

MEMO# 34081

March 21, 2022

DOL Adopts Amendments to Several Class Exemptions to Remove Credit Rating References

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TO: ICI Members

Pension Committee

Pension Operations Advisory Committee SUBJECTS: Pension RE: DOL Adopts Amendments to Several Class Exemptions to Remove Credit Rating References

The Department of Labor (DOL) recently finalized amendments to six prohibited transaction exemptions (PTEs) to remove references to credit ratings pursuant to the requirements of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank).[\[1\]](#) Section 939A of Dodd-Frank requires each federal agency to review any regulation it issued that requires the use of an assessment of the credit-worthiness of a security or money market instrument, modify such regulation to remove any reference to or requirement of reliance on credit ratings, and substitute in such regulations a standard of credit-worthiness as each respective agency deems appropriate.

Proposed Amendments

DOL proposed these amendments in 2013 and reopened the comment period last year.[\[2\]](#) ICI submitted a comment letter in 2013, noting that DOL had based some of its changes on similar changes that the SEC had proposed but had not yet finalized.[\[3\]](#) ICI's letter urged DOL to await issuance of final rules from the SEC before finalizing the amendments. The SEC has since finalized its amendments Dodd-Frank amendments to rules 2a-7 and 5b-3.[\[4\]](#)

Final Amendments

DOL is adopting the amendments as proposed, with minor changes to address comments it received and changes the SEC made in finalizing its Dodd-Frank amendments. The amendments go into effect on May 9, 2022.

Of the six PTEs amended, the following three may be of interest to ICI members.[\[5\]](#)

PTE 75-1

PTE 75-1 provides relief from ERISA's prohibited transaction provisions for certain

transactions between plans and broker-dealers or banks if certain conditions are met. Included among the covered transactions are (1) a plan's acquisition of securities during the existence of an underwriting syndicate, from a person other than a plan fiduciary, where a plan fiduciary or its affiliate is a member of the underwriting syndicate, and (2) a plan's purchase or sale of securities from or to a "market maker" with respect to such securities who is also a plan fiduciary. Among the required conditions for each of the above two types of transaction is a requirement that the issuer of the securities (including any predecessors) must have been in continuous operation for not less than three years. However, DOL included several exceptions to this requirement, including an exception for securities that are non-convertible debt securities rated in one of the four highest rating categories by at least one nationally recognized statistical rating organization.

DOL's amendment replaces the credit rating reference in this exception to require that "[a]t the time of acquisition, such securities are nonconvertible debt securities that are (i) subject to no greater than moderate credit risk and (ii) sufficiently liquid that such securities can be sold at or near their fair market value within a reasonably short period of time."

PTE 97-41

PTE 97-41 provides relief from ERISA's prohibited transaction provisions for the purchase by a plan of shares of one or more mutual funds in exchange for the assets of the plan transferred in kind to the mutual fund from a collective investment fund ("CIF") maintained by a bank or plan adviser where such bank or plan adviser is a plan fiduciary and also the investment advisor to the mutual fund. Exemptive relief is conditioned upon a pro-rata division rule, which requires that the transferred assets must constitute the plan's pro rata portion of the assets that were held by the CIF immediately prior to the transfer. However, notwithstanding this rule, DOL provided that the allocation of fixed income securities held by a CIF among plans on the basis of each plan's pro rata share of the aggregate value of the securities will not fail to meet the pro rata division rule's requirement if (1) the aggregate value of such securities does not exceed one percent of the total value of the assets held by the CIF immediately prior to the transfer, and (2) such securities have the same coupon rate and maturity, and at the time of the transfer, the same credit ratings from nationally recognized statistical rating organizations.

The amendment replaces the existing credit rating reference with a requirement that such securities be of "the same credit quality." In preamble language, DOL notes that, in making a determination as to the credit quality of fixed income securities for purposes of this amended condition, a fiduciary should, to the extent possible, engage in credit quality comparisons using the same standards for each set of securities and may rely in this regard on reports and advice given by independent third parties, including ratings issued by ratings agencies.[\[6\]](#)

PTE 2006-16

PTE 2006-16 provides relief from ERISA's prohibited transaction provisions for the lending of securities that are plan assets to certain banks and broker-dealers that are parties in interest to the plan and for the payment to a fiduciary of compensation for services rendered in connection with securities lending, if certain conditions are met. One condition is the plan's receipt from the borrower, by the close of the lending fiduciary's business on the day in which the securities lent are delivered to the borrower, of either "U.S. Collateral" or "Foreign Collateral." Included within the definition of "Foreign Collateral" are "foreign

sovereign debt securities provided that at least one nationally recognized statistical rating organization has rated in one of its two highest categories either the issue, the issuer or guarantor."

The amendment modifies this provision as follows: "foreign sovereign debt securities that are (i) subject to a minimal amount of credit risk, and (ii) sufficiently liquid that such securities can be sold at or near their fair market value in the ordinary course of business within seven calendar days."

Also included within the definition of "Foreign Collateral" are "irrevocable letters of credit issued by a Foreign Bank, other than the borrower or an affiliate thereof, which has a counterparty rating of investment grade or better as determined by a nationally recognized statistical rating organization."

The amendment modifies this provision as follows: "irrevocable letters of credit issued by a Foreign Bank, other than the borrower or an affiliate thereof, provided that, at the time the letters of credit are issued, the Foreign Bank's ability to honor its commitments thereunder is subject to no greater than moderate credit risk."^[7]

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endnotes

^[1] The final amendments were published at 87 Fed. Reg. 12985 (March 8, 2022), available at <https://www.govinfo.gov/content/pkg/FR-2022-03-08/pdf/2022-04866.pdf>. DOL's news release on the amendments, dated March 7, 2022, is available at <https://www.dol.gov/newsroom/releases/ebsa/ebsa20220307>. For more detailed information on Dodd-Frank, see ICI Memorandum No. 24431 dated July 19, 2010, available at <https://www.ici.org/memo24431>.

^[2] For a summary of the proposed amendments, see ICI Memorandum No. 27367, dated July 10, 2013, available at <https://www.ici.org/memo27367>. DOL's announcement of an additional 45-day comment period was published at 86 Fed. Reg. 33360 (June 24, 2021), available at <https://www.govinfo.gov/content/pkg/FR-2021-06-24/pdf/2021-13149.pdf> ("This reopening of the comment period provides interested persons with the opportunity to submit additional comments on the proposed amendments due to the passage of time since the proposal was originally published in 2013.").

^[3] For an overview of ICI's comment letter in response to the proposed amendments, see ICI Memorandum No. 27478, dated August 20, 2013, available at <https://www.ici.org/memo27478>.

^[4] See ICI Memorandum No. 29357, dated September 18, 2015, available at <https://www.ici.org/memo29357>; and ICI Memorandum No. 27845, dated January 15, 2014, available at <https://www.ici.org/memo27845>.

[5] The remaining three PTEs DOL is amending are PTE 80-83 "Use of Proceeds from Sale of Securities to Reduce or Retire Indebtedness," PTE 81-8 "Short Term Investments," and 95-60 "Insurance Company General Accounts."

[6] 87 Fed. Reg. at 12991.

[7] As proposed, the amendment had included at the end of this subsection the phrase "with an adequate capacity for payment of principal and interest." In making this change, DOL notes that "[m]oderate credit risk would denote current low expectations of default risk, with an adequate capacity for payment of principal and interest." 87 Fed. Reg. at 12991.

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