

Key Differences Between Hedge Fund Management Liability and Directors & Officers Liability Only

D&O Only		Hedge Fund Mgmt Liability ¹	
		Hedge Fund Coverage	Hedge Fund Liability plus EPL for Investment Management Entity
Who is an Insured	Investment Management/Advisory Entity ONLY.	<ol style="list-style-type: none"> 1. Hedge Funds, private investment funds and private equity funds 2. Directors, officers, members of the board of management, general partners, managing general partners, employees, trustees of the insured Private Funds 3. Affiliated Service Providers (Investment Management Entity) in their role of operating the fund(s). 	Same plus Investment Management entity for employee related EPL claims.
What is Insured	<p>Directors & Officers and Employment Practices Liability ONLY [Note: for private companies without an outside board of directors the coverage is essentially providing employment practices coverage ONLY-the exception would be offshore funds that have external boards requiring D&O.]</p> <ol style="list-style-type: none"> 1) Directors & Officers Liability <ol style="list-style-type: none"> a) Wrongful acts committed by your firm including error, omission, misstatement, misleading statement neglect or breach of fiduciary or other duty b) Losses resulting from lawsuits alleging misrepresentation, mismanagement or material error or omission in the disclosure of financial information by your firm c) Liability arising out of any matter asserted against you solely by reason of your status as a director, officer, member of the board of 	<ol style="list-style-type: none"> 3) Professional Liability <ol style="list-style-type: none"> a) Liability arising out of professional services provided for your clients, hedge funds, private investment funds and private equity funds b) Additional professional services such as estate planning, tax work, record keeping, and other miscellaneous services, including those performed by Outside Service Providers. c) Wrongful acts committed by your firm or by those for whom your firm has legal responsibility while performing or failing to perform professional services d) Client allegations that your firm's performance was inadequate 4) Hedge Fund Entity Coverage <ol style="list-style-type: none"> a) Liability arising out of the operation and management of any insured Private Funds b) Wrongful acts in connection with a purchase or sale, or an offer to 	<ol style="list-style-type: none"> 1) Employment Practices Liability <ol style="list-style-type: none"> a) Wrongful dismissal b) Discharge or termination of employment c) Breach of any oral or written employment contract or quasi-employment contract d) Employment related misrepresentation, defamation or wrongful infliction of emotional distress e) Violation of employment-related discrimination laws including workplace harassment f) Wrongful failure to employ or promote g) Wrongful discipline h) Wrongful deprivation of a career opportunity i) Negligent supervision j) Invasion of privacy

	<p>management, general partner, or trustee of your firm</p> <p>2) Employment Practices Liability</p> <ul style="list-style-type: none"> a) Wrongful dismissal b) Discharge or termination of employment c) Breach of any oral or written employment contract or quasi-employment contract d) Employment related misrepresentation, defamation or wrongful infliction of emotional distress e) Violation of employment-related discrimination laws including workplace harassment f) Wrongful failure to employ or promote g) Wrongful discipline h) Wrongful deprivation of a career opportunity i) Negligent supervision j) Invasion of privacy 	<p>purchase or sell securities for any insured Private Funds</p> <ul style="list-style-type: none"> c) Allegations that the insured Private Funds have violated local or foreign securities laws d) Liability arising out of any matter asserted against an insured solely by reason of their status as directors, officers, members of the board of management, general partners, managing general partners, employees, or trustees of insured Private Funds <p>5) Directors & Officers Liability</p> <ul style="list-style-type: none"> a) Wrongful acts committed by your firm including error, omission, misstatement, misleading statement neglect or breach of fiduciary or other duty b) Losses resulting from lawsuits alleging misrepresentation, mismanagement or material error or omission in the disclosure of financial information by your firm c) Liability arising out of any matter asserted against you solely by reason of your status as a director, officer, member of the board of management, general partner, or trustee of your firm <p>6) General Partnership Liability</p> <ul style="list-style-type: none"> a) Wrongful acts committed by a general partner, managing general partner or employee of a Private Fund including error, omission, misstatement, misleading statement or breach of fiduciary or other duty b) Losses resulting from lawsuits alleging misrepresentation, mismanagement or material error or omission in the disclosure of financial information or performance of a hedge or private fund <p>7) Fiduciary Liability (OPTIONAL)</p> <ul style="list-style-type: none"> a) Negligent Acts, errors or omissions in the administration of any insured plan 	
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Professional Supervision	Not Covered	<p>Insured's selection of an Outside Service Provider and its oversight and direction of the performance of such Outside Service Provider in providing Professional Services. While most hedge fund operations that Chubb chooses to quote are well run operations, and don't expect lawsuits, a potential source of liability arises from the vicarious liability associated with outside service providers (accounting, back office, etc.) If an error is made in misstating performance or financials, the fund bears responsibility.</p>	n/a
Advantage for Investors	None	<p>To give investors and service providers an extra degree of security and comfort. The 40ActPlus is an excellent selling point to potential investors.</p> <p>All hedge funds have indemnity agreements and carefully structured agreements between the fund and investment management entity, to protect the latter. The trouble is if a suit is brought against the management entity, it is the fund's assets which are used to indemnify. The 40ActPlus acts to make the fund whole and "fund" these indemnification payments, to the degree that the claim is covered [Note: there is a duty to defend under the 40ActPlus policy until is determined the insured is not guilty]</p>	

