



Board Report 22-24

Date: April 19, 2022

To: Board of Deferred Compensation Administration (Board)

From: Staff

Subject: Fiduciary Liability Insurance

Board of Deferred Compensation Administration
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Raymond Ciranna <i>Vice-Chairperson</i>
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Recommendation:

That the Board of Deferred Compensation Administration receive and file report regarding fiduciary liability insurance and the City's Deferred Compensation Plan.

Discussion:

A. Background

At its October 20, 2020 meeting, the Board considered Board Report 20-38, which addressed financial education and investment advice services and deferral of a previously planned participant fee holiday. Related to that report was a discussion with the Board regarding the potential for purchasing Deferred Compensation Plan (DCP) fiduciary liability insurance. Staff was requested to report back regarding considerations regarding fiduciary liability insurance. Staff worked with the City Attorney and Segal Consulting to research this matter.

B. Findings and Board Action

In Board Report 20-38 staff indicated that the City, by establishing the City's DCP in Los Angeles Administrative Code Division 4, Chapter 14, has a statutory duty to defend and indemnify individual Board members and staff acting in the scope of their duties, pursuant to California Government Code (CGC) Section 995. Further, staff indicated that the City may, under Government Code Sections 995.6 and 995.8, indemnify Board members in administrative and criminal actions if it determines that (i) the action was brought on account of an act or omission in the Board member's scope of employment, (ii) the defense would be in the best interests of

the City, and (iii) the Board member acted, or failed to act, in good faith, without malice and in the apparent interests of the City. Staff indicated that the City could also defer its decision regarding indemnifying the Board member until after the criminal or administrative action has concluded and facts relevant to the decision have been determined. In such an instance, the accused Board member may be required to fund their own defense costs on an interim basis until the City provides the indemnity or fully if the City does not indemnify. If the accused Board member is found guilty, then it may be difficult for the City to make the required findings for the indemnity. Staff noted that it may be possible for the Board to purchase separate fiduciary liability insurance for those situations where the City would not provide indemnification to the Board.

C. Funding Source

Purchasing fiduciary insurance requires a funding source. Staff first reviewed the question of whether it is permissible to use participant fees to purchase fiduciary liability insurance for an oversight body. Under the Los Angeles Administrative Code, DCP expenses are required to be funded solely by participant fees. Further, certain restrictions exist on the use of participant fees relative to what is considered to be a valid plan expense.

To address this question, the City Attorney reached out to DCP outside tax counsel Ice Miller. Ice Miller indicated that the Department of Labor (DOL) issued Information Letter 07-28-1998 which addressed the application of the Employee Retirement Income Security Act of 1974 (ERISA) to the payment of certain expenses by multiemployer pension plans. As part of that Information Letter, the DOL indicated that plan assets may be used to purchase fiduciary insurance, as indicated in the following excerpt:

Similarly, the trustees must consider whether to purchase the linked insurance for the plan in light of all the relevant facts and circumstances and in accordance with their responsibilities as fiduciaries. In this regard, section 410(b)(1) of ERISA expressly allows, but does not require, a plan to purchase insurance for its fiduciaries or for itself to cover liability or losses occurring by reason of the act or omission of a fiduciary, provided that such insurance permits recourse by the insurer against the fiduciary in the case of a breach of a fiduciary obligation by the fiduciary.

As noted above, any insurance policy would thus need to provide recourse by the insurer if the fiduciary breached his/her fiduciary obligation. This presumably could be incorporated into a policy.

D. Types of Coverage

Based on staff's research, generally there are three major types of insurance policies available:

- Side A Coverage – Side A coverage insures **directors and officers** for claims which are not otherwise indemnified.

- Side B Coverage – Side B coverage insures **organizations** for claims which are not otherwise indemnified.
- Side C Coverage – Side C Coverage insures **organizations** for particular types of claims (e.g. claims related to violations of securities laws).

Together, these three lines of coverage could be included within a single policy and would be triggered either individually or jointly available based on the type of claim situation or event which occurs. It is also possible to purchase Side A coverage as an individual policy, and potentially it could be less expensive to do so.

E. Next Steps

On April 4, 2022, through the DCP consulting relationship with Segal Consulting, staff met with Segal Select Insurance Services, Inc. (Segal Insurance Services), an insurance brokerage subsidiary of The Segal Group, Inc. Segal Insurance Services is a broker supporting plan sponsors and boards/directors in obtaining fiduciary liability insurance and other types of coverage. Segal Insurance Services outlined certain considerations for plan sponsors with respect to fiduciary liability insurance and how it assists plan sponsors in protecting the plan and insured persons.

Staff requested that Segal Consulting, on the City's behalf, develop a report to the Board with respect to general trends and findings in terms of the current state of industry providers within this space, general information regarding the scope and costs of coverage, as well as options and considerations with respect to procuring for coverage. This report will be provided to the Board at its May 17, 2022 meeting.



Submitted by:

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