# ERISA Advisory Council

## Fidelity/Crime Discussion

***September 8, 2022***



Willis Towers Watson

# FINEX Coverage Overview

## Core insurance products

| | |
|---|---|
| **Directors & Officers Liability (D&O)** | •Covers individual Directors and Officers from personal liability and the Organization from liability for Wrongful Acts arising out of the management of the Organization. |
| **Errors & Omissions or Professional Liability (E&O)** | •Covers the Organization and its employees for Wrongful Acts in the rendering of (or failure to render) Professional Services. |
| **Employment Practices Liability (EPL)** | •Covers the Organization and its employees from liability from Employment Related Wrongful Acts. Wrongful Acts include wrongful termination, discrimination, workplace harassment, and retaliation. |
| **Fiduciary Liability** | •Covers the Organization, any Sponsored Plan (including employee benefit plan, pension benefit plan, and welfare benefit plan), employees, and natural person trustees and fiduciaries of a Sponsored Plan from liability arising out of ERISA violations and negligent acts in the administration of any Sponsored Plan. |
| **Fidelity Bonds** | •Covers the Organization against loss from employee theft and various criminal acts carried out by third parties. |
| **Cyber** | •Covers the Organization and its employees from liability and expenses arising out of a data security breach or privacy event. |

# FINEX Coverage Overview

## Fidelity Bonds

**Who's Typically Covered?**

- First Party Coverage – first party indemnification policy. Do not cover losses to third parties except where such losses were incurred due to the insured's employee's dishonesty or while the third party property was in the possession (care, custody, control) of the insured.

- Fidelity/Crime policies are for the **"sole use and benefit of the Insured"** — only the Insured can file a claim.

**Summary**

- Protects the company against losses caused by dishonest employees and various types of third party fraud.

- The policy is peril specific and requires a direct loss of assets resulting from a named peril. The assets covered include money, securities and other tangible property, as defined by the policy.

- Meets ERISA  requirements for the bonding of Employee Benefit Plans assets from theft by plan fiduciaries.

- Coverage is written on a Discovery – based form.  Meaning coverage is afforded to losses discovered while the bond is in force, regardless of the date on which the loss actually occurred.

# Additional Insuring Agreements

## Fidelity Bond

| Insuring Agreement | Coverage |
|---|---|
| Computer Systems Fraud | ▪ Loss resulting from the fraudulent entry of or change of Electronic Data or Computer Program which causes property to be transferred paid or delivered, an account to be added, deleted, credited or debited. |
| Fraudulent Transfer Instruction-Social Engineering | ▪ Loss resulting directly from the Insured having, in good faith, transferred Money on deposit in a Customer's account, or a Customer's Certificated Securities, or an Insured's account in reliance upon a fraudulent instruction transmitted to the Insured via telefacsimile, telephone, or electronic mail. |

# Basic Insuring Agreements

## Fidelity Bond

| Insuring Agreement | Coverage |
|---|---|
| A – Fidelity | ▪ Covers loss resulting from dishonest or fraudulent acts committed by an Employee acting alone or in collusion with others, acts are committed with the intent (1) to cause the Insured to sustain a loss; or (2) obtain a financial benefit for the employee, or another person or entity |
| B – On Premise | ▪ Covers loss of property, if it is the result of:<br>▪ Robbery, burglary, misplacement, disappearance, or<br>▪ Theft, common law or statutory larceny, committed by a person on the premises of the insured, while the property is located within the premises of the insured. |
| C – In Transit | ▪ Loss of property relating to theft, misappropriation or unexplainable disappearance of property in the custody of a Messenger or Transportation Company. |
| D – Forgery or Alteration | ▪ Loss resulting from transferring Property in reliance on a written, original negotiable instrument with a forged signature, or change in beneficiary under and insurance policy which bears a signature that is a Forgery. |
| E – Securities | ▪ Loss resulting from acquiring, delivery or giving value in reliance: a) on a written, original Certificated Security, letter of credit, evidence of debt, or insurance policy loan agreement which bears a signature which is a Forgery; b) on Certificated Securities, letters of credit or deeds and mortgages which are Counterfeit. |
| F – Counterfeit Currency | ▪ Covers losses resulting from the receipt, in good faith, of any counterfeit or altered money of any foreign country in which the insured maintains a branch office. |

