



Understanding Fiduciary Coverage

Presented by

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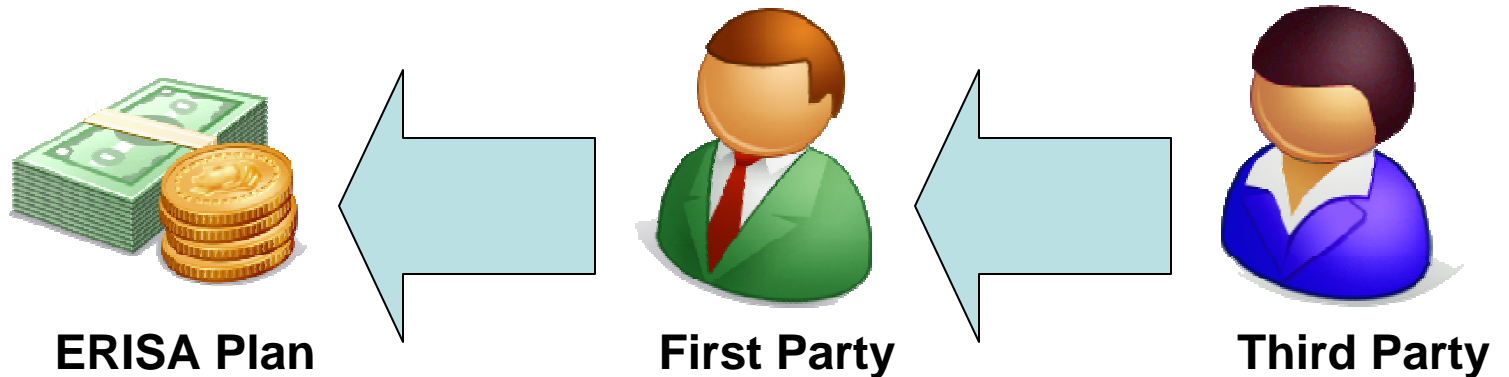
Recognized industry experts on the subject of investment
fiduciary responsibility

The screenshot shows the homepage of the fi360 website. The header features the 'fi360' logo on the left, a 'Resource Line: 1-866-656-8170' in the center, and a 'Login here...' dropdown menu on the right. Below the header is a navigation bar with the text 'YOUR GUIDE TO GLOBAL FIDUCIARY INSIGHTS' and a menu of links: 'About Us', 'Foundation for Fiduciary Studies', 'Center for Fiduciary Studies', 'Fiduciary Analytics', and 'Global Ventures'. A vertical sidebar on the left contains a menu with the following items: 'TRAINING', 'TOOLS', 'FIDUCIARY STORE', 'CEFEX CERTIFICATION', and 'ANNUAL CONFERENCE'. The main content area features a large photograph of a lighthouse on a grassy cliff overlooking the ocean. Overlaid on the bottom of the photograph is the quote: 'It is the set of the sails, not the direction of the wind that determines which way we will go' by Jim Rohn.

Overview

- Understanding the difference between First Party vs Third Party Coverages
- What Insurance products are available to Investment Advisers?
- What Insurance products are available to Plan Sponsors?
- Do I need to be bonded (ERISA)?

First Party vs Third Party



- Named plan fiduciaries, or anyone acting in the capacity as a fiduciary
- Direct relationship to the plan as an owner, employee, or trustee

