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THE FINAL AMENDMENT TO THE QPAM EXEMPTION (THE "FINAL AMENDMENT")

The U.S. Employee Retirement Income Security Act of 1974 (**"ERISA"**) and the U.S. Internal Revenue Code of 1986 (the "**Code**") prohibit typical commercial transactions, such as sales, purchases, leases, loans and services, between "**Plans**"[1] and their "**Parties in Interest**"[2] in order to prevent potential abuse and unfair dealings. However, there are exemptions that may allow for such transactions to proceed under certain, specific conditions. One prominent exemption is Prohibited Transaction Class Exemption 84-14, commonly known as the "**QPAM Exemption.**" Under the QPAM Exemption, investment funds that are treated as the assets of Plans can engage in most commercial transactions with their Parties in Interest that would otherwise be per se prohibited, provided that the transactions are overseen and managed by sophisticated independent fiduciaries known as "qualified professional asset managers" ("**QPAMs**").

The final amendment (the "**Amendment**") to the QPAM Exemption, published in the Federal Register on April 3, 2024, will significantly affect registered investment advisers, banks and insurance companies that manage funds that include the assets of Plans. After the Amendment becomes effective on June 17, 2024 (the "**Effective Date**"), three possible results are expected: (1) there will be fewer managers willing or able to act as QPAMs over time; (2) managers will need to meet new requirements on an ongoing basis in order to rely on the QPAM Exemption in their routine transactions with the assets of Plans that they manage;

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[1] As defined in section 3(3) of ERISA, an "employee benefit plan" would include any plan, fund, or program established or maintained by an employer and/or an employee organization that (i) provides retirement income for employees or otherwise results in a deferral of income by employees for periods extending to the termination of covered employment or beyond or (ii) is maintained for the purpose of providing its participants or their beneficiaries with medical benefits, vacation benefits, or benefits in the event of sickness, accident, disability, death or unemployment. The issues described in this alert relate to employee benefit plans that are subject to the fiduciary conduct requirements and the prohibited transaction prohibitions of Part 4 of Subtitle B of Title I of ERISA. The term Plan is limited here to those plans that are subject to Part 4 of Subtitle B of Title I of ERISA. As defined in section 4975(e)(1) of the Code, a "plan" would include (i) a trust created or organized in the United States that forms part of a tax-qualified stock bonus, pension, or profit-sharing plan described in section 401(a) of the Code (including a plan covering only self-employed individuals) and which is exempt from taxation under section 501(a) of the Code, (ii) an individual retirement account ("**IRA**") or Roth IRA described in section 408(a) or section 408A of the Code and (iii) a heath savings account described in section 233(d) of the Code ("**HSA**").

[2] Parties in Interest means "parties in interest" under section 3(14) of ERISA and "disqualified persons" under section 4975(e)(2) of the Code.

and (3) managers and counterparties to Plans may choose to rely on other prohibited transaction exemptions to cover their routine, commercial transactions when the opportunities present themselves.

Important: The changes to the QPAM Exemption do not change when an investment fund is determined to hold the assets of Plans (e.g., the 25% test mechanics are not changing), and the Amendment does not otherwise change the fiduciary standards of conduct that apply when one is managing an investment fund that holds such assets of Plans.

MANAGERS MUST PROVIDE A ONE-TIME NOTICE TO THE DOL IN ORDER TO USE THE QPAM EXEMPTION

An entity seeking to qualify or remain and act or continue acting as a QPAM must provide a one-time notice to the U.S. Department of Labor (the "**DOL**") within ninety (90) calendar days following its reliance on the exemption or a change to its legal or operating name. An entity that has been relying on the QPAM Exemption as of the Effective Date and that wishes to continue to rely on the QPAM Exemption must email the DOL (QPAM@dol.gov) no later than September 15, 2024. There will be a website available to the public that will list such entities that have notified the DOL that they qualify as a QPAM. A manager's failure to timely notify the DOL of its reliance on the QPAM Exemption will make the QPAM Exemption unavailable to that manager.

MANAGERS THAT BECOME INELIGIBLE TO REMAIN QPAMS MUST INDEMNIFY THEIR PLAN CLIENTS

The Amendment provides a one (1) year winding down period (the "**Transition Period**") following the manager's ineligibility in order to help Plans avoid or minimize the disruption that can arise from terminating or switching managers or adjusting asset management arrangements when a QPAM becomes ineligible pursuant to Section I(g) and to give QPAMs a reasonable period to seek an individual prohibited transaction exemption from the DOL.

QPAMs do not need to amend their existing written management agreements ("**WMAs**") to provide their Plan clients with special indemnification provisions (as had been required in the previous proposal). However, any manager that becomes ineligible to remain a QPAM and is required to wind down its QPAM business during the Transition Period must provide written indemnifications to Plan clients relating to losses arising from the manager's wind down of its QPAM business.

