QPAM Exemption that would create significant, new and unnecessary complexities for QPAMs. We believe that the Proposal would also result in several unintended and adverse consequences that will penalize Plan investors.

First, the Proposal creates significant, additional risks,[6] operating costs and administrative requirements that will compel some investment managers to limit the investments that they accept from Plans. Specifically, investment managers seeking to limit their exposure to the Proposal, assuming adoption in its current form, will need to have Plans invest in commingled funds in which the Plan participation is sufficiently limited so that the commingled funds will satisfy the ERISA 25% test so that the investment managers are not managing ERISA plan assets. Furthermore, even if current QPAMs wish to continue managing ERISA plan asset funds, they may nonetheless be forced to abandon their QPAM status because they are unable to meet the Proposal's new requirements and/or bear its corresponding increase in risks and costs. Such changes in the industry will ultimately lead to consolidation in the market and reduced investor choice because there will be fewer eligible investment managers that Plans will be able to hire and fewer available investment funds in which Plans will be able to invest.

In addition, Plans will also find it more difficult to obtain advice that is customized to their particular needs since separately managed accounts and "fund of one" products will be less available, i.e., managers may be less willing to accept investment from Plans in structures other than commingled funds with fewer than 25% ERISA investors. This winnowing and consolidation of market participants will make it more expensive for Plans and their participants to access the diverse strategies and investment opportunities that QPAMs currently offer.

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[4] As registered under the Investment Company Act of 1940, as amended (the "1940 Act").

[5] There are other exceptions to managing Plans outside of plan asset funds that are beyond the scope of this letter.

[6] For example, the application of the proposed mandatory indemnity and withdrawal provisions, especially when these new requirements would be coupled with an expansion of the criteria for QPAM disqualification. Also, the lack of clarity regarding "no new transactions" during the wind-down period, discussed further below, creates additional risk when QPAMs must still manage Plan assets with prudence and loyalty.

Second, the Proposal adds a new recordkeeping requirement that would require QPAMs to maintain records demonstrating compliance with the exemption for six years.[7] Despite the Department's expectation that "the recordkeeping requirements would impose a ***negligible*** [emphasis added] burden,"[8] this requirement will, in fact, prove incredibly burdensome and costly, as QPAMs will need to be able to demonstrate compliance for ***every transaction*** and in some cases to prove a negative, e.g., that each transaction was the sole responsibility of the QPAM. Quantitative funds and QPAMs that engage in high-volume trading more generally could face extraordinary costs to comply with this requirement – costs that would be passed on to Plan investors.

Not only would the new recordkeeping requirement be burdensome and costly, but it would also be redundant. QPAMs are already subject to extensive recordkeeping requirements by their primary regulator, i.e., as investment advisers registered[9] with the Securities Exchange Commission under the Investment Advisers Act of 1940, as amended.[10] In fact, many of the records RIAs are required to keep are very similar to and/or overlap with what the Department has proposed. Accordingly, we believe any new recordkeeping requirement should be deemed satisfied if the QPAM complies with the recordkeeping obligations of its primary regulatory authority.

Third, QPAMs will shoulder new costs for the necessary review of and revision to existing agreements with counterparties to address the requirements of the Proposal, e.g., updating the written management agreement. Because many existing agreements include specific provisions based on and responsive to the terms of the existing QPAM Exemption, the Department significantly underestimates the true costs that would materialize from review and revision of existing agreements. Depending on the number of counterparties and agreements a QPAM has that rely on the QPAM Exemption, the Department's estimated cost of revising the written management agreement - $135,540 across all QPAMs in total[11] – could be many multiples of that number, if not more, but on a per-QPAM basis, especially since many QPAMs may have hundreds of existing written management agreements. QPAMs will ultimately be forced to use assets from a plan asset fund to cover these costs, harming the Plan and its investors.

Fourth, the mandatory investment management agreement provisions will harm investors. In particular:

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7 Proposing Release, *supra* note 2, at 45213.

8 Department of Labor, Notice of Initial Regulatory Flexibility Analysis for the proposed amendment to the QPAM Exemption, Initial Regulatory Flexibility Analysis for Proposed Amendment to Prohibited Transaction Class Exemption 84-14 (the QPAM Exemption), 87 Fed. Reg. 56912, 56919 (Sept. 16, 2022).

