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Fidelity bond requirements for Plan Sponsors

If you sponsor a company retirement plan as a benefit for your employees, you may be required to maintain a type of insurance called a "fidelity bond." The purpose of a fidelity bond, also known as a "surety bond," is to protect a company-sponsored retirement plan from losses due to potential fraud or dishonesty by those responsible for handling the plan funds. This may include staff or vendors who process payroll, the plan trustee(s) and any others who regularly work hands-on with the plan's assets.

Usually, retirement plans governed by ERISA, such as 401(k), profit sharing and defined benefit plans are required to have a fidelity bond. In fact, without a fidelity bond, the plan would be considered out of compliance with ERISA.

Fidelity bond insurance must cover, or "bond", every person who handles plan assets or property – what ERISA deems "handling funds." Someone is considered to be handling funds when there is a risk that their duties or activities could result in losses to the plan and its participants if that person were to misuse or misappropriate plan assets.

More specifically, a person is defined as handling plan funds if they have:

- **physical contact** with cash, checks or other similar plan property
- **the ability to secure physical possession** of plan funds
- the potential **capability to transfer plan funds** to themselves or other third parties

If the plan outsources a function that requires bonding, such as payroll processing, the plan's fiduciaries are responsible for ensuring that the third-party service provider is properly bonded (unless the service provider is exempt from ERISA's bonding requirements).

At a *minimum*, the coverage amount required for a fidelity bond is the greater of:

- $1,000 or
- 10% of plan assets (as measured on the first day of the plan year)

The *maximum* bond amount is generally $500,000 for plans with $5 million plus in assets as of the first day of the plan year.

In both cases, the bond must cover the plan for the entire year.

There are some exceptions:

- The maximum bond amount required is $1 million for plans that invest in stocks or other securities of the company sponsoring the plan (like an ESOP)
- For plans that invest in "non-qualifying" assets, such as real estate, limited partnerships, private company stock or other non-publicly traded securities, the minimum bond amount is the greater of 10% of the plan assets or 100% of the non-qualifying assets' value

While ERISA requires plan fiduciaries to maintain sufficient fidelity bond insurance, no penalty is incurred if your coverage falls below a certain amount. That said, if your plan is consistently under-insured, it may raise red flags with regulators, which could result in an audit.

Most property and casualty insurance firms can help you obtain a fidelity bond. Keep in mind that only certain insurance companies can issue them. Here is a list of approved insurers (https://fiscal.treasury.gov/surety-bonds/list-certified-companies.html).

Having the proper fidelity bond coverage in place as required by ERISA is important because the plan's named fiduciaries and trustees could be held personally liable for any losses. However, fidelity bonds are easy and inexpensive to implement and if needed, the costs can be paid from plan assets. You must verify adequate fidelity bond coverage annually and report it on your plan's Form 5500.

An experienced retirement plan adviser can help you determine if your plan requires fidelity bond insurance, how much coverage you need and where to obtain it.

Our consultants are skilled at helping public and private organizations better understand their fiduciary responsibilities. Contact **Stu Herskowitz** at **860.856.2071** or **sherskowtiz@hhconsultants.com** to start a conversation.

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