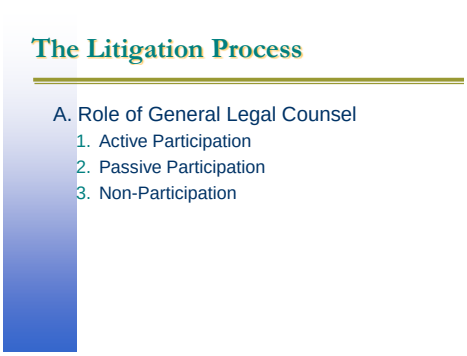
III. NAVIGATING THROUGH LITIGATION

One of the most important and often times misunderstood areas of responsibility of an association general counsel is the general counsel's role in litigation when defense counsel has been appointed by the association's insurance carrier. The following overview will attempt to touch upon various areas of general counsel involvement and explain the complexities of civil litigation, the discovery process, general representation during litigation and settlement.



A. ROLE OF GENERAL LEGAL COUNSEL LITIGATION

The following discussion is premised upon the understanding that the association's insurance carrier has assigned insurance defense counsel to represent the association, as well as possibly the association's management company in litigation. At the outset, several items need to be reviewed and considered in determining general counsel's role in the litigation when insurance defense counsel has been appointed. First and foremost is whether or not the insurance company has issued a reservation of rights on the lawsuit. Generally, a reservation of rights is a position taken by the insurance company based upon an analysis of the allegations set forth within the complaint and over viewed with coverages afforded under the insurance policy. Reservation of rights letters can run the gamut from being relatively minimal in their reservation, i.e., the vast majority of the claims are covered, to quite extensive wherein there may be only a thread of a claim in the complaint that is requiring the insurance company to afford a defense. In such cases, the reservation may be so significant that there may not be any duty to

ultimately indemnify or pay any judgment in the event of an adverse result. Attached is an exemplar of a reservation of rights letter.

Depending upon the extent of the reservation or rights letter issued by the insurance company, the association may have a right to demand that cumis counsel be appointed to defend the association. Cumis arises when reservation of rights may create a conflict between the insurance company and the insured defendant. In such cases, there is often a concern that the defense afforded by the insurance company through the insurance defense counsel could be guided or geared in such a way as to avoid or destroy coverage. In such circumstances, the insured, i.e., the homeowners association can demand that cumis be appointed, i.e., counsel of the association's choosing to be paid for by the insurance company. There are certain limitations to cumis counsel.

Assuming that cumis is not at issue with respect to defense and the litigation coverage, the next item that general counsel must consider is whether or not general counsel's role should be active, passive or non-participatory.

1. Active Participation:

Active participation of general counsel often arises when there is either a significant reservation of rights, but may not arise to a cumis counsel level, and/or there is concern that the defense attorney assigned may not have the appropriate experience and knowledge to afford a thorough defense on behalf of the association. Items to look at is whether or not the defense counsel being assigned is an in-house defense attorney, i.e.

actually employed by the insurance company (which is often the case), or an outside panel counsel. Often times, outside panel counsel are actually paid a flat fee for a defense of the case, regardless of the amount of work required and this kind of fee arrangement can impair the defense that is being afforded to the association. General counsel may wish to be more active in the cases where the amount of the claim exceeds the policy limits or can have far reaching ramifications to the association as a whole if an adverse judgment arises. In such cases, active participation would generally include reviewing of all communications by and between the defense counsel and the insurance company; meeting and conferring with defense counsel in creating a defense and discovery plan; providing ideas on how to litigate the case, etc.

2. Passive Participation

In the event that the reservation of rights issued by the carrier is relatively minimal in nature and, if the defense counsel assigned appears to be knowledgeable and experienced in the defense of associations, then the association may make a decision to have general counsel's role be more passive in its participation. Again, we would recommend that defense counsel provide copies of any and all communications by and between itself and the insurance carrier to the general counsel. In addition, there will likely be some participation between general counsel and defense counsel in fully preparing the defense; however, general counsel's role would be far more limited.

3. Non-Participation

In the event that there is no reservation of rights and counsel that has been assigned appears to be knowledgeable in the practice field, the general counsel's role would likely be extremely minimal and again may be limited to simply reviewing the correspondence by and between defense counsel and the insurance company, possibly interacting with general counsel if and when a settlement is reached.

Overall, a key role of the general counsel in litigation, whether it be active, passive or relatively non-participatory is to review any proposed settlement to ensure that:

i. It is appropriate for the association, i.e., will not have ramifications for the association outside of that which is specifically agreed to as part of the settlement.

ii. It will not open the association up to further and additional claims.

iii. It is a full and complete release pursuant to *Civil Code* Section 1542.

iv. It will allow the association and its members to make whatever appropriate disclosures are necessary and compliant with California law.

