U.S. ERISA QPAM Exemption

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Avoiding Prohibited Transactions

- An investment adviser or manager, as an ERISA Plan Fiduciary, acting on behalf of a plan or IRA must be careful to avoid a prohibited transaction under ERISA section 406.[1]

- The ERISA prohibited transaction rules prohibit a number of transactions between a plan and a "party in interest" unless an exemption is available.[2]

- A party in interest includes a fiduciary and any person providing services to the plan.

[1] There are parallel prohibited transaction rules under the Internal Revenue Code. This discussion refers to only the ERISA citations.

[2] See U.S. ERISA Prohibited Transactions for a list of who is a "party in interest" under ERISA section 3(14) and a list of "prohibited transactions" under ERISA section 406.

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Prohibited Transaction Exemptions

- There are three types of prohibited transaction exemptions available:
  - Individual exemption
  - Class exemption
  - Statutory exemption
- The QPAM Exemption is a class exemption (PTCE 84-14).[1]

[1] PTCE 84-14 has been amended many times since 1984. The current requirements are discussed in this section.

What is a QPAM

- "QPAM" is a qualified professional asset manager.[1]

- PTCE 84-14 is the main class exemption relied upon by investment advisers and managers to conduct business on behalf of a plan or IRA.

- Although it does not eliminate all investment restrictions, meeting the QPAM requirements substantially reduces the number of restrictions.

[1] This discussion does not cover the In-House Asset Manager ("INHAM") Exemption issued in 1996.

QPAM Exemption

- A QPAM may enter into a transaction that would normally be prohibited under ERISA section 406(a) such as:
  - Loans and extensions of credit
  - Leases
  - Provision of services between a plan and a party in interest
- A QPAM is not a shield, however, for ERISA section 406(b) which involve a breach of fiduciary duties.

QPAM Exemption

- Under PTCE 84-14, as amended, a QPAM must meet the following requirements:[1]

  – The QPAM must be a bank, savings and loan or insurance company with equity capital or net worth in excess of $1 million or a registered investment adviser with assets under discretionary management in excess of $85 million and equity in excess of $1 million.

  – The counterparty must not be the QPAM or related to the QPAM or to the fiduciary that appointed the QPAM (i.e., decided to invest in the fund).

  – The asset manager must represent in writing to the client that it is acting as a fiduciary.

  – The QPAM must negotiate the terms of the transaction and decide on behalf of the plan whether to engage in the transaction.

  – The QPAM may not have been convicted of certain activities that could bear on financial trust.

[1] A QPAM must undergo an annual compliance audit with respect to its investment activities to maintain QPAM status.

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QPAM Transaction

- Under PTCE 84-14, as amended, a QPAM transaction must satisfy the following conditions:
  - Assets of a plan entering into a transaction (and related plans) may make up no more than 20% of all assets managed by the QPAM.
  - The terms and conditions of the transaction must be at least as favorable to the plan as are available in an arm's length transaction.
  - Neither the counterparty nor any affiliate may, at the time of the transaction, have the power to appoint or terminate the QPAM as manager of the plan assets involved in the transaction or negotiate on behalf of the plan the terms of the QPAM's management agreement.[1]

[1] This effectively excludes transactions with the sponsoring employer or its affiliates.

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QPAM Exemption

- Under QPAM Exemption, extensive relief is provided for an investment manager of a plan assets look-through hedge fund re:
  - Acquisition of securities on margin.
  - Short sale transactions.
  - Entering into SWAPS.
- Under QPAM Exemption, the investment manager of a plan assets look-through hedge fund may enter into trades with a broker-dealer who is a service provider (e.g., provides execution services) to a benefit plan investor of the fund.