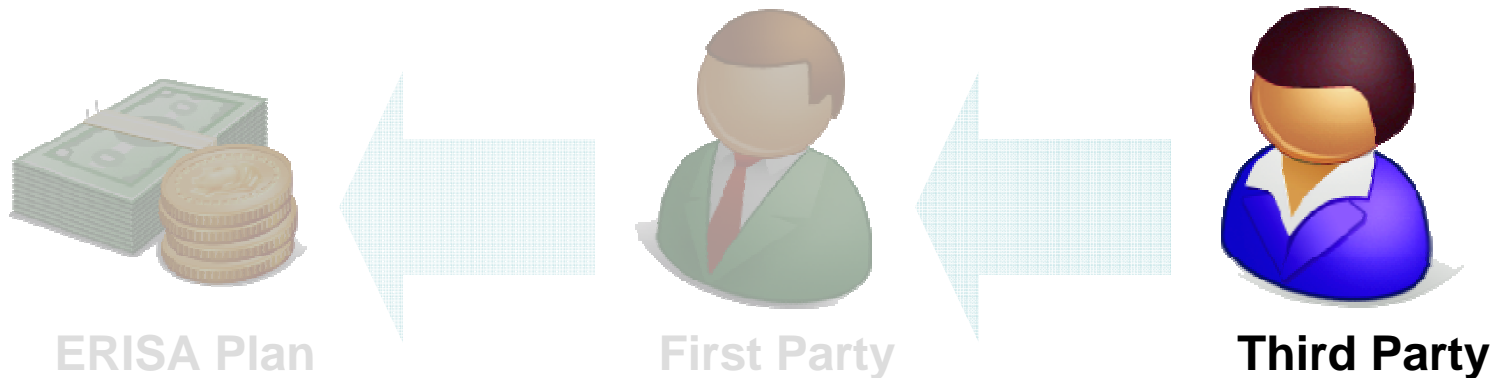
- Provide services to the First Party, Plan, and/or Trustees
- Investment Advisor, Plan Consultant, Third-party Administrator
- May still be acting in a “fiduciary” capacity

First Party Coverage

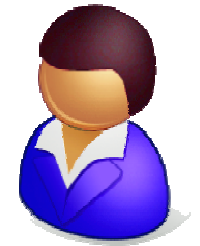


- **Fiduciary Insurance**
 - Protects plan fiduciaries for breach of fiduciary duties
- **ERISA Bond**
 - Protects plan assets from theft
- **Employee Dishonesty / Crime**
 - Protects company assets from theft

Third Party Coverage



- **Errors & Omissions Insurance**
 - Protects professional for errors and/or omissions in their professional services rendered
- **Investment Advisor ERISA Bond**
 - Protects your client's plan assets from theft by you or your employees



Third Party

Investment Advisers Professional Liability



Understanding Insurance

- 90% of the calls NAPLIA receives from Investment Advisers are requests for information about “Fiduciary Insurance”
- What you need is Errors & Omissions for acts as a Fiduciary for your clients.

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If you believe your investment advisor breached his or her fiduciary duty to you, and this breach resulted in losses in your account, contact us for a comprehensive and confidential investment advisor fraud evaluation with no obligation.

If you or a loved one has been harmed by investment advisor fraud, please call or e-mail our experienced investment advisor fraud lawyers today to find out if you have a case. We'll evaluate your claim for free and help you get the justice you deserve.

Securities Fraud Lawyers

Investment Advisor Fraud Attorney

of Fiduciary Duty

Investment brokers and investment advisors are fiduciaries that owe their clients a duty of loyalty and care. An investment advisor, as an agent of the customer, stands in a relationship of trust, confidence and responsibility, with certain obligations to his customer. Because of this relationship, investment advisors and securities brokers hold themselves out as being experienced, and able to provide specialized service. The level of loyalty and care owed depends on the type of accounts held by the investors. In a discretionary account the broker can trade the customer's account without obtaining explicit customer approval for each individual transaction. On the other hand, for a non-



Free Claim Evaluation
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Claims Statistics

- Average Defense Costs \$42,000*
- A lawsuit typically can cost more than \$100,000 in legal fees and take five years to resolve.**
- Investors were awarded damages in 55% of cases filed***

*Bud Bigelow, president and CEO of Cambridge Alliance

** Chinks In The E&O Armor, Tracey Longo

*** The Hartford Claim Statistics

Investment Advisers and Consultant's Professional Liability (or Errors & Omissions)

- Protects advisers and consultants against losses due to any actual or alleged negligent act, error or omission committed in the scope of their duties as investment counselors/advisers.
- Professional liability insurance or errors and omission insurance is available for a number of different types of investment advisers and consultants:
 - Investment Advisers
 - Investment Consultants
 - Trustees
 - Broker/Dealers
 - Pension Consultants
 - Litigation Consultants
 - Actuaries

