Segal Select Insurance Services, Inc.

Memorandum for Board of City of Los Angeles Deferred Compensation Plan

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June 7, 2022

Introduction

At the Board’s request, below is a general overview and findings of the current state of the fiduciary lability insurance for governmental plans. The report is being provided for the Board’s review and consideration in procuring the insurance coverage. As referred to under ERISA, a governmental plan is a “plan established or maintained for its employees by the Government of the United States, by the government of any State or political subdivision thereof, or by any agency or instrumentality of any of the foregoing.”

Highlights

1. **What is public sector Fiduciary Liability insurance?**

- Fiduciary Liability Insurance for public sector employee benefit plans is designed to protect plans and/or trustees, committees and employees against lawsuits alleging breaches of fiduciary duty and negligence in the administration of the plan. Some policies will also cover IRS penalties and voluntary correction programs. Policies vary widely and coverage may vary based on plan size and structure.

2. **As a Member of a Public Sector Board do you need Fiduciary Liability Insurance?**

- While there is not an obligation to purchase insurance it is designed to provide coverage for the plan, its committees and its trustees where indemnity or sovereign immunity is not available or does not apply, such as when a fiduciary faces a claim of bad faith or acting outside the proper scope of employment. As gaps in immunity and indemnification protections vary and are not always certain depending on the type of allegations, the need for greater level of protection exists. The fiduciary policy also can provide balance sheet protection to the sponsoring governmental entity, even when governmental immunity or indemnification could apply.

- Various operational issues can expose plan trustees and their committees to litigation. Examples include participant services, investment offerings, fees, plan governance, failure to meet statutory requirements, strategic partnerships and scandals. The claims of potential highest severity include claims of imprudent investments or services. Although public sector plan trustees are exempt from ERISA, they may face increased liability risk if they’re subject to statutes that “mirror” ERISA as well as to trust and/or common law. And, depending upon the state or municipality, public sector plan fiduciaries may be subject to a “faithful performance” standard that’s higher than ERISA’s “prudent-man” standard.

3. **Coverage Options: What is the main difference between a fiduciary liability insurance policy and Governmental side-A policy?**

- Whereas a fiduciary liability policy provides coverage to both the plan and the plan fiduciaries, an A-Side policy covers the personal liability of just the plan fiduciaries. An A-Side policy can be purchased on its own, or in conjunction with the fiduciary policy, if the governmental entity wants to provide additional protection for its plan fiduciaries. Typically, self-retentions apply for fiduciary liability policies for indemnification claims whereby Side A policies generally have a zero-retention applied to the policy.

- Other coverage options: Excess Insurance is typically available to assist plans and trustees in expanding the limits available through placing the insurance with one or more carriers.

4. **Market Conditions**

- Over several years, there has been a spike in lawsuits alleging excessive fees and recordkeeping litigation against 401(k) defined contribution plan sponsors public and private sector and more recently against private universities related to 403(b) and Taft-Hartley plans. These claims allege breach of fiduciary duties and alleging unfair treatment by employers for investment options, services and lack of documentation in plan documents. Claims usually name the plans, their boards, individuals, investment advisors and consultants.

  This growing area of litigation has caused disruption in the fiduciary liability market including underwriters instituting stricter underwriting requirements. Most carriers are requiring pointed underwriting questions to address key concerns about recordkeeping fees, the RFP processes in place and the evaluation process for investment options. With plan sponsors facing more expensive litigation, carriers are increasing self-retentions and raising insurance premiums across the board.

5. **What to expect for limits, retentions and pricing?**

- Litigation tends to be costly, risking organizational assets, fiduciaries and employees' personal assets or both. That's why ensuring you have a broad scope of coverage with reasonable limits and a competitive premium is critical.

- Understanding what coverage terms apply for your benefit plan matters because policy terms can vary by the type of benefit plan.

- Based on the Peer Group of similar asset size, typical limits purchased are between $15-million and $25-million for the Side A policy depending on risk appetite.

- Based on Peer Group of similar asset size, typical limits purchased are $25-million or higher for the Fiduciary Liability Insurance policy depending on risk appetite.

- The Fiduciary Liability policies premiums will depend based on market conditions, underwriting review and have generally increased over the past few years.

- Working with carriers to obtain the best terms and negotiate no policy retentions as available.

Important Note

You, the prospective insured, represent and warrant that the information provided by you in connection with the application for insurance is complete and accurate through the later of the date that (i) coverage is bound or (ii) coverage becomes effective. You agree to immediately notify Segal Select Insurance Services, Inc., in writing, if any of the information included in the application changes between date the application for quotation/insurance coverage is submitted and the later of (i) the date of the quotation or the date coverage is bound or (ii) the effective date of coverage. You understand and acknowledge that the quoting insurance carriers may reserve the right to withdraw or amend any outstanding quotations based upon such changes and that Segal Select Insurance Services, Inc. will not have any liability whatsoever for the decisions of any quoting insurance carriers based on any such changes.

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