May 2016

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Mid-Atlantic

Construction Insider

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Important to Know the Difference!

ERISA Fidelity Bond and Fiduciary Liability Insurance

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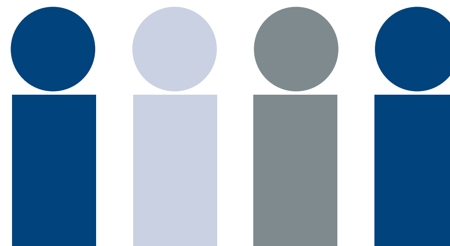
Managing plan fiduciaries' general obligations and responsibilities with regards to plan governance can be an intimidating task. Frequently important details slip through the cracks because of misunderstanding the requirements of ERISA or Department of Labor (DOL) regulations. There are some important terms that are often misunderstood but are integral to ERISA compliance. Let's take a look!

ERISA Fidelity Bond

ERISA requires all fiduciaries and any other individuals (referred to as plan officials) who handle plan assets to be covered by a fidelity bond. The purpose of the fidelity bond is to protect the plan from risk of loss due to acts of fraud, dishonesty or negligence by the individuals whose positions require them to come in direct contact with, or have control over, plan assets. Plan officials usually include the plan administrator, any officers or employees of the plan sponsor who handle plan funds, and service providers (if they perform functions ordinarily carried out by any of the above listed individuals).



Generally, plan officials have —

- Physical contact with cash, checks or other plan property;
- Authority to approve disbursement of funds, e.g. authorizing benefit payments;
- Authority to transfer or negotiate plan assets for a price, e.g. providing investment management services to the plan; and/or
- Supervisory or decision-making authority over any individual described above. (If a plan sponsor committee has the authority to authorize any of the above functions, the committee members are considered to be handling plan funds and must be bonded.)

Fidelity Bonds Must Satisfy Several Requirements

- The bond must be purchased and be in effect before any plan assets are handled.
- The bond must cover at least 10 percent of plan assets handled by the bonded individual(s) in the preceding year or $1,000, whichever is greater. Additional coverage may be required if the plan has non-qualifying assets. The maximum bond amount required is $500,000 ($1 million if the plan holds employer securities). The bond does not need to specify a dollar amount. Instead, it can provide for at least 10 percent of funds handled, with minimum coverage of $1,000. If there is no previous plan year information based on which to determine the cover-

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age needed, the amounts must be estimated using the prescribed procedures per ERISA.

- The bond must be placed with a surety or reinsurer that is named on the Department of Treasury's Listing of Approved Sureties, Department Circular 570.
- The bond term is typically one year. It can cover multiple years if it insures the plan for the required amount each year and the plan officials monitor the coverage to ensure it remains sufficient.
- The DOL regulations permit several forms of bonds, including individual, name schedule (covering several named individuals), position schedule (covering a list of positions), blanket (covering all officers and employees without a specific list identifying them), and a combination of forms.
- The plan can be insured on its own bond or can be added as a named insured to an existing employer bond or insurance policy, provided it is specifically named or otherwise identified on the bond in a way that would allow the plan's representatives to make a claim under the bond in the event of a loss due to fraud or dishonesty. If the plan sponsor maintains multiple plans, the named insured can be "all employee benefit plans sponsored by… ."
- Under the terms of the fidelity bond, the plan should be designated as the "loss payee" for any future claims.
- Plan sponsors must evaluate their bond coverage at the beginning of each subsequent plan year to ensure that the minimum bonding requirements are met.

It is important to note that unfunded employee benefit plans or plans not subject to Title I of ERISA are exempt from the bonding requirement.

> "Obtaining an ERISA fidelity bond is not optional: it is a requirement under ERISA."

Fiduciary Liability Insurance

Fiduciary liability insurance insures a plan and its fiduciaries and/or the plan sponsor against losses caused by breaches of fiduciary responsibilities. Obtaining such insurance is optional and not required by ERISA, but it is subject to ERISA's fiduciary standards which allow a plan to purchase the insurance and pay the premiums from plan assets if the policy permits recourse by the insurer against the fiduciary in the case of a fiduciary breach. The fiduciary liability insurance generally may be obtained from any properly qualified insurance broker.

Although it isn't required by ERISA, all plan officials should seriously consider obtaining fiduciary liability insurance as they are personally liable for losses incurred by a plan due to their breach of responsibility.

Difference Between Fidelity Bonding And Fiduciary Liability Insurance

The fidelity bond insures a plan (and its participants) against losses due to fraud or dishonesty by plan officials who handle plan assets. Fiduciary liability insurance, on the other hand, generally insures **the plan and/or the plan officials** against losses caused by breaches of fiduciary responsibilities.

Fiduciary Indemnification

Fiduciaries may also expect or request an assurance from the plan sponsor that they will be indemnified against personal liability. This is not covered by the fidelity bond nor by the fiduciary liability insurance. Indemnification of the fiduciaries means compensating them for certain losses incurred as a result of service in a fiduciary capacity.

Obtaining an ERISA fidelity bond is *not* optional: it is a requirement under ERISA. Although there are no specific penalties for failing to comply with the ERISA bonding requirements, it is considered a *breach of fiduciary responsibility or duty* for which the plan officials can be held personally liable. Plan sponsors should also consider purchasing fiduciary liability insurance and deciding whether the company will indemnify individuals who act as plan fiduciaries.

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