Underwriting requirements

Underwriters will review the following information before providing pricing, limits and deductibles when quoting this investment adviser consultant exposure:

- Investment Advisers/Consultants application
- Asset types
- Asset under management
- ADV or other marketing information
- Manager experience
- Prior claims experience
- Designations
- Client contracts

Hartford's Policy Definition of a Professional

Investment Adviser mean an insured who is register investment adviser as defined in the Investment Advisers Act of 1940, or

in “The bottom line is, if you render advice on a continuous basis and that advice is particularized to that plan and people rely on that advice, ... then you are a fiduciary.”

- Marcia Wagner, Esq

compensation to be paid therefore: but not limited to, **an insured who acts as fiduciary with respect to an employee benefit plan** covered by the Employees Retirement Income Security Act of 1974

Cambridge Alliance Policy Definition of a Professional Services

22. "**Professional Services**" means services rendered for or advice given to others by the **Insured** for a fee, remuneration or other consideration in the **Insured's** practice as a **Financial Advisor**. **Professional Services** shall not include: (1) any services rendered during the period of any suspension or revocation of the **Insured's** certification, licensure, accreditation, appointment or other right to practice as a **Financial Planner, Registered Representative, Registered Investment Adviser or Life Insurance Agent**; or (2) activities as a partner, principal, officer, director, manager, member or employee of any organization or public office other than the Named Insured or an organization specifically endorsed by name onto this policy.
23. "**Registered Investment Adviser**" means an **Insured** who meets the definition of investment adviser as defined in the Investment Advisers Act of 1940, as amended, and who is registered as required by law with either the Securities Exchange Commission ("SEC") or the appropriate state authority.
24. "**Registered Representative**" means a person who: (1) is registered with the National Association of Securities Dealers, Inc. as a **Registered Representative** of a **Broker** or **Dealer** pursuant to the provisions of the Securities Exchange Act of 1934; and (2) is in the business of buying and selling **Securities** for the account of others, including but not limited to, direct participation products such as limited partnerships, shares in mutual funds, unit investment trusts and variable annuities. It does not include any person while acting in the capacity of a principal of a **Broker** or **Dealer**, including but not limited to a General Securities Principal or Limited Principal General Securities Sales Supervisor.

Eight disadvantages *of* maintaining your insurance only through your Broker Dealer

Eight disadvantages of maintaining your professional liability insurance ONLY through your Broker/Dealer

1. Not portable

Insurance through your Broker/Dealer (B/D) is tied directly to the services you provide for that B/D. If you move to another B/D, or move on to provide other services, you can not take your insurance coverage with you.

2. Prior acts coverage may end when you leave the Broker/Dealer

In addition to not being portable, you will typically lose your prior acts coverage (coverage for previous work that you performed) when you move to another B/D.

3. Limits may be eroded by other Registered Representatives claims

The aggregate limit on a B/D policy is typically shared by all of their Registered Reps. Therefore, claims against other Representatives may reduce your available coverage.

Eight disadvantages of maintaining your professional liability insurance ONLY through your Broker/Dealer

4. May not cover other services or products outside of those provided by the Broker/Dealer

A typical B/D policy will only provide coverage for services and products provided with that named B/D

5. May exclude RIA activities

The B/D policy may not cover all of the services that you provide and typically will not provide coverage for RIA services.

6. May exclude entity coverage

A B/D policy is intended to provide coverage for the individual representative of the B/D. Coverage may not be provide for you entity.

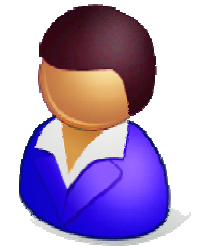
Eight disadvantages of maintaining your professional liability insurance ONLY through your Broker/Dealer

7. May limit best options as a fiduciary

Not all policies are the same and with increasing scrutiny on fiduciary responsibilities, you want to make sure your policy provides coverage for your role as a "fiduciary".

8. No ability to amend coverage as a certificate holder

As a certificate holder of your B/D's coverage, you do not have the ability to amend coverage as necessary to your specific needs.



