

Fiduciary Liability Insurance for Trustees:

What Are You Missing?

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Anyone who is a trustee of a pension or employee benefit plan occupies an undeniable position of power. As a group, trustees are responsible for investing the plan assets and may do so by the unilateral exercise of their discretion. Relative to trustees, beneficiaries are in a fairly vulnerable position. By law, this vulnerability creates a fiduciary relationship between trustees and beneficiaries, and therefore trustees have a duty to act with utmost good faith, with the highest degree of honesty and in the best interest of plan beneficiaries according to Black's Law Dictionary, Eighth Edition. Naturally, trustees are therefore exposed to liability, by and large in the form of claims alleging a breach of fiduciary duty. Even when trustees act in strict compliance with their duties, there is the ever-present possibility that they may find themselves in the middle of a long and drawn-out litigation. Consequently, it has become commonplace that trustees have fiduciary liability insurance. However, coverage under these policies is not absolute and, unfortunately, many trustees are unaware of what their policies are missing.

Fiduciary liability insurance is insurance that is designed to protect trustees against claims for breaches of the duties imposed upon them as fiduciaries, by

statute, by the common law or by the terms of the trust agreement. Coverage under a policy generally entitles the insureds to recover any amount they become legally obligated to pay as a result of a claim; this often includes damages, judgments, settlements, interest and legal costs. Trustees should appreciate exactly what the policy covers and what it does not, in order to prevent a false sense of security.

As is the case with most legal documents, the manner in which fiduciary liability insurance policies are written can be confusing. However, it is in trustees' best interests to take the time to sit down with their insurance provider and their legal counsel to go over just what is covered and what they must do when faced with a claim.

Fiduciary liability insurance does not provide absolute coverage; in fact, all policies contain conditions that must be fulfilled before, during and after a claim is made so that losses can be recovered under the policy. To make matters worse, these conditions vary by insurance provider and may even vary within one provider from year to year. It is important therefore to keep up to date on any changes made to the policy. In addition, all policies include specific exemptions outlining which types of claims are not covered. In fact the average policy contains between nine and 19 exclusions. Although these exemptions differ from policy to policy, there are certain ones that tend to be included

in fiduciary liability insurance policies across the board. Some of these are described below.

Exemptions

Previous/Pending Claims and Disclosure

When purchasing fiduciary liability insurance, disclosure is key. Prior to purchasing insurance, trustees should advise their insurance provider of any existing claim or pending claim. Failure to do this will disqualify those undisclosed claims from being covered by the policy. This is intended to prevent trustees from buying insurance as a reaction to rumors of an impending claim, in hopes that they can slip the claim under the radar by not disclosing it to their provider. Furthermore, even if the claim is disclosed to the provider before signing the policy, the policy may not cover the claim. In addition, claims that have been disclosed to a previous insurance provider or under a previous insurance policy will usually be excluded from coverage.

Litigation can be unpredictable and costly; any particular claim can last for years in the judicial system, especially if it includes judicial review or an appeal.



Criminal or Fraudulent Acts or Omissions

If a claim is brought against a trustee that makes allegations of criminal or fraudulent behaviour and it is eventually found that the allegations are true, it is unlikely that a fiduciary liability insurance policy will cover any damages or legal costs arising from the claim. These policies are not designed to shield trustees from their illicit activities.

Illegal Remuneration or Advantage

For similar reasons, any claim that demonstrates that a trustee or board of trustees has obtained remuneration, profit or advantage to which they are not legally entitled will be excluded under the bounds of policy coverage. This would include claims alleging that trustees illegally ac-

cepted payments as an incentive to invest plan assets with a particular company.

Notice/Reporting Requirements

Under most fiduciary liability insurance policies, trustees must give written notice of any claim, together with full particulars of the claim "as soon as practicable" in order to recoup any losses under the policy. *As soon as practicable* is not defined in most policies and is therefore subject to judicial interpretation in the event coverage is denied on the basis that notice was not given soon enough. Furthermore, notice is required not only when a claim has been made, but also when a claim is pending. The effect of this clause of course is that any delay in disclosing pertinent information to the insurance provider could hinder the recovery of losses, such as damages and legal costs. Therefore, any claim or any threat of a claim should be disclosed to the insurer straightaway.

Nonmonetary Relief

Some policies exclude any claim requesting only non-monetary or injunctive relief. This means that claims asking for an order to prevent a board of trustees from doing some act, for instance, from investing the plan assets with a particular company, would not be covered by the policy. Given the amount of decision making required of boards of trustees, this exclusion could certainly leave a large gap in coverage under the policy.

Libel, Slander and Defamation

Claims arising from allegations of libel, slander or defamation of a person are typically excluded from coverage under fiduciary liability insurance policies.

Bodily Damage or Damage to Property

Additionally, claims relating to allegations of damage to person or property are generally also excluded under these policies.

Limit on Coverage

When considering purchasing fiduciary liability insurance, it is important that a proper risk assessment be conducted to determine the ideal amount of coverage required. Litigation can be unpredictable and costly; any particular claim can last for years in the judicial system, especially if it includes judicial review or an appeal. It is notable that under most fiduciary liability insurance policies, costs associated with defending the claim (e.g., legal fees) are part of, and not in addition to, the limit of coverage under the policy. So, for example, if a trustee has coverage for \$1 million under the policy and during the course of litigation the legal costs exceed this amount, the insurance company will not provide any more money to the trustee under the policy; the policy limit has been exhausted. Any litigation costs accrued thereafter, in addition to any damages that result from the claim, would therefore not be covered by the policy.

Third-Party Administrators

Additionally, if the board of trustees does not actually administer the pension or employee benefit plan itself and that responsibility has been delegated to a third party, it is imperative that the policy include a specific clause that provides for the coverage of the third-party administrators as well. Without the clause, any wrongful acts committed by the third-party administrator will not be covered by the policy.

The Good News

The good news is that fiduciary liability insurance policies can often be tailored to suit the needs of a particular trustee or board of trustees. This may allow trustees to amend or remove altogether some of the above-mentioned exclusions from their policy, thereby broadening the coverage and ultimately providing better protection to the trustees. This possibility should be discussed with the insurance provider.

Conclusion

The reality is that trustees of pension and employee benefit plans are exposed to liability. Fiduciary liability insurance is therefore an essential part of a multifaceted strategy designed to protect trustees. However, as evidenced by the exclusionary provisions discussed above, coverage under these policies is not absolute. Trustees therefore would be well advised to take the time to educate themselves about the exclusions of these complex policies.



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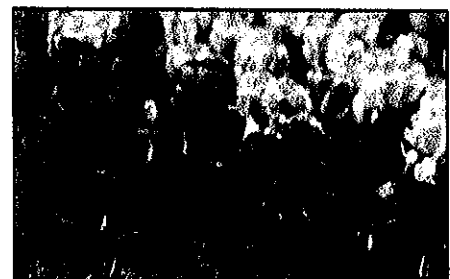
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