



No Myth

The Truth About Errors and Omissions Coverage

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A number of myths circulate regarding property manager exposure in the community association industry. We'll call these the "Teflon Myths," since managers who believe them seem to think nothing sticks to them. The first myth is often brought up when I ask a property manager if he or she has errors and omissions coverage. The answer I am most often given is that "errors and omissions coverage is not necessary, because my management agreement with the community association provides me with a hold harmless provision or an indemnity agreement." The second myth that is often proffered is that "the community association's directors' and officers' liability policy will protect me."

The reality of these myths is that, as with most myths, although they make great stories, they aren't quite accurate.

The first problem with a hold harmless or indemnity agreement is that they are just that: "indemnity" agreements. Indemnity provisions, unlike an errors and omissions liability policy, do not provide a defense. Accordingly, after the property manager has spent his or her own money to defend an action, the agreement with the association will allow the property manager to go back to the community association and request reimbursement. There are many problems with this. First, the property manager must seek reimbursement from the hand that feeds him or her. This will definitely be an uncomfortable process. Second, community associations are budget driver entities that probably have not planned for such reimbursements. Therefore, the association will most likely have to take the steps to approve and issue an assessment against the members. This, in turn, will undoubtedly give rise to animosity from members who believe the property

manager should not be reimbursed if they were at fault. In the end, this is not a pretty road to traverse.

Another problem with indemnity agreements is that they are in most cases "general indemnity" provisions, and in most states, they will not extend to the property manager's active negligence. Thus, property managers that were not savvy enough to have a foolproof indemnity provision will end up liability for both defense and indemnity.

The next myth is that the property manager will be fully covered by the community association's directors and officer's liability policy. Unfortunately, there is a big hole in the D&O coverage in virtually all policies. That gap is when the community association itself sues the property manager. Under these circumstances, the property manager is going to need his or her own coverage.

Another factor that has led to the need for property manager errors and omissions coverage is the fact that comprehensive general liability policies routinely exclude professional services or other professional liability coverage. Specifically, underwriters began to sustain significant losses from professional liability in the mid 1970's. As a result, professional services exclusions became standard exclusions in the general liability policies that property managers generally purchased as part of their business packages.

Property managers must also take into consideration the reality that we live and work in an increasingly litigious society combined with heightened performance standards being demanded of professionals. Property managers, like other professionals, must look at errors and omissions coverage as the cost of doing business and incorporate this into their pricing.

Finally, businesses routinely require firms and individ-



uals have evidence of professional liability coverage as a prerequisite for engaging their services. In fact, a community association that does not require this of its property management company isn't being wisely counseled.

The intent of this article is to provide an introduction into the following areas:

- What are the key exposures for community association property managers that give rise to the need for insurance?
- What is generally covered by a property manager errors and omissions policy?
- What are some of the larger issues confronting property managers that may impact the availability and cost of errors and omissions coverage?
- What are some of the more common property manager errors and omissions claims?
- What steps can be taken to minimize property manager errors and omissions claims?

Property Managers Key Exposures

To understand what you need to know about property manager errors and omissions coverage, it is first helpful to review what some of the main exposures for the community association property managers. The following are the key exposures we see as underwriters of property managers errors and omissions coverage:

- Misrepresentation and /or miscalculation of the financial strength of managed properties.
- Inaccurate record keeping or tax preparation for managed property.
- Failure to adequately perform due diligence before hiring subcontractors.
- Failure to provide a written description of services to be performed for the community association.
- Abuse of discretionary authority provided to property manager with regard to capital improvement or repairs.
- Management of properties that are not in compliance

with statutory and regulatory requirements for persons with physical handicaps.

- Inadequate budgeting for property managed.
- Abuse of authority in drafting check or money management activities performed by property manager.
- Failure to perform proper background checks on prospective tenants.
- Entering improper indemnity or limitation of liability agreement.
- Personal injury including libel, slander and invasion of privacy.
- Failure to report insurance claims in a timely manner.

This is not an attempt to exhaust the potential exposures of community association property managers. Rather, the intention is to bring up some of the more common exposures to put the insurance issues into context.

What's Covered

Like most professional liability errors and omissions policies, most property manager errors and omissions policies are "claims made" policies. What this means is that:

- Coverage under the policy is triggered when a "claim" is made against an "insured"
- For a "wrongful act"
- Which happened during or prior to the policy period,
- But after the retroactive date (unless the policy is a full prior acts policy)
- Resulting in "loss."

The claim is a demand on the property manager to do or refrain from doing something – for example, a demand to reimburse the association for a tenant who skipped out because they were a bad credit risk and the property manager did not do a proper background or credit check. The alleged wrongful act was the improper credit check. The alleged wrongful act occurred during the policy period. Thus, the policy would be triggered to provide a defense for the prop-



erty manager.

As indicated above, the typical claims intended to be covered by the association manager error and omission policy are the following:

- Mismanagement of property claim brought by the property owner.
- Failure to process eviction notice properly.
- Personal injury claims including libel, slander or other defamation.
- Inadequate background checks while tenant screening.
- Failure to perform proper tax filing services on behalf of the property.
- Inadequate record keeping.