Third Party

Investment Advisers ERISA Bond



Investment Adviser ERISA Bond

- Section 412 under **ERISA** states every fiduciary of an employee benefit plan and every person who handles funds or other property of such a plan shall be “bonded” against fraud or dishonesty.
- Investment Advisers who control Plan Assets and make investment decisions for ERISA Plans are required to maintain an Investment Advisers ERISA Bond. Up to a maximum of \$500,000 for each qualifying plan. \$1,000,000 for companies offering company stock
- Bonds can be written on an individual basis, where each plan is identified, or written as a blanket bond covering all plans.

Investment ERISA Bond Notes

- ERISA plans should require third-party vendors who handle plan funds to provide a copy of a current ERISA bond with the individual plan named as evidence of insurance.
- Most bonds will automatically cover new clients added during the year at no cost
- Investment Adviser ERISA bonds are sometimes also called 3rd Party Fidelity Bonds



First Party

Fiduciary Insurance



Fiduciary Insurance

Who is considered a Fiduciary under ERISA law?

- **ERISA fiduciaries are either named in the plan document or are identified by the function they perform for the plan.** Since fiduciary status may be based on a person's conduct rather than his title, it is possible to be a fiduciary without being aware of it. Regardless of whether he has knowledge of his status, an ERISA fiduciary must (1) act for the exclusive purpose of providing retirement benefits to plan participants, (2) fulfill a duty of loyalty to the participants, (3) act prudently, and (4) avoid conflicts of interest and acts of self-dealing known as prohibited transactions.
- The definition of a fiduciary includes any person who exercises any authority or control respecting the management or disposition of plan assets. Assuming that an investment professional lacks such control, he could also be a fiduciary to the extent that he renders advice for a fee or other direct or indirect compensation, with respect to any moneys or other properties of the plan, or has any authority or responsibility to do so. In other words, if you receive compensation for which you have the responsibility to provide investment advice or for which you actually provide investment advice, you will be a fiduciary.

Provided by Marcia S. Wagner, Esq. The Wagner Law Group
www.erisa-lawyers.com

Fiduciary Insurance

- A fiduciary liability policy protects the personal assets of plan fiduciary due to allegations of breach of fiduciary duties.

What can fiduciary insurance policies cover?

- Breach of fiduciary duties
- Negligent errors and omissions
- Improper disclosures to plan participants
- Remiss investment advice
- Imprudent choice of outside service provider (OSP)
- Faulty advice of counsel
- Improper amendments to plan documents

Plans subject to ERISA

- **Pension Plans**
- Profit Sharing
- Thrift and Savings (401k)
- Employee stock ownership (ESOP)
- Tax Reform Act stock ownership plans (TRASOP)
-
- **Welfare Plans**
- Life Insurance
- Hospital – surgical – medical insurance
- Dental and vision care insurance
- Accident insurance
- Disability insurance
- Scholarship plans (funded)
- Supplemental unemployment
- Prepaid legal services
- Some severance pay plans

Fiduciary Insurance

Why Purchase Fiduciary liability?

- *To Avoid Loss of Plan Assets* – Using plan assets to defend ERISA litigation is a very questionable use of plan assets, and potentially a breach of fiduciary duty. Another potential breach is for the plan to lose money that could have been paid by a fiduciary liability policy, had one been in place. ERISA explicitly allows for the purchase of fiduciary liability insurance.



First Party

ERISA Bonds



ERISA Bond

- ERISA requires that each fiduciary of employee benefit plan be bonded. Each ERISA (Fidelity Bond) must meet the following criteria:
- The bond must be equal to 10 percent of the plans assets at the start of the plans fiscal year not less than \$1,000 and not greater than \$500,000.
- If more than one plan is covered under a single bond, the bond must allow for recovery by each plan in the amount that would be required if an individual bond was purchased.
- The bond must cover the plan against loss of assets due to fraud or dishonesty on the part of a plan administrator, trustee, officer, or employee.
- The bond must provide coverage from first dollar. No deductibles are permitted
- Plan ERISA bonds are relatively inexpensive and may be covered by a business employee dishonesty policy. All bonds should be compliant with ERISA regulations regarding coverage intent.

