Mesirow Financial’s Strategy For Success

Fiduciary Liability Insurance

For Municipal Pension Funds

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Overview for Today

- **(I) What is the fiduciary liability of governmental plan trustees via the Illinois Pension Code?**
- **(II) Common claims associated with public funds.**
- **(III) How to protect yourself with fiduciary liability insurance**

Fiduciary Liability Insurance For Municipal Pension Funds

- Trustees and employees of governmental, municipal and quasi-governmental pension plans face increased exposure in their roles as fiduciaries. Allegations of breaches of duty are costly to defend, and may result in personal liability of the trustees. Mesirow Financial Insurance Service's Fiduciary Liability specialists provide the following summary of the Illinois Pension Code ("Pension Code"), and offer a solution to lessen your fiduciary exposure.

- The fiduciary duties under the Pension Code mirror standards similar to those outlined in ERISA. These duties include: acting solely in the interest of the participants and beneficiaries, adhering to the so-called "prudent investor" standard and adhering to other provisions of the Pension Code.

Enforcing Provisions and Limitations on Liability

- The Pension Code provides that participants, beneficiaries, fiduciaries and/or the Attorney General may bring suits to enforce a fiduciary's duties and other provisions of the Pension Code.
- The Pension Code offers no real limitations on liability and makes clear that litigation against fiduciaries is permissible. Any fiduciary that breaches his/her duty can be held personally liable to make good to such pension fund any losses resulting from such breach.

Insurance Authorization and Indemnification Provisions

- The Pension Code permits, but does not guarantee, the indemnification of trustees and employees of the pension fund
- This potential indemnification is NOT provided for allegations of willful misconduct or gross negligence
- Each board and pension fund is authorized by the Pension Code to purchase insurance to protect against the liability of trustees, staff and employees which may arise as a result of claims.

The Illinois Pension Code

- The Illinois Pension Code requires fiduciaries to adhere to many of the same standards outlined in ERISA. Breaches of established fiduciary duties may translate into personal liability for the trustees of Illinois pension plans. But, this same Pension Code allows for the purchase of insurance to protect the plan, the trustees and the staff from such liability.
- Our professionals at Mesirow Financial Insurance Services are experienced in structuring comprehensive fiduciary liability insurance programs to provide trustees with added protection in their roles as fiduciaries of Illinois pension funds.

Common Claims

1) <u>Imprudent Investments</u>

- Participants or co-Fiduciary files a lawsuit alleging that the Trustees breached their fiduciary duties (failure to act solely in the interest of beneficiaries and for the exclusive purpose of providing benefits) in association with an investment.
- Includes failure to diversify investments, employer stock claims and real estate claims.

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Common Claims (cont.)

2) <u>Prohibited Transactions</u>

- Self Dealing – Trustees are prohibited from engaging in self-dealing – that is, using assets of the Plan for their own interest or the interests of an adverse party.
  - A Trustee may avoid engaging in self-dealing by removing himself from the decision-making process and not otherwise exercising fiduciary authority over the decision;
  - A Trustee will be found to have used Plan assets for his own interest if he uses the authority or control that makes him a fiduciary to cause the plan to use assets in such a way that he will benefit, and the Trustee has an interest in the transaction at issue that could affect his judgment as a fiduciary.
  - For example, a Trustee participates in a decision to retain his son to provide services to the plan for a fee; or
  - A Trustee invests plan assets in companies in which he owns a substantial equity interest; or
  - A Trustee participates in a decision to pay himself an excessive salary.

Common Claims (cont.)

3) <u>Benefits Due</u>

- Most Common Claim that is filed under breach of Fiduciary Duty.
- Includes claims related to miscalculations of benefits.
- Includes claims related to decision to not extend and/or to terminate benefits.

4) <u>Errors & Omissions (E&O)</u>

- Includes failure to educate plan participants.
- Includes failure to monitor other trustees and their actions.
- Includes failure to monitor plan vendors and administrators.

Critical Insurance Policy Features

1. Claims-Made Coverage + Prior Acts Coverage
2. Coverage for Administrative Errors (in addition to Fiduciary Duties)
3. Optional Choice of Counsel
4. Severability of Application and the Exclusions
5. Final Adjudication Wording
6. Deductible ($0?)
7. Underwriting-Specific Exclusions (i.e. specific investments, funding status, trustees)

Underwriting Process

- **Required:** Application, Audited financial statements for pension fund
- **Markets:** Ullico, AIG, Travelers, Chubb
- **Underwriting considerations that affect pricing:**

--claim history

--funding status

--limits purchased

--total assets in plan

--how high profile a municipal pension plan may be

- **Receive/Review Quotes (7 – 10 days)**
- **Formal Proposal of terms/conditions/pricing to Board**

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