



Fiduciary Liability Insurance – General Overview SCTR Conference 2009

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What is Fiduciary Liability?

Fiduciary Liability Insurance is an insurance product designed to transfer risk for the financial protection of fiduciaries of employee benefit plans against legal and statutory liability arising out of their role as fiduciaries, including the cost of defending those claims that seek to establish such liability.

Who is a Fiduciary?

- Any person or entity who exercises discretionary authority with respect to the management of a plan or the disposition of its assets.
- Any person or entity who has discretionary authority or responsibility with respect to a plan.

Who will the policy cover?

- Fiduciaries with administrative duties to the plan/participants.
- Fiduciaries with a fiduciary duty to the plans.
- The Sponsor Organization
- The Plans

What will the Policy Cover?

- Administrative Error & Omission Claims.
- Breach of Fiduciary Duty claims.
- Benefit Claims (Defense Only) Policy will not cover actual benefits.

Definition of Fiduciary Duties

“Prudent Man rule”

To run the plan solely in the interest of the plan participants and for the exclusive purpose of providing benefits to plan participants.

To diversify assets so as to minimize loss.

To minimize the expense of administering the plan.

Defined Contribution Plans

- Defined Contribution plans are pension plans for which no set benefit is promised. Instead, the amount received at retirement is determined by how well the plan's investments perform over time and how much is contributed to the plan
- The fiduciaries have to provide information to the plan participants on a regular basis regarding each of the investments and/or any changes in the investments
- There is no specific promised benefit, the employer is generally relieved of meeting specific earnings targets and funding levels.
- The exposure from these plans is still great. Plan sponsors and fiduciaries have a duty to make prudent investment choices in these plans and continually monitor investment performance to defray the expenses associated with running the plans, to run the plans solely in the interest of the plan participants and to run the plans as a prudent expert would.

Defined Benefit Plans

- Under a traditional Defined Benefit Plan, the sponsor guarantees the pension benefits will be paid at retirement. These benefits are typically based on a percentage of a participant's last several years of employment, usually when income is at the highest level in the participant's career. This type of plan favors older, long term employees.
- Usually this plan is funded entirely by the sponsor organization, although occasionally employee contributions are required.
- Defined Benefit Plans are expensive for the sponsor. In addition to having to fund the plan, the sponsor also must retain an independent actuary to calculate contribution amounts and pay premiums to the Pension Benefit Guaranty Corp (PBGC), the governmental agency that oversees Defined Benefit Plans and guarantees pension payments in the event of the sponsor organization's and/or the plan's insolvency. In addition, the sponsor fully bares the investment risk of the plan.
- For these reasons, many sponsor organizations are terminating these plans and replacing them with 401K plans, or converting the plans to cash balance arrangements.

Welfare/Health Plans

- Vision Care
- Vacation
- Medical, Dental, Life, Disability
- Training
- Tuition Reimbursement
- Alcohol and Drug abuse programs
- Eldercare Services/Children Services

Standard Exclusions

- Profit or Advantaged Exclusion
- Fraud Exclusion
- Discrimination Exclusion
- Interrelated Acts Exclusion
- P&P Litigation Exclusion
- Failure to Collect
- Bodily Injury/Property Damage (does not apply to defense cost for breach of duty)
- Pollution Exclusion with Pollutants Defined
- Exclusion for claims related to an insured's capacity as fiduciary or administrator of any plan other than a plan covered under the policy

Claims Examples for Defined Benefit Plans:

- Miscalculation of Benefits
- Reversion of assets
- Failure to diversify investments
- Failure to choose prudent investments
- Failure to fund/make contributions
- Failure to monitor investments

Claims Examples for Defined Contribution Plans:

- Failure to timely distribute assets
- Failure to choose/offer prudent investments
- Failure to monitor investment performance
- Failure to diversify investments
- Failure of investments to perform as promised
- Failure to provide participants information
- Failure to take steps to stop/minimize loss
- Failure to timely deposit money in participant accounts

Insurance Market Conditions

- Diminished Industry Capital & Surplus
- Cat Property Losses in 2008
- Expected Write Down of Bonds
- Diminished Expectation for Investment Income
- Expectation of Diminished Underwriting Profit During Economic Downturn
- Rates up by 10% in 2009 – Property First Followed by Liability

Carriers Specializing in Large Public Entity Fiduciary Liability

- AIG
- Chubb
- Travelers
- Zurich
- XL – Greenwich
- ACE USA
- Philadelphia

Fiduciary Liability Industry Position

- Very few carriers underwrite line of business
- Limit capacity often restricted to \$10 - \$15 Billion
- Account size capacity often restricted
- Fiduciary Underwriting often part of Executive Risk, D&O and E&O Departments

Fiduciary Liability Market Conditions

- Subject to influence from deteriorating underwriting experience from Executive Risk, D&O and E&O marketplace.
- Fiduciary Underwriting Skeptical of Retirement System Deteriorating Funding Levels
- Harder Reinsurance Marketplace
- Subject to other market factors mentioned previously
- Anticipate moderate rate increases going forward for at least two years

THANK YOU!