THE CIRCUMSTANCES THAT MAY LEAD TO QPAM INELIGIBILITY HAVE EXPANDED

The Amendment outlines new pathways for managers to lose eligibility as QPAMs. Engaging in one of five types of "**Prohibited Misconduct**," as defined in Section VI(s) and VI(t), by any of the QPAM, its affiliates or any owner, direct or indirect, of a five (5) percent or more interest in the QPAM (collectively, the "**QPAM or its affiliates**"), or even simply endorsing or failing to prevent such behavior, will lead to disqualification, as a criminal conviction would, as detailed below. Prohibited Misconduct includes entry into a domestic non-prosecution agreement ("**NPA**") or a deferred prosecution agreement ("**DPA**") in the United

States where the underlying conduct would have constituted a crime that would have otherwise triggered QPAM ineligibility.

The Amendment also treats a substantially equivalent foreign criminal conviction of any of the QPAM or its affiliates like a domestic criminal conviction of any of the QPAM or its affiliates that would render the manager ineligible to use the QPAM Exemption. Excluded from this rule are foreign criminal convictions issued by certain countries listed as “foreign adversaries” by the U.S. Department of Commerce.

While the signing of a domestic NPA or a DPA by any of the QPAM or its affiliates would similarly render a manager ineligible to use the QPAM Exemption, such ineligibility is limited to domestic NPAs and DPAs only.

Participation in a Prohibited Misconduct or the signing of a domestic or substantially equivalent foreign NPA or DPA requires the QPAM to notify the DOL.

THE AMENDMENT CLARIFIES A QPAM'S REQUIRED AUTHORITY OVER INVESTMENT DECISIONS

The Amendment stresses that a QPAM relying on the QPAM Exemption cannot simply act as an independent transaction approver. Instead, the QPAM must possess and exercise sole discretion over the terms of the transaction, commitments and investments, as well as any associated negotiations.

RATCHETING OF SHAREHOLDER CAPITAL AND ASSETS UNDER MANAGEMENT

QPAMs must satisfy minimum equity and assets under management requirements. The Amendment increases those thresholds to reflect the baseline change in the Consumer Price Index. Increases in the threshold will be effective as of the last day of the QPAM’s fiscal year in which the increase takes effect. The thresholds are increased as follows:

- **Effective for the fiscal year ending December 31, 2024:**

  $101,956,000 of assets under management and $1,346,000 of shareholders' or partners' equity

- **Effective for the fiscal year ending December 31, 2027:**

  $118,912,000 of assets under management and $1,694,000 of shareholders' or partners' equity

- **Effective for the fiscal year ending December 31, 2030**:

  $135,868,000 of assets under management and $2,040,000 of shareholders' or partners' equity

The DOL will update the equity and asset management thresholds every year for inflation, rounding them to the closest $10,000. The updated thresholds will be published in the Federal Register by January 31st of each year.

QPAMS MUST SATISFY NEW RECORDKEEPING REQUIREMENTS

The Amendment requires that QPAMs keep records for six (6) years demonstrating that they satisfy the QPAM Exemption. QPAMs should keep records starting from the date of a transaction with respect to which a manager relied on the QPAM Exemption. QPAMs cannot seek relief for a transaction if they do not keep the necessary records for that transaction. The records must be made available for examination by certain parties, including the DOL and Plan fiduciaries. Those QPAMs who have undergone independent audits (as are required for in-house QPAMs) may be well placed to meet the recordkeeping requirement.

MANAGERS SHOULD BE CAUTIOUS WITH SIDE LETTER PROVISIONS INVOLVING THE QPAM EXEMPTION

A manager who operates an investment fund subject to the "25% test"[3] and who has promised through side letters to accept appointment as a QPAM if the investment fund it manages is determined to hold the assets of Plans must consider whether they can or will be able to accept such an appointment after the Effective Date.

ALTERNATIVES TO THE QPAM EXEMPTION

The DOL clarifies that the QPAM Exemption is unique and an expression of a person's or entity's status as a worthy fiduciary of a Plan. If a manager relying on the QPAM Exemption becomes ineligible and can no longer rely on it, the manager should discuss with its advisors strategies for managing the assets of Plans without the QPAM Exemption.

[3] Under the 25% test, an entity will not be subject to ERISA if Plans own less than 25% of each class of equity interests. For purposes of conducting the 25% test, the value of any equity interests held by a person or entity (other than a Plan) that has discretionary authority or control, or that provides investment advice for a fee (directly or indirectly), with respect to the assets of the entity or any affiliate of such a person or entity is disregarded.

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