
CLIENT ADVISORY

DECEMBER, 2002

Ganfer & Shore, LLP will be hosting another in our series of breakfast panel discussions addressing topics that, we believe, are of significant interest to cooperatives, condominiums and real estate owners. The topic of our next seminar will be how to protect against discrimination claims in the applicant approval process. This discussion will be held on Wednesday, January 22, 2003 from 8:00 A.M. to 10:00 A.M. in the New Harmonie Room of the Harmonie Club, 4 East 60th Street, New York, New York. If you plan to attend, please either call Amarilys Garcia of our office at 212-922-9250, ext. 262, or send a confirming e-mail to her at agarcia@ganshore.com by January 17, 2003.

PRESIDENT BUSH SIGNS THE TERRORISM RISK INSURANCE ACT

The following article was graciously contributed by Andrew H. Marks, Pres./CEO of MLW Services, Inc.

September 11th was an enormous blow to an already weakening insurance market with an estimated \$50 billion of covered losses. With rates in the New York Metropolitan area sometimes doubling or tripling, the property insurance market has hardened to stone. Accordingly, after a great deal of lobbying by real estate and financial interests, the *Terrorism Risk Insurance Act* was passed by both the House and Senate and signed into law by President Bush on Tuesday, November 26, 2002. This legislation was designed to facilitate the creation of an insurance market to cover losses caused by acts of terrorism which had virtually disappeared as a result of reinsurers excluding Terrorism coverage from their contracts and treaties and passing these exclusions along to the general market. The *Act* obligates the Federal government to pay 90 percent of all covered insured loss experienced by any insurer after certain claim thresholds are exceeded, thereby defining the boundaries of risk for insurers if only for 3 years, the effective term of the bill. At this time nobody knows exactly how the marketplace will respond to this legislation. Certain impacts were immediate because Terrorism exclusions incorporated in so many policies were automatically voided pending the acceptance or rejection by consumers of an offer for the coverage. The next 90 days will tell the tale as to the pricing that companies will provide to insureds, and insureds' acceptance or rejection of that pricing. It is our feeling that new rates will be competitive with the rates previously provided by the stand-alone underwriters providing separate Terrorism coverage.

INSURER MUST DEFEND SUIT DESPITE EXCLUSION FOR INTENTIONAL ACTS

Board members are occasionally named as defendants in suits brought by shareholders or potential purchasers in which they are alleged to have defamed the shareholder or potential purchaser in the exercise of their duty as a board member. Some insurance policies specifically exclude libel, slander, and defamation or similar acts. The courts have generally enforced those exclusions, and the insurer would have no duty to defend the board member. However, some insurers do not have specific exclusions and rely upon exclusions referring to "intentional" acts to try to exclude coverage under their policies. The decision of the New York State Court of Appeals, in Town of Massena v. Healthcare Underwriters Mutual Insurance Co. (NYLJ, 9/18/02, p. 18, col. 6), reinforced existing case law which placed the burden squarely on the insurance companies to prove that, as a matter of law, there is no possible factual or legal basis on which the insurer might eventually be obligated to indemnify the insured under any policy provision. In Massena, a doctor ("Plaintiff") brought an action against the Board of Managers and Executive Committee of a local hospital. There were several insurance carriers providing coverage to the

hospital and each one sought to avoid defending the board members against the defamation claim by the Plaintiff. The board members and the hospital filed a separate action for a declaration by the court requiring the insurance companies to defend them under the existing policies. Those insurers with specific exclusions were found to have no duty to defend the board members. The one company with the general exclusion for "intentional" acts was held to have a duty to defend the board members. The court noted that whenever allegations in a complaint state a cause of action that gives rise to a reasonable possibility of recovery under the policy, the insurer is required to defend the entire action. The burden rests on the insurance company to demonstrate that the allegations can be interpreted only to exclude coverage, and the right to coverage exists even if debatable theories are alleged. This case offers important guidance to board members in the event that an insurance carrier seeks to deny coverage based upon a policy exclusion. A court's interpretation of policy language may differ from the insurers and result in available coverage and significant savings. We would also suggest that you review your existing policies to see if there is a specific exclusion for libel, slander and defamation and, if so, that an effort be made to delete any such exclusion.

BOARDS' ACTIONS REMAIN SUBJECT TO CHALLENGE

We continually stress to board members that although the Courts have generally given great deference to the decisions of a cooperative corporation's Board of Directors, board members should not mistakenly presume that the Court's deference is unlimited. When a director acts in a manner that is contrary to the duty to act fairly, impartially, and in the best interests of the corporation, courts will review claims of misconduct. In addition, if a board member's breach of fiduciary duty is found to be sufficiently egregious, punitive damages may be recoverable over and above damages calculated to compensate a Plaintiff for his or her proven loss. Another recently reported case has come to our attention in which a board may have failed to act fairly, and then tried to "cover its tracks". In Louis and Anne Abrons Foundation, Inc. v. 29 East 64th Street Corporation (2002 N.Y Slip Op. 06292, August 29, 2002), the Appellate Division, First Department, reviewed a board's adoption of a sublease fee. This cooperative corporation (the "Coop") was composed of 50 units, with 7 units being commercial units owned by the Plaintiff. The Plaintiff challenged the Coop's imposition of a sublet fee, alleging that the sublet fee was discriminatory, directed solely at Plaintiff, and enacted in bad faith and in violation of board members' fiduciary duty to treat shareholders fairly and evenly. Plaintiff brought to the Court's attention that at the time that the sublet fee was adopted, the Coop prohibited subletting of residential units. The Coop submitted evidence showing that the subletting policy had been revised, and that the fee would thus apply to all shareholders. However, the court noted that the only sublet of a residential unit that had been approved was of a board member's units, which was approved after the commencement of the Plaintiff's action, and coincidentally the revised policy was adopted on the same day that the Plaintiff submitted reply papers to the Appellate Court. The Court found these facts and coincidences sufficient to raise a question of fact as to the propriety of the board's actions, and overturned the lower court's grant of summary judgment to the Coop.

CARBON MONOXIDE DETECTORS NOW REQUIRED

Section 378(5)(a) of the Executive Law of the State of New York has been amended to require that an operable carbon monoxide detector be installed in every one or two-family dwelling or any cooperative or condominium dwelling constructed or offered for sale after November 27, 2002, the effective date of the revised subdivision.

To our clients and friends, we extend our best wishes for a healthy and happy holiday season and New Year.