In order to address these types of claims, the intent of the property manager errors and omissions policy is generally to contain the following:

- Coverage for wrongful acts of the insureds arising out of the rendering of property management services including development and implementation of management plans, securing of tenants and management of tenant relations, processing evictions, implementation of loss control, management of contracts, feasibility of studies, personnel administration, and record keeping.
- Coverage that applies to liability of the insureds' wrongful acts of any person for whom the insureds are legally responsible.
- Any claim for personal injury as defined in the policy is covered, such as libel or slander, malicious prosecution, or unlawful entry or other breach of privacy.
- Claims for both monetary and non-monetary relief including formal administrative or regulatory proceedings.
- Coverage for punitive, exemplary or multiple damages (where insurable by law.)
- Defense coverage for an illegal profit claim.
- Defense coverage for a fraud/dishonesty claim.
- Knowledge or acts of one insured person are not imputed to another insured person.

- Ninety-day automatic extended reporting period.
- If the claim is settled through mediation, the retention will be reduced by 50 percent or \$10,000, whichever is less.
- Policy is non-cancelable unless the insured fails to pay the premium.
- Insurer must give 60-day notice of non-renewal or new terms.
- Will not exclude management of property as long as ownership interest by insured of managed property is less than 20 percent.
- Coverage for defense costs associated with any actual or alleged discrimination.

The typical exclusion for community association errors and omissions policies are:

- Owned entity exclusion applies where the managed property is owned by the insured, but only if owned corporation is more than 20 percent owned (if privately held) or more than 10 percent owned (if publicly traded).
- Illegal profit exclusion applies only if it is established in a final adjudication by a judge, jury or arbitrator that the insured gained illegal profit, remuneration or advantage; acts or one insured person are not imputed to another insured person.
- Fraud exclusion applies only if it is established in a final adjudication by a judge, jury or arbitrator that the insured committed fraudulent or criminal acts with actual knowledge of their wrongful nature or with intent to cause damage; acts of insured person are not imputed to another insured person.
- Bodily injury and property damage exclusion.
- Failure to maintain or obtain insurance exclusion.

Common Claims

What are the most common community association manager claims? The intended claims sought to be covered under the policy were discussed above. By far in our experience as underwriters of this genre or



risk, the most common claims being brought against property managers are discrimination/harassment claims. What is most frustrating from an underwriting standpoint is that these are generally avoidable type of claims. The claims very often result from inadequate training of employees or monitoring of employees. The typical policy will provide a defense to these types of claims, but will not pay out any indemnity.

Another common claim is libel or slander. Community associations are generally high-maintenance organizations filled with a lot of emotions. Accordingly, the property managers, as the professional staff, generally are put in the middle of these issues. Sliding is difficult to avoid and property managers very often are accused of siding, which often turns into allegations of libel or slander.

There are a number of misconceptions regarding the property manager errors and omissions policy. The key misconception corresponds to the most commonly denied claim. The community manager errors and omissions policy does not provide coverage for bodily injury or property damage claims. This is an exposure that needs to be covered in a general liability policy.

Another misconception is that the community association errors and omissions policy, as opposed to the community association directors' and officers' liability policy, does not include employment practices coverage. This is a coverage that must be purchased separately.

Steps to Minimize Claims

As discussed, the most common community association errors and omissions claims are based on discrimination and harassment. One way to avoid such claims is to understand the breadth, magnitude and reach of various fair housing and other discrimination laws. For example, the Fair Housing Laws:

- Prohibit sale, rental and financing of dwellings, and other housing –related transactions based on race, color, national origin, religion, sex or family status.
- Title VI of Civil Rights Act of 1964 prohibits discrimination on the basis of race, color, or national origin and activities receiving financial assistance.
- Section 504 of the Rehabilitation Act of 1973 prohibits discrimination based on disability in any program receiving financial assistance.
- Section 109 of Title I of the Housing and Community Development Act of 1974 prohibits discrimination on the basis of race, color, national origin or religion in programs and activities receiving financial assistance from Community Development and Block Grant Program.
- Title II of the Americans with Disabilities Act of 1990 prohibits discrimination based on disability in programs, services, activities provided or made available by public entities. HUD enforces this act as it relates to state and local public housing, housing assistance and housing referrals.
- Architectural Barriers Act of 1968 requires that buildings and facilities designed, constructed, altered, or leased with certain federal funds after September 1969 must be accessible to and useable by handicapped persons.
- Age Discrimination Act of 1975 prohibits discrimination on the basis of age in programs activities receiving federal financial assistance.

The challenge with continued violations of the Fair Housing Law include the fact that there is no cost to plaintiffs for any out of pocket expenses to file fair housing complaints. Accordingly, community managers must be up to date on fair housing laws as well as continued education for employees. Race, national origin, disability and children/family status are the most common fair housing violations.



The best advice for avoiding manager errors and omissions claims is to participate in CAI and its certifying programs and educational opportunities. The first thing that an employee of a manager will say when being deposed in a lawsuit is: “I was never trained on that issue.” The second thing the employee will say is: “I was never told about that law or requirement.” The ignorance of your employees or yourself is not a defense to most of these claims. Community association managers are professionals and are expected to have the experience, training and expertise to carry out his or her duties and obligations.

Notwithstanding the best training, education and expertise, the one thing that is for sure – right up there with death and taxes – is that you will experience a claim no matter how good you are. That is why you need errors and omissions coverage. With the coverage, you can have full comfort that you can fight the claim.