THE TWO BIGGEST

MISTAKES COMMUNITY ASSOCIATIONS MAKE INVOLVING DIRECTORS & OFFICERS LIABILITY INSURANCE

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The Directors & Officers Insurance policy ("D&O") is a small part of an association's insurance coverage and premium puzzle, but it is a critical piece. It is important because it protects the community members who agree to accept a very often no-win and often thankless volunteer job to manage the association. Contrary to the other pieces of the insurance puzzle, D&O coverage can differ significantly from insurer to insurer. There are currently two significant mistakes associations make in regards to D&O policies.

The first mistake is *price over coverage*. Boards have a fiduciary obligation to manage the association. This obligation includes the procurement of insurance that is in the best financial interest of the association. Accordingly, the first item of business is to obtain the best **coverage** for the association, because the best coverage will respond to the most claims thereby costing the association less at the end of the day. The existence of coverage at the time of a claim is the most important part of the insurance purchase equation.

The average D&O policy is probably about $1,000 for a $1 million limit with a $1,000 deductible. Notwithstanding this incredibly low price, one of the biggest problems we find is that the main focus in the purchase transaction is price as opposed to coverage. *It is always easy to sell price*. What boards must understand is that the point of sale price is only a small part of the equation. An association may save $50, $100, or even $500 on a policy, but if there is an uncovered claim, those purported savings will be dwarfed. The defense of a single uncovered D&O claim can cost the association thousands or tens of thousands of dollars. Moreover, if an association has to fund a lawsuit itself, it may not be able to defend it vigorously and may have to settle notwithstanding the fact that they did nothing wrong. Where will reimbursement come for those uncovered costs and settlement; it will come from the association. Three cheers for the special assessment.

During the past year, I have reviewed thousands of claims. Very often, I review claims as part of an application when an association comes to use because a claim was not covered by its existing policy. Do you know what is covered by your policy? Many policies do not cover: defense of breach of contract, defense of failure to maintain or obtain insurance, discrimination claims, non-monetary claims, emotional distress damages, defamation, wrongful eviction, invasion of right of privacy, challenges to elections, or challenges to architectural review committee decisions. Some policies may not cover past directors, community managers, developers on the board, volunteers, or actions between individual board members. Remember, three cheers for the special assessment.

How does the association know what the best coverage is? There is no shortcut— do your homework. The best place to start is with a professional that specializes in associations. If the professional does not have adequate experience, find one who does. Many associations rely on their managers and many are extremely experienced. However, do not assume they are experienced. Ask your manager how many D&O policies they have reviewed, how many D&O claims they have been involved with, or ask them to explain to you what is or is not covered in various D&O policies. If you are satisfied, great, still call the agent.

The second biggest mistake that associations make with D&O policies is the *untimely reporting* of a claim. D&O policies are normally *claims made and reported policies*. In brief, the policy provides defense and indemnity for a "wrongful act" (the board's alleged mistake) for a "claim" (demand that the board do or not do something about the mistake) made during the policy period **and** reported to the insurer during the policy period.

This policy is different than most associations or their attorneys are familiar. As a result, many claims that would ordinarily be covered are denied because they are not reported in timely fashion. Accordingly, it is imperative to understand in each policy how "wrongful act" and "claim" are defined and what the reporting obligation is. Insurers and courts have no mercy for and have upheld stringently the reporting requirements of these policies.

Fortunately, these two mistakes are very preventable as long as the associations and their managers do the necessary homework. It is always better to be educated than surprised.