

August 2005

DOL Finalizes Changes To QPAM Exemption

The U.S. Department of Labor (DOL) recently announced that it has adopted amendments to Prohibited Transaction Class Exemption (PTE) 84-14, the "QPAM" Exemption. The QPAM Exemption permits certain transactions between employee benefit plans and parties in interest that would otherwise be prohibited by ERISA or the Internal Revenue Code, provided that the transaction is entered into at the direction of a "qualified professional asset manager" - the QPAM. The amendments affect both the definition of QPAM, as well as the transactions covered by the Exemption. The amendments are substantially similar to those proposed in September 2003 and, except as specifically stated below, are effective August 23, 2005:

Who Can Act as a QPAM?

Definition of QPAM: In general, a QPAM must be a bank, insurance company or registered investment adviser that satisfies certain threshold requirements regarding total client assets under management and stockholder's or partner's equity. The requirements for a registered investment adviser have been changed in two important respects:

- ♦ Effective as of the last day of the adviser's first fiscal year beginning on or after August 23, 2005 (December 31, 2006, for advisers with a calendar year end), the thresholds for total client assets under management and stockholder's or partner's equity increase from \$50,000,000 and \$750,000, respectively, to \$85,000,000 and \$1,000,000, respectively, to adjust (according to the DOL) for inflation since 1982 when the QPAM Exemption was initially proposed.
- ♦ The DOL has clarified that the determination of QPAM status as of the "last day of [the adviser's] most recent fiscal year" applies only to the total client assets under management requirement and not to the equity requirement. Therefore, an adviser that has the requisite total client assets under management as of its last fiscal year, but does not have the requisite equity, can become a QPAM immediately upon adding to its equity.

Independence Requirement: In addition, the DOL has clarified, or added a new requirement, depending upon your viewpoint, that a QPAM must be *independent* of the sponsoring employer whose plan's assets it manages. In other words, a manager cannot be a QPAM with respect to its own plan or the plan of an affiliate. Because of the many comments from managers who, often on the advice of counsel, believed that they could be the QPAM for their own plans, this new requirement will not apply until such time as the DOL has granted a final amendment to the QPAM exemption that permits financial service entities to act as their own QPAM. In this regard, concurrent with the publication of the final amendment discussed herein, the DOL published a proposed amendment that would grant such an exemption provided certain additional conditions, including the adoption of written policies and procedures designed to assure compliance with the new provisions and an annual exemption audit conducted by an independent auditor (similar to that required under the In-House Investment Manager, or "Inham" Exemption), are satisfied.

Conditions for QPAM Availability

The DOL has also made three changes to the general condition that the transaction cannot be with a party in interest that has the power to appoint the QPAM, each of which will provide greater flexibility:

- ♦ **Deletion of One-year Look Back Rule.** The DOL deleted the one-year look back rule contained in Part I of the QPAM Exemption that provided that the Exemption did not apply to a transaction with a party in interest who has, or, within the prior one-year period had exercised, the power of appointment over the QPAM. Only the appointment authority of the party in interest at the time of the transaction is now relevant.
- ♦ **Only Assets Involved in Transaction Referred To.** In addition, with respect to the power of appointment rule, the DOL has clarified that the power of appointment refers only to the power to appoint the QPAM with respect to the assets involved in the transaction, and not with respect to any of the plan's assets.

- ◆ **Transactions with Party who has Power of Appointment Permitted in Commingled Funds.** Finally, the DOL has broadened the availability of the Exemption to cover transactions with a party in interest to a plan that invests in a commingled fund *even if the party has the authority to redeem or acquire units in the fund*, provided the plan's interest in the fund, together with the interests of any other "related" plans, represents less than 10% of the total fund assets.

When is a Person an "Affiliate" or Related to a QPAM?