		Bottom line: The coverage prevents a fund from needing to liquidate positions or use cash for pay for defense costs.	
Cost Can be Allocated to the Funds	No (no advantage to investors-only to investment mgmt entity and outside board members)	Since the funds are actually insured for the benefit of investors too, there is a benefit and is generally recognized as acceptable behavior for hedge funds to allocate 30-40% of premium to the fund as an expense. This dramatically shrinks the net cost and difference in premium between a 40ActPlus policy and D&O only coverage. [Note: this is an unofficial guideline. You should check with your counsel first]	
Coverage for Funds if Named in a Suit	Most standard D&O policies do not provide entity coverage for hedge funds. This means if both the individual directors are sued, as well as the fund, there would be no coverage for the fund, or to defend the fund. This is important because, as we all know, everybody gets sued if something goes wrong.	Policy designed around this exposure. Definitely covered.	
Sources of Exposures	<ol style="list-style-type: none"> 1) Claims against Outside Directors of offshore funds alleging mismanagement of the management entity. 2) Typically Employment Practices Liability for claims brought by employees of the private partnership 	<p>A. Exposure for suits brought by investors/unit holders/limited partners of the private partnership, which invests in other companies (portfolio companies) or securities</p> <p>B. Exposure for suits brought by shareholders of the portfolio companies which the private partnership invests in.</p> <p>C. Exposure for actions brought by regulatory bodies such as the SEC or foreign regulatory bodies for actual or alleged securities violations.</p> <p>D. Employment Practices Liability for claims brought by employees of the private partnership</p>	Employment Practices Liability for claims brought by employees of the private partnership

<p>Examples of Suits</p>	<p>Wrongful Termination, Sexual Harassment</p>	<p>DIRECTORS & OFFICERS LIABILITY (D&O)</p> <p>(i) claims brought by shareholders of portfolio companies against the private partnership or partnership insureds who serve as directors or officers of the portfolio company, alleging securities laws violations, breach of duty and/or mismanagement (usually as a result of poor performance)</p> <p>(ii) claims brought by shareholders of portfolio companies against D&O's for conflict of interest</p> <p>Please note that in the case of a private EQUITY partnership, the source of exposure for the partnership can also arise from managing principals of the partnership serving in an "outside" capacity as directors of the board of a portfolio company, particularly if the portfolio company is going public or already is publicly traded.</p> <p>PROFESSIONAL LIABILITY (E&O)</p> <p>(i) claims brought by limited partners/investors against the investment manager of the private partnership for mismanagement of their invested assets, breach of fiduciary or other duty, (obviously, this exposure can be limited substantially..but not entirely..by strong indemnification and hold harmless agreements)</p> <p>(ii) claims brought by shareholders of portfolio companies themselves against the private partnership and its directors, officers and employees for alleged acts, errors or omissions in rendering or failing to render professional services to the portfolio company</p> <p>(iii) claims brought by the portfolio companies against the private funds, venture capital, private equity or investment firm</p>	
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		C. GENERAL PARTNER LIABILITY (GPL) (i) claims brought by limited partners (outside unaffiliated investors) against the general partner of the private partnership for breach of fiduciary duty.	
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Note: this comparison is based on the modules in Chubb's 40ActPlus policy only.