

No Coverage Under D&O Policy for Property Damage or for Amounts Incurred in Connection with Equitable Relief

January/February 2010

The United States District Court for the Middle District of Tennessee has held that no coverage existed under the D&O provisions of a homeowners association's policy for loss sustained due to the association's obligation to repair structural defects in its members' townhouses for two independent reasons: the policy's property damage exclusion applied, and the association's obligation to make the repairs stemmed from a state court declaratory judgment and thus were not "damages" the insured was "legally obligated to pay" as required by the policy. *Huntingdon Ridge Townhouse Homeowners Ass'n, Inc. v. QBE Ins. Corp.*, 2009 WL 4060458 (M.D. Tenn. Nov. 20, 2009). In so ruling, the court rejected the insured's argument that the property damage exclusion applied to "claims" but not "suits," and held that the policy was otherwise unambiguous.

One of the homeowner's association members had previously sued it over defective construction. A state court entered a declaratory judgment that the association bylaws obligated the association to make certain repairs. The association filed a claim with the insurer under its condominium association insurance policy, and the insurer denied the claim. The relevant policy language from the D&O portion of the policy obligated the insurer to pay "all 'loss' [the] insured becomes legally obligated to pay as damages" The policy defined "loss" as "the damages the insured is legally obligated to pay because of judgment or settlements arising out of 'claims' or 'suits'" The policy also stated that it did not "apply to any 'claim' or 'suit' . . . [w]here all or part of such 'claim' is directly or indirectly, based on, attributable to, cause by, arising out of, resulting in or relating in any way to . . . 'property damage'"

The court held that the state declaratory judgment action was "clearly" related to property damage under the policy. The association argued that the property damage exclusion applied only to "claims" and not "suits" because the operative language describing the exclusion only used the former term. The court rejected that argument, reasoning that the specified language was a sentence fragment that "does not make sense unless it is read in conjunction with the relevant antecedent language," which used both terms. The court accordingly held that the exclusion applied to suits as well as claims and barred coverage for the association's loss.

The court also concluded that the policy did not cover the insured's claim because the state court declaratory judgment action did not award damages. The policy defined covered losses as "the damages the insured is legally obligated to pay." The court noted that while the policy did not define "damages," legal precedent showed that in the insurance context "damages" means legal damages, not equitable relief. The policy thus did not provide coverage for the association's obligations resulting from the unfavorable declaratory judgment.