9 Registered investment advisers ("RIAs").

10 For simplicity, we have focused in these comments on investment managers who are RIAs rather than on insurance companies or banks that could also act as QPAMs.

11 Proposing Release, *supra* note 2, at 45218.

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(a) subsection I(g)(2)(A) will force managers to "fire sale" assets (i.e., by requiring unrestricted withdrawals in funds where the existing withdrawal provisions are carefully tailored to prevent harm to non-withdrawing investors);[12]

(b) subsection I(g)(2)(B) will inappropriately shift expenses and other similar items to non-withdrawing investors (i.e., by precluding managers from withholding an investor's share of such expenses and other similar items, as well as any investor-specific items, from the withdrawal payments made to such investor); and

(c) subsection I(g)(2)(C) will subject managers to an overbroad and unclear indemnification standard, which will further disincentivize managers from agreeing to manage Plan assets.

Finally, the proposed changes to the assets under management and the shareholder/partner equity thresholds will substantially limit the ability of small and new investment managers to offer their specialized investment expertise to Plans that are seeking such expertise. The commercial reality is that Plans often require that their investment managers agree to qualify and act as QPAMs when managing plan asset funds, and if such managers are not eligible to rely on the QPAM Exemption, Plans will either (i) lose access to these managers, or (ii) be required to invest through vehicles that do not include an ERISA fiduciary standard of care and other associated protections, *i.e.*, funds that satisfy the 25% test or that are registered as investment companies under the 1940 Act. This would only result in further consolidation, reduce investor choice and increase costs on Plans.

2. The proposed effective date – 60 days after an adopting release is published in the Federal Register – would make it impracticable, if not impossible, for QPAMs to meet new requirements outlined in the Proposal.

The Proposal includes several changes related to the requirement to have a written investment management agreement.[13] One particular addition would require QPAMs to, in certain circumstances, "indemnify, hold harmless, and promptly restore actual losses to each client Plan."[14] The Proposal does not grandfather existing agreements. Therefore, QPAMs will be required to amend all existing written investment management agreements with Plans by the Department's arbitrarily determined 60-day effective date. Contrary to the Department's assertion, such amendments will not take the form of a "one-size-fits-all"[15] template, and this new requirement will create significant costs for QPAMs and Plan investors, as they work to revise and update or implement each individual written investment management agreement. Furthermore, the 60-day effective date from an adopting release's publication in the Federal Register will only compound these costs, as both QPAMs and Plans

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[12] We also note that in certain cases the Proposal may actually create a conflict between the manager's obligations under the QPAM Exemption and its obligations under applicable law (e.g., the unfettered withdrawal rights mandated by the Proposal may conflict with a manager's obligations under sanctions, AML, or other similar laws).

[13] Proposing Release, *supra* note 2, at 45208.

[14] *Id.*

[15] "QPAMs will need to send the update to each of their client Plans, but the QPAM likely would be able to prepare a single standard form with identical language and then send it to each client Plan." *Id.* at 45218.

will be required to mobilize their internal and external resources on a rush basis to re-paper existing agreements.

We also believe that these changes will in many cases require consent of Plans and other investors (including non-ERISA investors) in the commingled and other vehicles or accounts for which the manager relies on the QPAM exemption. This is because the changes are likely to have an adverse effect on investors in such vehicles or accounts. This fact materially increases both the time and cost involved in making the changes mandated by the Proposal, in each case far beyond what the Department has provided or estimated.

For QPAMs, however, the work does not end there. They have other arrangements and agreements with multiple service providers. For example, investment managers have agreements with prime brokers and other trading counterparties, trustees, administrators and others. If QPAMs are required to include a new indemnification clause in their written investment management agreement, they will likely also need to update and revise their agreements with these other parties to address the same contingencies that necessitate the new indemnifications and other required changes for Plan clients. Furthermore, QPAMs may need client consent before even initiating such changes with other parties.

Such an undertaking would be costly and time consuming even in the face of a lengthy deadline, and the Proposal's exceptionally short 60-day effective date would make an already expensive and difficult endeavor nearly impossible even for the largest QPAMs – let alone for those without similar resources. Accordingly, we would encourage the Department to consider an effective date for the changes contemplated in the Proposal that is at least two years from an adopting release's publication in the Federal Register.

3. The Department should reconsider how it implicates QPAMs for the prohibited misconduct of an affiliate that has little to no relationship or nexus with the QPAM.

