Fiduciary Insurance and Fidelity Bond Coverage

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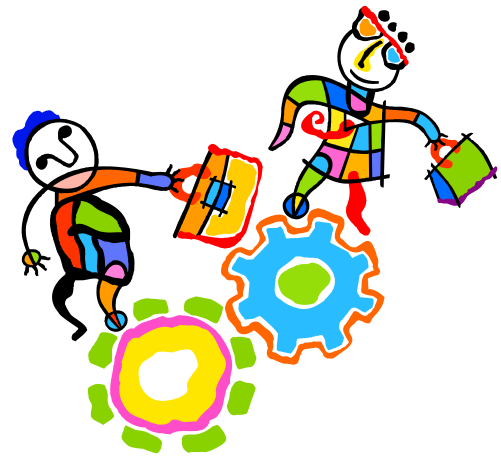
Plan administrators often ask me to explain to them the difference between a *fidelity bond,* which is required, and *fiduciary liability insurance*, which is optional. These coverages are not the same and it is important to understand the difference between them.

Fiduciary Liability Insurance: A fiduciary is anyone who has discretionary authority or control over the plan's assets. Plan fiduciaries can be sued by plan participants for failure to properly discharge their duties and the fiduciary can be held personally liable for any expenses related to the lawsuit. The costs must be paid out of personal assets, including their home or business. The plan's fidelity bond does not protect a fiduciary's personal assets and a retirement plan cannot relieve the fiduciary of responsibility with indemnification language. Employee benefits liability insurance normally only applies to claims arising from administrative errors and is usually subject to a single limit. However, fiduciary liability insurance can protect a fiduciary by providing coverage that will pay in the event of a legal liability caused by alleged errors or omissions or a breach of fiduciary duties, including such things as failure to file required reports, errors in computing eligibility, failure to make timely contributions, failure to keep plan documents up-to-date, and improper advice given to participants about their coverage. Fiduciary liability insurance is not required of any fiduciary. However, it is certainly a prudent purchase! When purchasing this type of protection, it is important to work with a provider that can explain the recourse/nonrecourse policy options, help determine the appropriate amount of coverage and the deductible amount, and counsel the fiduciary as to whether they want a policy that provides that the insurance company will have the right to select defense counsel or one that allows the insured to select their own counsel.



Fidelity Bond Coverage: A fidelity bond provides coverage for dishonest and/or fraudulent acts of employees in the course of handling plan money or securities. ERISA requires that every administrator, officer and employee of a plan who handles plan funds must be covered by this type of bond. "Handling" plan assets includes having physical contact with cash or checks, the power to transfer funds from the plan to a third party, and the authority to authorize disbursements and decision making responsibility with respect to the plan assets. The bond may list each person individually (a name schedule bond) or may

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provide coverage to all persons who handle the assets (a blanket bond). Each person must be bonded for at least 10% of the amount of the funds he handles, up to a maximum of $500,000 per plan (or $1,000,000 per plan if it holds employer stock). The minimum bond amount is $1,000. It is unlawful for any plan official to permit any other official to receive, handle, or exercise custody over plan funds if that person is not properly bonded. The cost of the bond may be paid from plan assets. The plan may be insured on its own bond or it may be insured through a rider on the employer's crime policy. The bond cannot have a deductible and may not exclude coverage in situations where the employer "knew or should have known" that a theft was likely.

Not all bond coverage is alike. Plan sponsors should review different options and see how they compare with respect to the scope of the coverage provided. The bond may only be obtained from a provider that is named on the Department of Treasury's listing of Approved Sureties. It is acceptable to issue a bond for a period longer than one-year, so long as the bond insures the plan for the statutorily-required amount. The bond does not have to specifically state the dollar amount of coverage, so long as it provides the required statutory amount of 10% of plan funds handled for each official. The bond may contain an "inflation guard" whereby the amount of the bond coverage automatically increases as the plan assets grow.