Also, and though it is rare, there are times that even if a cumis situation does not exist that the insurance company will hire general counsel to act as the defense attorney based upon the general counsel's expertise and

knowledge of the issues confronting the association and the desires of the Homeowners association. Again, this is rare, but certainly not unheard of; however, general counsel would need to follow the administrative requirements of the insurance carrier, including billing practices, fees, reporting, etc.

B. LITIGATION PROCESS

The litigation process is often time long and laborious. The purpose of the discovery process is an attempt for both sides, i.e., both the association, as well as the Plaintiff to attempt to determine information from the other side to either prosecute or defend the claim. Discovery can take many forms as set forth below:

The Litigation Process

B. Litigation Process
1. Interrogatories
2. Requests for Admissions
3. Requests for Production of Documents

1. Interrogatories

Code of Civil Procedure Section 2030.010 et seq. allows parties to propound both Special Interrogatories, as well as Form Interrogatories. Interrogatories allow one side to ask the other side questions which include, but are not limited to, the identification of witnesses, documentation, intentions, basis of claims and damages, etc. in which either the complaint or defense is based upon.

2. Requests for Admissions

Requests for Admissions are allowed under *Code of Civil Procedure* Section 2033.010 et seq. Requests for Admissions are generally an attempt to have one party have the other either admit or deny certain statements

and/or contentions. Requests for Admissions can be a very useful tool if implemented and asserted properly and it can be extremely dangerous if a party fails to timely respond to the Requests for Admissions. Requests for Admissions are often times used for setting up a Motion for Summary Adjudication of Issues, a Motion for Summary Judgment, i.e., dispositive motions on the case.

3. Requests for Production of Documents

Requests for Production of Documents are allowed under *Code of Civil Procedure* Section 2031.010 et seq. This discovery tool allows the parties to seek documents or other materials from the other parties. In the context of an association, such documents generally include, but are not necessarily limited to, minutes, agendas, financial records, budgets, non-privileged consultant reports, newsletters, communications between the board and Management, etc. With respect to Requests for Production of Documents, it is imperative that counsel review the documents carefully to determine whether or not certain items should be redacted including, but not limited to, private information such as Social Security numbers, credit card numbers, drivers license numbers, etc.

Overall, with respect to written discovery, if you have an insurance company supporting the association, one method of attacking the plaintiff is to "paper" the other side. Specifically, written discovery becomes a war of attrition and the association has the insurance company behind it to try to attack

the plaintiff and force them to expend significant time, money and energy on the case in the hopes of softening them for an ultimate settlement. At times, this may require the active participation of the general counsel to help push the defense counsel forward in propounding not only the appropriate discovery, but the volume of discovery that may be beneficial in softening the plaintiff up.

Please note: the manager will need to be sensitive to any request for documents from a plaintiff that is also a homeowner/member for documents requested pursuant to Civil Code Section 1365.2. Any such request for association records received during litigation where the Plaintiff is also a member of the association needs to be sent to the association counsel and general counsel for review before the documents are issued. As this Civil Code Section has narrow times (5,10 and 30 days) to respond it is important that such a request be promptly forwarded to counsel for review.

C. RESPONDING TO DISCOVERY REQUESTS

It is good practice to have defense counsel prepare draft responses to the discovery and provide same to the association for review and supplementing. A final response can then be prepared by defense counsel and provided to the client for a final review and, if it is acceptable, verified by the association.

It is important to understand that the board of directors should never execute a verification with respect to written discovery until such time

as they are provided with the final responses to the discovery. Lazy counsel will often times provide a verification to an insured, without providing them with the proposed response and simply request that the client execute the verification after which time they attach it to the discovery response that the insured has never seen. Such conduct can often be devastating at the time of a deposition when the deponent is questioned on discovery responses that they had never seen before but had verified under penalty of perjury.

Further, it is our strong recommendation that defense counsel meet with the board and the manager, if appropriate, several times during the litigation. Defense counsel should meet early on in the litigation to get an understanding from the board and management of what there understanding of the facts are with respect to the case and help to commence the creation of a defense position. Such an early meeting also helps create a relationship between the association and counsel which will be necessary as the case progresses. Unfortunately, this early meet and greet is often ignored by defense counsel who may be in litigation for 50 or more cases at one time. This is a time where general counsel may get involved to try to help promote an early meeting.

D. ORAL DISCOVERY

Oral discovery generally deals with depositions. Depositions can be of various individuals and entities including, but not limited to, representatives of the board of directors, a person most knowledgeable from the board, the manager, possibly vendors who have worked on the job that may be relevant to the complaint,

etc.