The Proposal would increase the scope of violations that would affect a QPAM's eligibility to use the QPAM Exemption in circumstances where it or five percent or more of its owners or the QPAM's affiliates participate in certain prohibited misconduct.[16] In other words, if an affiliate engages in prohibited misconduct, the QPAM may be disqualified from relying on the QPAM Exemption. We disagree with this preliminary determination to cast a wider net vis-à-vis prohibited misconduct. Instead, we encourage the Department to focus on the specific entity or individual that has engaged in the prohibited misconduct to determine whether the QPAM should be permitted to continue to rely upon the QPAM Exemption.

In many instances of prohibited misconduct by an affiliate, the affiliate may have little to no relationship with the QPAM, yet the QPAM is punished notwithstanding the QPAM's compliance with ERISA and other regulatory requirements. This outcome ultimately harms the plan asset fund and Plan investors, and what the Department has proposed will only exacerbate this likelihood. In the case of foreign crimes, the Department seems to believe that they "call into question a firm's culture

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[16] *Id.* at 45208.

of noncompliance just as much as domestic crimes."[17] This generalization is simply unfounded. An isolated foreign crime committed by an affiliate does not necessarily demonstrate a culture of noncompliance, especially as it relates to the QPAM. The case is the same for a non-prosecution agreement ("NPA") or deferred prosecution agreement ("DPA"); simply because an affiliate enters into an NPA or DPA does not indicate a culture of non-compliance nor "call into question a firm's culture" as it relates to the QPAM. Accordingly, the Department should not extrapolate the conduct of an affiliate to the QPAM with which it has no or little nexus or relationship.

4. The Department should relabel and clarify the meaning and terms of the proposed "wind-down period."

Once the proposed one-year winding-down period begins, relief under the QPAM Exemption would be available only for the QPAM's existing clients.[18] However, even though the investment manager must wind-down its reliance on the QPAM Exemption for existing clients, it is not precluded from utilizing another exemption to engage in otherwise prohibited transactions during, and subsequent to, the one-year winding-down period to continue its relationship with those existing clients.

Despite this option, the market and the investment manager QPAM's counterparties may interpret that the manager can longer work with that Plan regardless of other exemptions. This perception would, in part, be due to the Department's determination to label the one-year period as a "winding-down" period, which could give the impression that the investment manager is terminating its business with the particular Plan or altogether. Although we agree that the occurrence of a disqualifying event is a relevant factor that a fiduciary must consider in determining whether to terminate its relationship with a QPAM, we do not believe that any and all disqualifying events necessitate that outcome, especially given the potential lack of any nexus between a disqualifying event and the QPAM and its personnel. Therefore, we would encourage the Department to consider another term or label for the one-year period following the ineligibility date and clarify that even after the one-year period ends, an investment manager can still rely upon a different exemption to transact on behalf of the same Plan and plan asset fund.

The Proposal also prohibits QPAMs from engaging in "new transactions" in reliance on the QPAM Exemption for existing plan asset funds after a QPAM's ineligibility date.[19] It is unclear, however, what "new transactions" means for QPAMs during the wind-down period. A QPAM may interpret the "new transaction" prohibition to mean it cannot sell any security for an existing plan asset fund, or, alternatively, it can sell but not buy new securities. This leaves the open question whether a QPAM can, for example, close out a short position or roll a hedge. It also does not appear to preclude a QPAM from engaging in new transactions in reliance on another exemption during the wind-down period. The Department should clarify the "new transactions" prohibition during the one-year wind-down period.

[17] *Id.* at 45209.
[18] *Id.*
[19] *Id.* at 45211.

5. The Department should permit the use of certain withdrawal-related provisions during a QPAM's wind-down period.

The Proposal would prohibit a QPAM from (i) restricting a client's ability to terminate or withdraw from their arrangement and (ii) withholding expenses and other similar items from an investor upon withdrawal, in each case in the event of a criminal conviction or after the QPAM receives an ineligibility notice.[20] These provisions would harm investors by creating a race for the exits and by inappropriately shifting expenses and other similar items from withdrawing investors to remaining investors (as outlined above). The Proposal should therefore be amended to permit QPAMs to enforce withdrawal-related provisions that have been disclosed in advance to investors in the applicable fund or other vehicle (e.g., specified withdrawal dates, withdrawal notice periods, suspension/delay provisions and more).

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[20] *Id.* at 45212.