In general, the QPAM Exemption does not permit transactions with certain parties in interest who (i) have, or are affiliates of the party who has, the power to appoint the QPAM; (ii) are a sponsoring employer or one of its "affiliates" or (iii) are the QPAM or a party related to it. The DOL made significant revisions to the definitions of "affiliate" and "related". In general, these changes will cause fewer persons to be "affiliates" or "related" to a QPAM.

- ◆ **Affiliate.** The definition of an "affiliate" has been revised in two respects: (i) to delete those partnerships in which the sponsoring employer has less than a 10% interest (rather than 5% as previously was the rule), but only for purposes of whether an affiliate has the power of appointment, and (ii) to deem only highly compensated employees, and not all employees, as affiliates. For this purpose, the Internal Revenue Code definition of highly compensated employee is used, under which an employee is considered highly compensated in 2005 if the employee earned \$90,000 or more in 2004.
- ◆ **Related.** The definition of "related" with respect to a QPAM has also been revised in several respects. The determination of who is "related" to the QPAM is now to be made on the last day of each calendar quarter for the upcoming quarter, thereby allowing determinations to be made four times a year rather than every time there is a transaction. In addition, the original requirement that a QPAM and a party in interest be treated as related if either owned a 5% or more interest in the other has been revised to reflect the growing trend towards consolidation in the financial services industry. If the QPAM owns a 10% or more interest in a party in interest or if the party in interest owns a 10% or more interest in the QPAM, they are related. Furthermore, if a person controlling or controlled by the QPAM owns a 20% interest in the party in interest or a person controlling or controlled by the party in interest owns a 20% interest in the QPAM, they are related. In this latter case, however, if the interest is less than 20%, but more than 10% and the controlling party actually exercises control over the management or policies of the other party by reason of the ownership interest, the parties will be related.

In general, the DOL's revisions to the QPAM Exemption responded to various concerns raised by managers and their advisers and broadens the scope of the QPAM Exemption. *If you have any questions concerning how the changes may impact your business or the investment management relationship between QPAMs and ERISA clients, please contact Hannah Widlus at (312) 781-8656 or hwidlus@seyfarth.com, Joel Rubin at (312) 781-8600 or jrubin@seyfarth.com, or the Seyfarth Shaw LLP attorney with whom you work.*

ATLANTA

One Peachtree Pointe
1545 Peachtree Street, N.E., Suite 700
Atlanta, Georgia 30309-2401
404-885-1500
404-892-7056 fax

BOSTON

Two Seaport Lane, Suite 300
Boston, Massachusetts 02210-2028
617-946-4800
617-946-4801 fax

CHICAGO

55 East Monroe Street, Suite 4200
Chicago, Illinois 60603-5803
312-346-8000
312-269-8869 fax

HOUSTON

700 Louisiana Street, Suite 3700
Houston, Texas 77002-2797
713-225-2300
713-225-2340 fax

LOS ANGELES

One Century Plaza
2029 Century Park East, Suite 3300
Los Angeles, California 90067-3063
310-277-7200
310-201-5219 fax

NEW YORK

1270 Avenue of the Americas, Suite 2500
New York, New York 10020-1801
212-218-5500
212-218-5526 fax

SACRAMENTO

400 Capitol Mall, Suite 2350
Sacramento, California 95814-4428
916-448-0159
916-558-4839 fax

SAN FRANCISCO

560 Mission Street, Suite 3100
San Francisco, California 94105
415-397-2823
415-397-8549 fax

WASHINGTON, D.C.

815 Connecticut Avenue, N.W., Suite 500
Washington, D.C. 20006-4004
202-463-2400
202-828-5393 fax

BRUSSELS

Boulevard du Souverain 280
1160 Brussels, Belgium
(32)(2)647.60.25
(32)(2)640.70.71 fax

This newsletter is a periodical publication of Seyfarth Shaw LLP and should not be construed as legal advice or a legal opinion on any specific facts or circumstances. The contents are intended for general information purposes only, and you are urged to consult a lawyer concerning your own situation and any specific legal questions you may have. For further information about these contents, please contact the firm's Employee Benefits Practice Group.