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Does a Request for Resolution / ADR Constitute a Claim Under the Board's D&O policy?

By Timothy Cline, CIRMS, Timothy Cline Insurance Agency, Inc.

The California Civil Code requires an individual unit owner to demand Alternative Dispute Resolution (ADR) as a prerequisite to a lawsuit if they have issues with their Association and they want to enforce their association's governing documents or the Davis-Stirling Act. In California, ADR is described as follows (per California Civil Code §5925):

> (a) "Alternative dispute resolution" means mediation, arbitration, conciliation, or other nonjudicial procedure that involves a neutral party in the decision making process. The form of alternative dispute resolution chosen pursuant to this article may be binding or nonbinding, with the voluntary consent of the parties.
>
> (b) "Enforcement action" means a civil action or proceeding, other than a cross-complaint, for any of the following purposes:
>
> (1) Enforcement of this act.
>
> (2) Enforcement of the Nonprofit Mutual Benefit Corporation Law (Part 3 (commencing with Section 7110) of Division 2 of Title 1 of the Corporations Code).

Other interesting articles related to Directors and Officers insurance:

When is a Claim a Claim?

The reporting of a claim, or potential claim, is critical.

(Note: Original release date was prior to the Jan '14 changes in the CA Civil Code - Section 1369.510 is now 5925)

(3) Enforcement of the governing documents.

The board effectively has little choice in this process. It must agree to ADR if such a demand is made by the unit owner. If the board refuses to participate in the process and the case proceeds to court, the court can take that into consideration when it comes to the award of attorneys' fees. For example, if the association prevails at trial but did not mediate, the court may decide not to award all or perhaps any of the fees incurred feeling that the dispute would have been resolved at mediation.

For associations who have purchased the broader Directors & Officers Liability coverage, it's very likely such a demand would fall under the definition of a "claim" and a board of directors should be advised to immediately put the D&O carrier on notice. But would a notice of claim mean that the board should expect defense/legal counsel to be provided by the D&O carrier to defend the Board?

While it is difficult to definitively address every scenario, particularly where we do not have an actual claim to evaluate, we can offer these general comments.

A request for ADR can qualify as a Claim under the D&O Policy as long as it's a written demand for monetary or non-monetary relief or arbitration alleging a wrongful act by the board of directors. To benefit from the D&O coverage, the ADR request also has to be timely noticed during the policy period (and of course not otherwise excluded - i.e., bodily injury/property damage, etc.). However, an ADR request may not always rise to the level of a Claim particularly if it's an informal conciliation or other non-judicial procedure. Each case has to be evaluated on its own merits.

So our view is if it's a formal written request for ADR and it's reported in a timely fashion, there's at least a reasonable chance the D&O carrier would appoint counsel.

Finally, if the insured association requests counsel to assist on an ADR matter that technically may not qualify as a Claim, the insurer may still offer to appoint counsel if that may assist the association in resolving the matter and avoiding the expenses of litigation.

Of course, every claim has its own set of facts and it is impossible to make a broad statement regarding every ADR request and the response from the Association's

The Evolution of Directors and Officers Policies

Not all D&O policies are created equal.

D&O carrier. For example, package carriers who write D&O coverage as a modest endorsement to their policy often exclude coverage for non-monetary damages. These carriers will decline to provide defense when the dispute is a purely non-monetary issue such as an aesthetics-based challenge to Architectural Review Committee decision where non-compliance with existing ARC guidelines is being argued.

The best advice is to put the D&O carrier on notice and let the adjuster determine their participation level, if any, in support of a request for ADR. Failing to put the carrier on notice could have a catastrophic result. If the ADR is unsuccessful, the association does not want to potentially lose carrier-provided defense and indemnity for the resulting lawsuit simply because of a "late notice" -- for failing to put the D&O carrier on notice when the dispute first gave rise (when the homeowner requested ADR).

Special thanks to David C. Swedelson, Esq., of SwedelsonGottlieb, for his input.

By Timothy Cline, CIRMS

Timothy Cline Insurance Agency, Inc.