1. Preparation

It is very important that the client be prepared for their deposition. Generally, multiple members of the board of directors will ultimately be deposed so it may be beneficial to have a general meeting of the board members who will be deposed approximately two weeks before the deposition. During this time, general instructions can be provided by defense counsel and, if the association wishes general counsel to be involved, further instruction and hand holding can occur during that time. Role playing and question and answers are often beneficial during these sessions so as to get the board members thinking about the types of questions that they will likely encounter, how to deal with them, understanding appropriate responses that are generally short and concise versus providing narrative responses and taking away some of the anticipated fear and nervousness that occasions a deposition. As each individual board members deposition nears, it is then appropriate to have a private session with each board member for approximately one to two hours to go over their specific deposition testimony and put them at ease before the deposition. It is generally recommended that this final pre-deposition meeting occur at least one or more days prior to the deposition, as opposed to the morning of the deposition.

Two axioms tend to apply at deposition, i.e. as the Marines would say "sweat more and bleed less," i.e. be fully prepared in advance

so the actual deposition goes smoothly and do a deposition like a football game, i.e. only give up one yard at a time in answering questions as opposed to a long yard gain.

2. CEO Involvement

Often times, not only will the board and an individual manager be deposed, but also a management company's CEO/President. With respect to the on-site or portfolio manager and CEO/President, it is our general opinion that the insurance defense counsel does have an obligation to defend them during deposition due to the fact that they are an agent for the association; there is likely an indemnity agreement that exists between the management company and the association and; because of the theories of Respondeat Superior that apply between a manager and the association. As stated above, we would recommend that the manager be pre-deposed privately so as to provide them an opportunity to state what they need to say outside of the presence of the board and then the defense counsel can determine how best to use the manager's testimony during deposition.

The management company CEO may not have actual knowledge of the event that has given rise to the lawsuit, but often times are deposed in order to help determine the pattern and practice of the management company in handling certain claims. More succinctly, how have the individual managers been trained or told to react in the event that certain events arise? This could include issues such as notification, reporting, dealing with potentially dangerous

conditions that come to exist, etc.

E. EXPERT PHASE OF LITIGATION

A key element in defending a claim against the association is having appropriate experts evaluating the case and rendering opinions evidencing that the association's conduct is appropriate, non-negligent, potentially not in breach of their fiduciary obligations, etc. Often times a business judgment rule defense is also applied to a board of directors indicating that the decisions made by the board of directors, though not necessarily perfect, were made reasonably and in good faith and that such decisions were based upon reliance of the advice provided by professionals within the industry, i.e. general counsel, accountant, reserve study company, etc. Expert testimony, i.e. recognized professionals within the industry who are not Associated with the case at hand, i.e. they do not have involvement in the underlying facts that gave rise to the lawsuit, are generally employed to provide expert testimony to show that the conduct of the board was in fact reasonable and appropriate.

It is generally advisable to have the insurance company retain expert witnesses early in the litigation. By doing so early, the association may have the greatest opportunity of obtaining the best witness in the industry to work on their behalf. This is especially important in those areas where there may be very few "qualified" experts. In addition, early obtainment of an expert witness could help a defense attorney to formulate how to defend the case, litigate the matter and provide better overall evaluation of the case to both the association and to the insurance carrier.

Further, and as stated earlier, to the extent that general counsel can convince the insurance company to retain multiple experts in various disciplines who can provide valuable testimony and opinion on the issues at hand may be a benefit in the defense of the association, especially in again forcing plaintiff to incur additional costs and expenses by potentially hiring additional experts to counter the association's expert testimony, i.e. making the litigation expensive for the plaintiff to prosecute which may help lead to a satisfactory resolution on behalf of the association.

F. LEGAL REPRESENTATION OF MANAGEMENT

At the outset, defense counsel must first determine whether or not the lawsuit is against the association or the association and the management company. Assuming that both the association and management have been named in the lawsuit, a review of the management contract by general counsel is appropriate to confirm the fact that an indemnity agreement likely exists between the association and management company. Assuming that a properly executed indemnity agreement exists and that the claim is being brought by a third party, i.e. it is not a claim by the management company against the association for, as an example, breach of contract, then the tendering of the lawsuit to the carrier by general counsel should be demanding that the carrier assign defense counsel to represent both the association and management company. On those rare instances where there may be a potential conflict or finger pointing between the association and management, it may be necessary that separate

counsel be assigned. However, except in the rare circumstance where there is clear egregious conduct being performed by either the association or management, it is typically beneficial to have the association and management represented by one counsel, the defense coordinated and avoid finger pointing. More succinctly, "circle the wagons." Where necessary a written waiver of the conflict may need to be signed by the association and the management company which may also require independent consultation regarding the waiver. In the event that both the management company and the association are named defendants and there is one law firm assigned to represent both, then the attorney client privilege applies between those parties with respect to communications with the attorney.

