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Directors and Officers  
Liability Insurance  
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**D & O  
INSURANCE POLICY**



# Directors and Officers Liability Coverage

## What Every Board of Directors Member Needs to Know

by William F. "Chip" Merlin, Jr., Esq.

**F**lorida Statutes and case law hold condominium association directors and officers immune from liability in their individual capacity, absent fraud, bad faith, malicious or criminal activity, or self-dealing/unjust enrichment. Indeed, it would be extremely difficult, if not impossible, to find people willing to serve as volunteer directors, as is most often the case, if their life's work could be at risk simply because of service. That said, intentional conduct that falls short of a malicious act, such as sexual harassment or discrimination against a protected class, violation of a state or local ordinance, or the grant or denial of an easement, could be a basis for civil liability. Even the specter of civil liability would dissuade a reasonable person from service. Directors and Officers liability coverage (D&O coverage) can eliminate most real and perceived risk.

D&O policies generally offer three types of coverage. Side A, or direct, pays directors and officers for losses when the condominium association (or other business entity) is not legally obligated to pay for a loss or is financially unable to do so. Side B, or indirect, pays a condominium association for money expended to directors and officers pursuant to the association's own obligations to cover a director's loss: for example, when it is required by law to pay or is obligated to pay by bylaws, separate contracts with directors, or state law. "Entity Coverage" protects against claims of Security and Exchange Commission (SEC) violations made directly against an

association or other entity.

### **Who Needs D&O Coverage?**

Liability can be costly because business mistakes are costly. Even though Florida law holds condominium directors immune from civil liability in many cases, a person bringing suit often names a director for strategic reasons, and the director or condominium association will have to expend the costs associated with the defense. There are many instances where the condominium association cannot or will not cover the costs of defense: the association could be insolvent, a new board of directors could choose not to pay the old, or association bylaws could prohibit paying a director's loss. A director should insist upon D&O insurance as a condition of service.

### **What Does the Policy Cover and Whom Does It Cover?**

There is no standard D&O policy.

Policies vary widely in coverage terms and conditions, depending on the insurer and business of the insured. Coverage is subject to the terms and conditions of the policy, typically excluding coverage for fraud, criminal activity, and self-dealing. D&O policies cover liability for “loss” resulting from “claims” made by a third party for a “director or officer’s” “wrongful acts” made in his or her “insured capacity.” Each quoted term is defined specifically or by exclusion in the policy, but there are some generalities. “Loss” usually includes monetary damages, and often judgments, settlements, and defense costs. The policy may specifically exclude taxes, fines, penalties, multiple or punitive damages, or losses that are uninsurable for public policy reasons. “Claim” is generally understood as a claim for money or property, a demand for payment or legal right with a threat of consequences. Lawsuits are clearly covered, less clear are letters or complaints. Anything less than a lawsuit is decided on a fact-specific, case by case basis. “Wrongful act” generally includes a breach of duty, neglect, error, omission, misstatement, or misleading statement. Florida law has held that a condominium director is not personally liable for a negligent act, even if the act is clearly wrong. Often at issue is whether intentional acts are covered. “Insured capacity” is defined specifically or by exclusions both in the policy, service contract, and bylaws. Likewise, “directors and officers” are defined by policy and may sometimes require that they are “duly elected” or include an officer’s spouse, personal representative, or heir.

#### **What Claims Are Covered?**

Coverage is almost always predicated on a claims-made basis. Claims-made policies cover claims made during the policy period, regardless of when the wrongful act occurred. This type of coverage is different from occurrence-based coverage, which covers “wrongful acts” that occur during the policy period, regardless of when the claim is made. D&O insurers prefer claims-made coverage because it provides certainty; once the policy period expires, the insurer’s exposure terminates. Most claims-made D&O policies will provide, at additional cost, “extended reporting” or “discovery” periods, where an association is covered for claims made after the policy period for wrongful acts which occurred during the policy period.

#### **When Does the Insurer Pay and What Is the Duty to Defend?**

Generally, a director or officer who is facing a lawsuit will first turn to the condominium association to pay legal fees and costs. The association will then look to the insurer for coverage, pursuant to a Side B policy. If the association is unwilling or unable to pay, the director can turn directly to the insurer.

In Florida, an insurer’s duty to defend is broader than its duty to pay a loss; if the underlying complaint alleges facts showing two or more grounds for liability, one within the insurance coverage and the other not, the insurer is obligated to defend the entire lawsuit. The duty to defend is determined by examining the allegations in the lawsuit, and the insurer must pay the defense costs when the complaint filed against the director alleges facts which fairly and potentially bring the lawsuit within policy coverage. If the allegations in the complaint leave any doubt regarding the duty to defend, the question is resolved in favor of the director and association.

#### **What Are the Obligations of the Insured?**

The policyholder’s obligations vary by policy. Noncompliance with such obligations can preclude recovery, so directors and condominium

associations should be careful to fulfill their obligations. Typically, the duty to provide notice of claims is specified as within the policy period, within a certain number of days, or as soon as practical. Contention can arise when a policyholder does not notify the insurer of a potential claim, something less than a lawsuit, during the specified notice period. In D&O policies, the duty to cooperate is the duty to provide information, most often notice of a claim or potential claim, and to provide all information and documents the insurer needs to review.

#### **Can a Policyholder Settle a Claim without the Approval of the Insurer?**

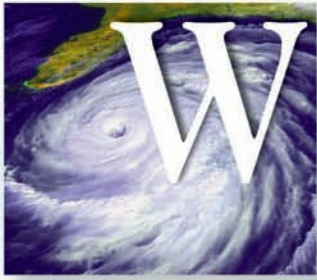
Many policies provide that an association may not settle a claim without the insurer’s consent. Policy-holders should insist on a clause that consent cannot be “unreasonably withheld.” Conversely, some D&O policies provide that if an insurer wishes to settle but a policyholder does not, settlement is subject to a hammer clause; the insurer’s exposure is capped at the amount of the rejected settlement.

#### **Conclusion**

A directors and officers liability policy is essential to protect persons willing to serve on a condominium board of directors. Before purchasing a policy, a condominium association should carefully read the terms and exclusions and negotiate for the type and amount of coverage it deems necessary. For most associations, the value provided by D&O insurance will be in peace of mind and encouraged service of high caliber directors; however, a good D&O policy could be invaluable to the association and homeowners alike if litigation does occur.

*William F. “Chip” Merlin, Jr., Esq. is the founder and president of Merlin Law Group, P.A. in Tampa and Coral Gables, FL.*

*For more information, please visit [www.merlinlawgroup.com](http://www.merlinlawgroup.com). ■*



# When Disaster Strikes Your Community, Where Will You Turn?



**A**t Merlin Law Group, we understand that property insurance issues can be complicated; especially when it comes to condominiums.

When disaster strikes, knowing how to navigate the insurance claim process can be difficult. Decisions made in the earliest stages of a claim can directly impact its outcome.

That's why Merlin strives to provide condominium Property Managers, Board Members, owners, and staff with much needed peace of mind by assisting in the burdensome task of negotiating an insurance claim.

For over twenty years, Merlin Law Group has represented communities like yours in disputes with insurance companies.

We would be pleased to do the same for you.

**William F. "Chip" Merlin, Jr.**

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