# Does your Fidelity/Crime Policy Cover Losses from 401(k) Fraud?

## Potential gaps/hurdles to coverage

1. Deductible – most plan participants have account balances of $100,000 or less, which is generally below the applicable deductible. Thus, even where coverage might exist, the loss would not likely exceed the deductible.

2. Social Engineering Insuring Agreement – as currently written, Social Engineering only applies when an employee of the Insured is being duped. Most employers outsource recordkeeping and fund disbursement functions to third party plan administrators, rendering the Insured's Social Engineering Fraud coverage inapplicable

3. Computer Fraud Insuring Agreement – as currently written, the majority of fidelity/crime policies require that the loss involve a computer/computer system owned/utilized by the Insured. The majority of these losses involve a computer/computer system owned or used by the plan administrator which is often an unaffiliated third party, rendering the Insured's Computer Fraud Insuring Agreement inapplicable.

# Pension Plan Fraud Policy

## Bespoke Crime Protection for Plan Participants

Insuring Agreement:

- Covers loss of funds or other property sustained in the account of a person participating in the Pension Plan of the Named Insured as a direct result of the Fraudulent Impersonation of such plan participant
- Fraudulent Impersonation means the fraudulent transfer of plan participant's funds or other property as the result of the Insured or the Plan Fiduciary acting upon fraudulent instructions purportedly sent by a plan participant or a person authorized by the plan participant to act on their behalf, that was sent electronically (including by internet), by telephone or in writing.
- The policy does not cover loss resulting directly or indirectly from a fraudulent instruction if the sender, or anyone acting in collusion with the sender, ever had authorized access to such plan participant's password, personal identification number (PIN) or other security code.

Limit of Liability:

- The limit of liability shown on the declaration page applies to each individual plan participant's account in the Insured's 401 K Plan
- The policy maintains an each and every loss limit, with no annual aggregate limit of liability
- A single loss occurrence in which multiple plan participant accounts sustain a loss from the same person or persons will not erode the per plan account limit of liability
- Deductible / Retention – None

# Fidelity vs Cyber

## Fidelity is intended to be a first party coverage only, responding to theft of tangible property.

- Responds to loss of funds taken directly by cyber criminals (Computer Fraud) or indirectly by using information gleaned from a hack of the insured's computer system (i.e. Business E-mail Compromise that leads to a Social Engineering Fraud Loss)
- Coverage is limited to money, securities, and tangible property

## Cyber, on the other hand, responds to theft of information and provides both first party expenses and third-party liability coverages such as:

- Notification costs to affected customers
- Damages resulting from the disclosure
- Cyber extortion
- Costs to repair a computer system resulting from a breach

However, Cyber policies usually specifically exclude the loss of funds or other property (other than computer data) resulting from the breach of the Insured's computer system.

# Limitations of Fidelity Bond to Address Cyber Risks

**There are three major exposures contemplated by a cyber policy:**

1) **the costs associated with the unauthorized access to or use of Personally Identifiable Information (PII).**
2) **the third-party liability arising from the breach and**
3) **1st party coverage for business income loss due to a cyber event, i.e. network goes down due to a breach or system failure and business income is lost.**

**<u>Fidelity bonds provide only first party coverage and do not respond to liability claims</u>**

**Furthermore, fidelity bonds contain a *confidential information exclusion* that serves to bar coverage for the losses arising from the loss of confidential information, except for those cases in which the stolen information is used to perpetrate a loss that would otherwise be covered under the policy.**