In those instances where the association is named in the lawsuit, but not the management company, but the manager is going to be a non-party percipient witness, there is a division of thought as to whether or not those conversations between the attorney and manager are in fact privileged under the attorney/client privilege. Generally, we believe that the privilege may apply in those instances where the communication is between the attorney and the manager or the attorney, manager and the board where the information being provided to and from the attorney is for the purposes of litigating the case. In those cases, the manager is a necessary third party of the client, i.e., the association, and is therefore important to include in the communications, thus wrapping the privilege around the manager. It is important to understand that in certain cases, opposing counsel will attempt to demonstrate that the manager is simply a witness, not a "client," and

therefore should not be protected under the attorney-client privilege and thus general counsel and defense counsel need to be prepared to fight that battle if it occurs.

G. OTHER LITIGATION EVENTS

1. Mediation

At an early stage in the litigation the court or the parties will likely suggest or be ordered to mediation. It is important that the board of directors be prepared for the mediation with a clear understanding of the issues and the damages. In some instances the insurance company will request that they be on telephone standby for a mediation. That should be reviewed based on the issues presented in the case and the amount of damages. In many instances having the insurance company representative in person at the mediation can improve the possibility of a settlement. It is easier to deny a request for additional funds if you are on the telephone rather than in front of the mediator and the insured.

2. Subpoenas

A subpoena is generally issued to a non-party for the purposes of compelling their appearance at deposition and may or may not include a demand that documents also be produced at that time. In the event that the management company is not a party to the case and they are subpoenaed as a witness for deposition, that subpoena should immediately be provided to defense counsel. Defense counsel, as stated above, should defend the manager at the time of the

deposition based upon issues of contractual indemnity, agency and Respondeat Superior. Also, the documents to be produced should be provided to defense counsel in advance for purposes of review and determination of whether or not various privileges or privacy issues may arise. In such events, it may be appropriate to file Motions to Quash or Protective Orders.

3. Emails

Also, an issue that often arises as part of a subpoena for a non-party manager or under a Request for Production of Documents to a party is emails. Though this can be a topic in and of itself, suffice it to say that emails should never be sent that cannot be defended by the author of the email at the time of a deposition. Name calling, inappropriate statements about members or board action, and off color remarks have no place in the emails since they are discoverable written records of the association.

4. Site Inspections/Access to Property

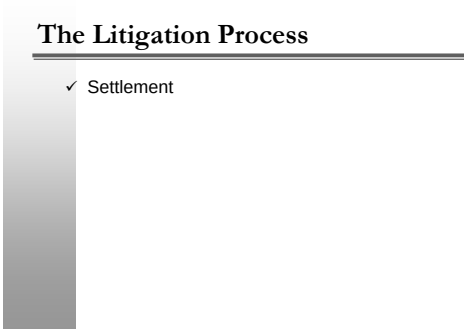
Generally in a claim for personal injury or property damage, a site inspection will be demanded by the Plaintiff. Such site inspections are allowed; however, during such site inspections, it is imperative that counsel for the Plaintiff be advised that they are not to speak to the manager or any homeowners at the site other than for minor pleasantries. You need to avoid turning the site inspection into a free discovery tool wherein the opposing party may try to determine issues of prior notice, potentially learning of other witnesses, and if the

association is a Plaintiff, potentially learning of statute problems, etc.

5. Trial Testimony

As most people are aware, the vast majority of cases settle. Settlement often occurs as one party learns during the litigation that their position is not as strong as they once believed, thus a settlement is appropriate. In other instances, costs become prohibitive thus driving an economic resolution. Also, people grow tired and weary of litigation and uncertainty may drive the parties towards resolution. However, in those rare instances where settlement does not occur, members of the board of directors and management must be prepared to appear and testify at trial. This can be time consuming and nerve racking for all involved; however, testimony of any given board member or manager could be the turning point as to whether or not the association is successful or is defeated during a trial.

H. SETTLEMENT



If the parties are able to reach a settlement, it is imperative that general counsel be intimately involved in the drafting and ultimate approval of the Settlement Agreement and Release. Defense counsel is most interested in settling the case and getting the insurance company off the clock in time and expense. However, due to

the nuances that are involved with respect to homeowners associations including the very important distinction between the association as a corporate entity versus the individual members, as well as disclosure requirements that the association has, it is imperative that the Settlement Agreement be drafted to protect everyone's interest. Further, in the event that the matter is proceeding towards trial and the carrier is taking a hard line towards settlement, but there is a settlement demand within the association's policy limits, often times the association is better served by having general counsel issue a demand letter to the carrier demanding that they settle the matter within policy limits or, if they fail to do so, setting forth the fact that the association will look towards the carrier to pay the entirety of the judgment even if it exceeds the policy limits. Though there is no consent clause in the association's insurance policy and the carrier has the discretion to settle or not settle the case, it is imperative that pressure always remain on the carrier by the general counsel to attempt to protect the association to the fullest extent possible.

Thank you!