The Role of Liability Insurance Policy Notice Conditions in Laboratory Liability Claims

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I. INTRODUCTION[2]

There is no special magic to the application of liability insurance policy notice provisions to laboratory liability claims. In a laboratory liability claim, like all other liability insurance claims, notice is an important component of the insurance contract. An insured's notice typically initiates the claims handling process. The notice provision specifies when an insured must inform its insurer of a claim. In general, the purpose of a notice provision is to provide the insurer with the opportunity to conduct a timely investigation and to prevent fraudulent claims. It is important for insureds to recognize that the notice requirement is not the beginning of an adversarial relationship. To the contrary, prompt and effective notice is intended to be the first step in a cooperative exchange of information consistent with the terms and provisions of the insurance contract.

Insurers frequently contend that the failure of their insureds to provide timely notice results in forfeiture of coverage. However, the effect of late notice varies from jurisdiction to jurisdiction. For example, some states provide that an insurer cannot rely on a late notice defense to avoid coverage unless the insurer can prove that the insured's untimely notice prejudiced the insurer.

This paper discusses the fundamentals of liability insurance policy notice provisions, the question of when an insured's notice obligation generally arises, and the consequences of late notice.

II. NOTICE CONDITIONS IN LIABILITY INSURANCE POLICIES

Historically, primary liability insurance policies typically contained notice provisions similar to the following:

Insured's Duties in the Event of Occurrence, Claim or Suit.

> (a) In the event of an occurrence, written notice containing particulars sufficient to identify the insured and also reasonably obtainable information with respect to the time, place and circumstances thereof and the names and addresses of the injured and of available witnesses shall be given by or for the insured to the Company or any of its authorized agents **as soon as practicable**.
>
> (b) If claim is made or suit is brought against the insured, the insured shall immediately forward to the Company every

[2] DISCLAIMER: This paper provides a general overview of some legal precedents involving insurance coverage issues. The law in this area is constantly changing. The reader should not rely solely on this paper in making significant legal decisions. In order to obtain a more complete picture of the applicable law impacting a particular matter, it is recommended that the reader seek legal advice.

demand, notice, summons or other process received by him or his representative.

(c) The insured shall cooperate with the Company and, upon the Company's request assist in making settlements, in the conduct of suits and in enforcing any right of contribution or indemnity against any person or organization who may be liable to the insured because of injury or damage with respect to which insurance is afforded under this policy; and the insured shall attend hearings and trials and assist in securing and giving evidence and obtaining the attendance of witnesses. The insured shall not, except at his own cost, voluntarily make any payment, assume any obligation or incur any expense other than for first aid to others at the time of accident.

More recent variations of primary liability coverage contain notice provisions consistent with the following policy language:

Duties In The Event Of Occurrence, Offense, Claim Or Suit

a. You must see to it that we are notified **as soon as practicable** of an “occurrence” which may result in a claim. To the extent possible, Notice should include:

(1) How, when and where the “occurrence” or offense took place;

(2) The names and addresses of any injured persons and witnesses; and

(3) The nature and location of any injury or damage arising out of the “occurrence” or offense.

b. If a claim is made or “suit” is brought against any insured, you must:

(1) Immediately record the specifics of the claim or “suit” and the date received; and

(2) Notify us as soon as practicable.

You must see to it that we receive written notice of the claim or “suit” as soon as practicable.

c. You and any other involved insured must:

(1) Immediately send us copies of any demands, notices, summonses or legal papers received in connection with the claim or "suit";

(2) Authorize us to obtain, records and other information;

(3) Cooperate with us in the investigation or settlement of the claim or defense against the "suit"; and

(4) Assist us, upon our request, in the enforcement of any right against any person or organization which may be liable to the insured because of injury or damage to which this insurance may also apply.

d. No insured will, except at that insured's own cost, voluntarily make a payment, assume any obligation, or incur any expense, other than for first aid, without our consent.

