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DOL Proposes Amendments to QPAM Exemption

by William D. Jewett on July 27, 2022

On July 27, 2022, the Department of Labor (DOL) proposed a set of amendments to Prohibited Transaction Class Exemption 84-14, the so-called "QPAM Exemption," which permits an investment fund[1] holding assets of ERISA plans and IRAs that is managed by a Qualified Professional Asset Manager ("QPAM") to engage in transactions with parties in interest to those plans or IRAs, subject to certain conditions. Without an exemption, these transactions generally would be prohibited by ERISA and the Internal Revenue Code.

The primary aim of the amendments is to tighten up the conditions which prevent QPAMs that have engaged in certain bad acts from being able to rely on the exemption and to establish procedures that apply when a QPAM is disqualified. However, several of the proposed amendments are unrelated to this aim and would make substantial changes to other aspects of the exemption. These proposed amendments will affect every QPAM, not just QPAMs that have (or whose affiliates have) engaged in bad acts. This post describes the changes affecting all QPAMs, leaving it for others to discuss the proposed rules that would affect QPAMs subject to disqualification for bad conduct.

The leading change of general applicability is an evergreen update to the financial requirements for being a QPAM. Currently, a QPAM generally must have at least $85,000,000 in assets under management as of the last day of its most recent fiscal year and at least $1,000,000 in equity capital shown on its most recent balance sheet prepared within the past two years. The proposed amendments would move to the following thresholds, reflecting changes in the Consumer Price Index:

- $135,870,000 in assets under management
- $2,720,000 in equity capital for banks, savings and loans, and insurance companies
- $2,040,000 in equity capital for registered investment advisers and broker-dealers

The proposed amendments call for adjusting these thresholds for inflation by January 31 of each year. Since these tests look back to the most recent fiscal year end and the most recent balance sheet prepared in the past two years, a QPAM that is close to one of the thresholds may have to project the dollar threshold it will need to satisfy once the next year's update takes effect. Smaller QPAMs with lower amounts of equity capital will have to shore up their capital structures and may have to do so each year on an ongoing basis.

[1] For purposes of the exemption, an "investment fund" includes 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 subject to discretionary authority of the QPAM.

The proposal also includes new document-related requirements. One is that every QPAM will have to send a one-time notice to the DOL of its intent to rely on the QPAM Exemption. (The DOL says that it intends to keep a current list of QPAMs on its public website.) While this requirement is not especially burdensome, it is a notable change from the status quo, and it will call for some vigilance, for example if a QPAM changes its legal or operating name.

A somewhat more burdensome change would require a QPAM intending to rely on the exemption to include in its written management agreements certain protections that would be triggered if the QPAM is disqualified from serving as a QPAM. These protections include (1) a notice that a client plan's ability to withdraw from the arrangement will not be restricted, and (2) an indemnification against losses and costs resulting from a failure of the QPAM to remain eligible to rely on the QPAM Exemption. This change, if finalized as proposed, would require an amendment to every investment management agreement a QPAM has with any client whose assets are considered "plan assets," including, presumably, agreements relating to the management of collective investment vehicles whose assets are treated as plan assets and which may not currently allow unrestricted withdrawals.

One set of wording changes that stands out from other more technical and clerical amendments is a provision that would permit use of the QPAM Exemption "only in connection with an Investment Fund that is established primarily for investment purposes." This language appears as an addition to Part I(c), which imposes a requirement that the terms of the transaction in question be negotiated by or under the authority and general direction of the QPAM, and that the QPAM make the decision to enter into the transaction. (This provision is generally thought of as prohibiting reliance on the exemption by a "rent-a-QPAM" whose sole function is to bless a transaction already negotiated.) The purpose of the new "established primarily for investment purposes" requirement is somewhat obscure, but a footnote explains that "the QPAM Exemption is unavailable if a plan sponsor hires a QPAM to engage a plan in transactions that do not include an investment component, such as hiring a party in interest service provider for a welfare plan." It is not obvious that anyone thought the QPAM Exemption could be used for this purpose, and it is worth considering whether the cure for this possibly non-existent confusion could create unanticipated problems in confirming whether the investment fund being managed by the QPAM was "established primarily for investment purposes." In a case where the account in question is the entire trust formed to fund benefits under a qualified retirement plan – for example, in the case of a QPAM appointed in connection with a derivatives agreement – it seems questionable whether that "investment fund" was established primarily for investment purposes.

Finally, the proposed amendments would add a recordkeeping requirement to the QPAM Exemption, requiring QPAMs to maintain records for six years sufficient to demonstrate compliance with the exemption. QPAMs would be required to make such records available to the DOL and other regulators, plan fiduciaries, and participants and beneficiaries of any plan or IRA invested in an investment fund managed by the QPAM.

In addition to these changes of general applicability, the proposed amendments would make many far-reaching changes to the QPAM Exemption's disqualification provisions. Others will doubtless debate those new protections for the duration of the 60-day comment period. The take-away from this post is that the proposed changes (which would take effect 60 days after publication of the final amendment) are by no means limited to QPAMs affected by the disqualification provisions. If you have questions regarding any of the changes described in this post, or any other aspect of the proposed amendments, please contact any member of Verrill's Employee Benefits & Executive Compensation Group.

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