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Directors and Officers Liability Insurance for Community Associations

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Today's condominium and community associations are confronted with wide ranging types of disputes and issues that can lead to costly litigation for an association. These issues range from disputes between unit owners, disputes over responsibility for repairs within individual units, as well as large and complex issues where litigation ensues, such as construction defect issues, contract claims and non-property damage claims, such as discrimination claims. Whether an association is confronted with a minor complaint or significant litigation, there comes the inevitable point in time where the association must evaluate how it will pay for the defense of the association, as well as the management company. The good news for unit owners and home owners is that a long forgotten insurance policy may be triggered and may be utilized to assist the association, its board and property management in funding defense of the claim or litigation.

Today's community associations have many forms of insurance to obtain when properly insuring the association from certain liabilities, and the importance of Directors and Officers liability coverage (also known as a D&O policy) should not be overlooked or underestimated. What this type of coverage provides is potential defense and/or indemnification coverage in the event the Association is sued for a non-monetary claim. The types of claims that are often covered under a D&O policy are wide-ranging and may provide extensive coverage to a board or association that is threatened with a costly lawsuit.

One common claim that is often submitted by associations under their D&O policy is breach of fiduciary. This type of claim is typically filed against the board for wrongdoing or lack of action in addressing certain situations. Many times unit owners, frustrated with the board or property management's lack of response in addressing a particular situation, file a breach of fiduciary duty claim against the board, seeking recovery for the board's violation of its obligation to the owners in administering the association. This situation may occur where the owner claims there was a failure to maintain the common elements which resulted in damage to an individual unit. Breach of fiduciary duty claims also may arise where there are allegations of self-dealing by board members, mishandling of association funds and other failures to adhere to the association's governing documents.

In addition, claims often submitted under a board's D&O policy include claims of discrimination against the board for discriminatory enforcement or application of the association's rules and regulations. In these types of disputes, owners may allege the board engaged in discrimination in the enforcement or application of the association's governing documents. This claim may arise where the board has expressed, or appeared to express, a preference for a particular group of owners, or has clearly treated a certain group of owners in an inferior manner as compared to another group of owners.

Other common types of claims that may trigger the board's D&O policy include challenges by unit owners to the election process conducted by the board, or a challenge to a decision of the board regarding a construction project. In situations where the election process is challenged, unit owners or home owners may challenge the manner in which the board and/or property management conducted the association's election, including challenges to the notice of the annual meeting, validity of the ballots and proxies, and/or validity of the ballot tabulation process. In claims involving a challenge by a group of owners to the board's determination regarding a construction project, the D&O policy may be triggered where the association's architectural review board or board of directors refused an owner's request to proceed with plans for modification or construction to his/her unit or home in the association.

The board's D&O policy also may be triggered in one large area of litigation involving associations and unit/homeowners- collection or eviction litigation. In this type of litigation,



the association has initiated an action against an owner for failure to pay association assessments. In response, many times owners will take the opportunity, now that the case is before a court, to bring a "defense" against the board on any number of bases, including breach of fiduciary duty, wrongful eviction and malicious abuse of process. In these types of actions, the association transcends from plaintiff, into a defendant in an action that may now be covered under the board's D&O policy.

While insurance coverage may not always be available, and may depend on the particular facts of the case and whether the act(s) complained of fall within the insurance policy period, it is very important for the association to timely evaluate whether a claim should be submitted under the D&O policy. Under many policies, associations are required to provide "reasonable" notice to their insurance provider in order to obtain coverage under the policy. It is important to note that what may seem "reasonable" to the average person may be not reasonable under the policy or in the jurisdiction in which the case is located. For example, in some situations, a delay of a few weeks or months may be determined to be unreasonable, versus other situations where a delay of a year or more may be reasonable given the circumstances. Significantly, under many insurance policies, the date that triggers the board's obligation to report a claim or potential claim to an insurance provider is on the date the association first had knowledge of a particular issue. As a result, the association's obligation to notify its provider may be triggered upon the date when the alleged wrongful acts occurred, the date when the association first received complaints from a unit owner regarding a particular situation or, in some cases, the date when the association first receives formal notice of the owner's complaint. In situations where the "knowledge" date is considered the date the board first had knowledge of a certain issue may become complicated if certain members of an association, including board members, were aware of the issue but failed to take formal steps to notify the insurance provider.

In any situation, where a claim or even a potential claim arises, it is imperative that the board or management company immediately take steps to determine whether a report or notice of a claim should be made to the insurance provider and whether to seek coverage under the D&O policy. The association may need to consult its attorney to determine when the appropriate time to submit the claim has occurred or will occur.

Not only must the board make a decision as to the timing of notifying the insurance provider, but the board must also determine whether to make a claim at all. In deciding whether to make a claim at all, the board of directors of the association must weigh all of the effects of giving notice of a claim to the insurance provider. This is significant because although the Association may enjoy the benefit of utilizing insurance proceeds to fund a defense of a certain claim, the board must consider the negative effect that insurance premiums may increase as a result of the claim. Accordingly, the board should consider all advantages and disadvantages of submitting a claim under the D&O policy and should make an attempt to assess the cost to resolve the issue without involving insurance.

In situations where the Board determines that a claim should be made with the provider, once a claim is made, the insurance provider will be required to make a determination as to whether the claim falls within the policy, based upon the facts alleged and based upon the policy period. In situations where a claim is denied by the insurance provider, the association may still be able to assert its right to coverage and file a "declaratory judgment" action. In this type of action, the association requests that the court make a declaration or ruling that the association is entitled to insurance coverage under the D&O policy.