

When Are You Not Covered by Your D&O Policy?

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When are you not covered by your Directors & Officers (D&O) policy? The question may seem simple, but it's really a multi-part question.

- Where does a community association's D&O policy fall within the entire insurance puzzle?
- Are all D&O policies created equal?
- How does the community association maximize its coverage?

Association members ask these questions because they want to know if the policy covers them for what they do in their volunteer work for the community association. For example, they want to know if they will be covered for situations listed in **fig. 1**.

From an underwriter's point of view, there are two motivations when producing an insurance product: write as many policies as possible and minimize the number of losses. In the context of community associations, the key is to attract the best

and most talented people to serve as the volunteer board members. To motivate these individuals to volunteer, it is imperative to provide them with insurance coverage to protect them from the decision making process. This is what the focus of what the D&O policy should cover.

What Doesn't Your D&O Policy Cover?

The basic concept of insurance is to spread the risk of the consequences of life that are not contrary to public policy, and that the insured can afford to pay the price of transferring the risk. For a community association, there are a number of puzzle pieces. If something is covered under one policy, it generally is not covered, or is "excluded" under another policy.

If you were to ask a D&O claims analyst what is the most rejected claim, the answer would be claims seeking bodily injury and/or property damages. The reason is twofold: First, bodily injury and property

(Fig. 1) Is Your Board Covered?	Yes	No
A vendor sues the board and the association for breach of contract.		
A unit owner sues to compel the board to purchase insurance.		
The community manager sues the association for slander seeking emotional distress charges.		
A unit owner's tenant sues the board for wrongful eviction.		
A unit owner sues because a volunteer sexually harasses a child at the pool.		
The association's doorman sues for wrongful termination.		
An outgoing board president sues to challenge the validity of an election.		
A unit owner sues to challenge an assessment for a new pool.		
A unit owner sues to prevent the removal of trees in common areas.		
The property manager is sued for a alleged unauthorized entry into a unit owner's condominium.		

(Fig. 2) Board Decision	Damage or Demand	Potential Coverage
The board decides to install speed bumps throughout the association streets that are two inches higher than code.	Due to the height of the speed bump, a resident's car is damaged.	The alleged property damage is possible covered by the General Liability policy if the bump's height is determined to be negligent. This would not be covered by the D&O, because of the Bodily Injury or Property Damage exclusion.
The board decides to install speed bumps throughout the association streets that are two inches higher than code.	A group of association members sues to board and the association to compel them to remove the speed bumps for being in violation of height requirements.	The board will be defended by the D&O policy. However, if the board loses, the policy will not pay the cost to remediate the bump height. This will not be covered under the GL policy, because the board's decision was not an "occurrence" (unintentional or accidental act) and therefore not covered.

damage claims normally are covered under a general liability policy, subject to other terms and conditions of those policies. The most common misunderstanding of insured parties (“insureds”) is that if the damage is the result of a board decision to misconduct, it should be covered. However, if the damage is only bodily injury or property damage, they must look to the general liability policy. This is exemplified in **fig. 2**.

The second reason that bodily injury or property damage claims are the most commonly rejected claims is that community managers and insurance agents believe it is better to be safe than sorry and submit such claims to every insurer and let the insurance companies deny them. On the one hand, this is understandable. On the other hand, what these professionals must understand is that every submission costs the insurer money to set up and investigate a claim, and the insurer is required to investigate and respond pursuant to most state insurance statutes.

The purpose of this is not to tell insureds not to submit claims, but to consider the consequences of shot gunning a matter to all insurers. As an alternative, insureds can submit a matter as a notice of potential claim that they are making to preserve their rights pursuant to the terms of the policy, but that they believe

that is more likely covered under another policy within their insurance program. Also not covered under the D&O policy is any action brought by the board of the association against association members or third parties. This type of scenario is often seen in instances when the board of association wants to sue the developer. The D&O policy is a liability policy in which the insureds are going to be defended for their conduct. The policy does not fund an action by the insured against others. It should be noted that when a D&O policy provides coverage for a developer, it is solely in his or her capacity as a board member and not for any work done in his or her capacity as a developer.

One mistake that many associations make is that they believe that when money is taken by a board member, employee or volunteer, coverage is available under a D&O policy. This is similar to the bodily injury/property damage situation discussed previously.

Coverage for this type of claim will be covered under a “fidelity” (otherwise known as “employee dishonesty”) policy or a “crime policy.” The key here is that the fidelity policy includes within the definition of “employee” the board members or others contemplated as an insured under the D&O policy.

Another mistake that associations make is not to

be sure they also have crime coverage, which comes into play when money is taken by a non-employee.

Other types of damage that are not covered under the D&O policy include breach of contract damages or the coverage that the board dialed to obtain when it was purchasing insurance. In the D&O context, the policies sometimes will provide a defense for the board and other named insureds, but it will not provide coverage for the damages that the claimant has incurred as a result. What provides coverage for those items is what is known as a moral hazard. These are exemplified in **fig. 3**.

Not All Policies Are Created Equal

Associations have to understand whether the policy they purchased provides the association with the coverage it needs. One basic notion in life applies directly to insurance: “You get what you pay for.” The other side of that coin should include the adage, “Don’t be penny-wise and pound foolish.” One thing you can be guaranteed of is that insurance companies do not

give insureds anything for free. If you are paying \$250 or \$350 for a D&O policy as opposed to \$850 or \$1,000, do you believe you are getting similar coverage?

There are two types of D&O coverage. First, there are D&O coverages that are included in a package policy. These tend to be very bare-bones policies from carriers that don’t have an interest in providing broad D&O coverage. There also are carriers that issue standalone policies that are tailored to the community-association industry business. The bottom line is how valuable is it to the association to save \$500, \$700, or \$1,000 on the D&O policy?

If the insurance policy doesn’t provide coverage, the association will be responsible and probably have to levy a special assessment. However, the increased cost of a valuable D&O policy is less than what each association member probably pays for an individual auto insurance policy.

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(Fig. 3) Claim	What is Covered	Potential Coverage
<p>The association fires the landscaper in year one of a two-year contract due to incompetence. The landscaper sues the board and the association for breach of contract.</p>	<p>The D&O policy will provide defense fees and costs for the board and the association if the D&O policy provides coverage for breach of third-party contracts.</p>	<p>If the board and/or the association are found to have breached the contract, the policy will not pay the breach-of-contract damages. To do so would encourage the board to breach contracts and look to the D&O to provide coverage.</p>
<p>The board of directors decides to buy a D&O policy that does not provide non-monetary damage coverage to save money and because they have never had a D&O claim in the past. There was a challenge to an election of board members and the board spends \$10,000 to fight the claim. An association member sues the board for its failure to purchase a D&O policy that would have provided coverage for the failure to purchase this type of policy.</p>	<p>The D&O policy will provide defense fees and costs for the board and the associations if the D&O policy provides coverage for failure to maintain or obtain insurance.</p>	<p>If the board and/or the association are found to have failed to obtain the appropriate coverage, the policy will not become the insurance coverage that the board failed to obtain. To do so would encourage the board to only purchase a D&O policy and nothing else.</p>