New ERISA Bond Requirement

- Applicable to all plans that offer company stock
- Effective 12/31/07
- Minimum bond requirement increased from \$500k to \$1MM

- **SEC. 622. INCREASE IN MAXIMUM BOND AMOUNT.**

(a) IN GENERAL.—Section 412(a) of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1112), as amended by section 611(b), is amended by adding at the end the following: “In the case of a plan that holds employer securities (within the meaning of section 407(d)(1)), this subsection shall be applied by substituting ‘\$1,000,000’ for ‘\$500,000’ each place it appears.”**(b) EFFECTIVE DATE.**—The amendment made by this section shall apply to plan years beginning after December 31, 2007.



First Party

Employee Dishonesty for Investment Advisors



Employee Dishonesty Insurance

- The difference between Employee Dishonesty coverage for Investment Professionals from standard Employee Dishonesty is the inclusion of coverage for the acceptance, and action on, client investments where the client investment is fraudulent.

Financial Institute Bond Form 14

- Investment Advisers
- Investment Consultants
- ERISA Plan Consultants
- Trustees
- Broker/Dealers
- Pension Consultants
- Litigation Consultants
- Actuaries

Employee Dishonesty Insurance

- Each bond provides coverage for loss of property that is caused by the dishonesty of employees and crimes of others (non-employees).

The bond is broken down into six assuring agreements:

Insuring Agreement A- Fidelity

Coverage is provided for loss involving any dishonest or fraudulent act of any employee. Such loss is covered no matter where it is committed and whether it occurs alone or in collusion.

Insuring Agreement B- On Premises

Agreement B responds to loss that occurs on an insured's premises, from robbery, burglary, larceny, theft, false pretenses, misplacement or mysterious disappearance, damage or destruction.

Insuring Agreement C- In transit

This coverage is similar to Insuring Agreement B while the property is in transit, custody of a messenger or armored car.

Employee Dishonesty Insurance

Insuring agreement D- Forgery or Alteration, Optional coverage

- This optional provision covers loss resulting from forgery or alteration of any negotiable instrument, except registered or bearer bonds.

Insuring agreement E- Securities Optional Coverage

- This provision handles a loss that occurs because in good faith, the insured for his or her own account, or others has acquired, sold or delivered, or has given value extended credit or assumed liability on the faith of an original; certified security; document of title; deed, mortgage or other instrument conveying title to, or creating or discharging a lien on real property ; certificate of origin or title; evidence of debt; corporate, partnership or personal guarantee; security agreement; based on the forged signature of any maker, drawer, issuer, endorser, assignor, lessee, transfer agent, register, acceptor, guarantor; or that has been altered; or lost or stolen.

Insuring Agreement F- Counterfeit Currency

- This agreement provides coverage for loss that results from the insured's receiving counterfeit money of the United States, Canada or any other country where the insured maintains a branch.

Risk Management



Why you should carry insurance

- Investment Advisors are targeted class for lawsuits
- Not enough to carry insurance, needs to cover your services
 - Fiduciary, Broker/Dealer
- Plan Sponsors may soon require Advisors to carry coverage
 - Marketing opportunity

Why your clients should carry insurance

- As an Investment Advisor it is prudent Risk Management to request your clients to carry Fiduciary Insurance and Employee Dishonesty Insurance
- Having a first party policy in place to make a client whole after a loss will minimize potential claims against you
- Harder for an insurance carrier to subrogate than for an attorney to file E&O claim

Future Webcast

- Fiduciary Insurance – Educating your clients – January 24, 2008
- Specifically designed presentation for Investment Advisors and Financial Professionals to learn how to educate your clients on Fiduciary Insurance.
- Free Powerpoint with tutorial
- **www.naplia.com/webcast**

Resources

- www.Naplia.com
- 1-866-656-8170
 - www.InvestmentAdvisorInsurance.com
 - www.fiduciaryinsurance.com
- www.fi360.com
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