For larger risks, insureds commonly purchase excess or umbrella liability insurance. These types of policies often contain different notice provisions than the primary policies issued to insureds. Excess insurance notice provisions commonly include language such as:

> Whenever the Insured has information from which the Insured **may reasonably conclude** that an occurrence covered hereunder involves injuries or damages which, in the event that the Insured should be held liable, is **likely to involve this Policy**, notice shall be sent to the company **as soon as practicable**, provided, however, that failure to give notice of any occurrence which at the time of its happening did not appear to involve this Policy but which, at a later date, would appear to give rise to claims hereunder, shall not prejudice such claims.

Thus, a significant factor in evaluating when notice should be given to an excess insurer is whether the occurrence has the potential to involve damages in an amount sufficient to reach the excess insurance policy layer of coverage.

III. THE ROLE OF NOTICE REQUIREMENTS IN LIABILITY POLICIES

The purpose of a notice requirement is to provide insurers with an adequate opportunity to: (1) investigate claims brought against their policyholders, (2) to prevent

fraudulent claims, and (3) to determine their rights and liabilities before they are obligated to pay a claim. *Couch on Insurance 3d,* § 186:14.

The requirement of timely notice of an accident gives the insurer an opportunity to make a timely and adequate investigation of all the circumstances. This concept of timeliness has been widely addressed. For example, the Tennessee Supreme Court observed in *Alcazar v. Hayes*, 982 S.W.2d 845, 849 (TN 1998), that:

> An adequate investigation often cannot be made where notice is long delayed, because of the possible removal or lapse of memory on the part of witnesses, the loss of opportunity for examination of the physical surroundings and making photographs thereof for use at the trial, and the possible operation of fraud, collusion, or cupidity. Such a requirement tends to protect the insurer against fraudulent claims, and also against invalid claims made in good faith. If the insurer is given the opportunity for a timely investigation, reasonable compromises and settlements may be made, thereby avoiding prolonged and unnecessary litigation.

In return for its agreement to defend and indemnify its insured, an insurer bargains for the right to prompt notice so that it can conduct activities to avoid or minimize liability. *See*, *e.g.*, *Commercial Union Insurance Company v. International Flavors & Fragrances, Inc.*, 822 F.2d 267 (2d Cir. 1987). By requiring that they be provided timely notice of an accident or an occurrence, insurers guarantee to themselves the ability to investigate the underlying facts and circumstances of a loss while the evidence is fresh. *Id*. at 271. Notice provisions allow an insurer to become aware of the facts and circumstances of the occurrence giving rise to the insured's claim early enough so that the insurer can have a meaningful opportunity to investigate. *Ormet Primary Aluminum Company v. Employers Ins. of Wausau*, 88 Ohio St. 3d 292, 725 N.E. 2d 646 (OH 2000). *See also Phico Ins. Co. v. Providers Ins. Co.*, 888 F.2d 663, 668 (10th Cir. 1989) (notice provisions are intended to give the insurer an opportunity to make a "timely and adequate investigation in order to form an intelligent estimate of its rights and liabilities").

The requirement of timely notice is additionally important where an insurer owes a defense obligation to its insured. By obtaining immediate written notice of any claim or suit against the insured, the insurer is afforded the opportunity to retain counsel and avoid improper handling of its insured's defense in the early stages of litigation that could compromise or prejudice the handling of the case thereafter.

Many courts have concluded that notice provisions are not mere technical requirements, but have declared them to be valid conditions precedent to the commencement of an insurer's contractual duties. *See*, *e.g*., *Commercial Underwriters Insurance Company v. AIRES Environmental Services, Inc*., 259 F. 3d 792 (7th Cir.

2001); *U.S. Fire Insurance Company v. Green Bay Packaging, Inc.*, 66 F. Supp. 2d 987 (E.D. WI 1999); *Northbrook Property & Casualty Insurance Co. v. Applied Systems, Inc.*, 313 Ill.App.3d 457, 729 N.E.2d 915, 920-21 (IL 2000).

IV. "CLAIMS-MADE" POLICIES DISTINGUISHED

There is an important difference between the notice requirement in a claims-made policy and an occurrence policy. As a federal district court in Pennsylvania explained:

> Both policies are intended to insure during a specific period of time against liability arising from the conduct of the insured. One type of policy, the occurrence policy, keys upon when that conduct occurs. If it occurs during the policy period, the insurer has a duty to indemnify and defend the insured regardless of when the claim against the insured is made. Conversely, the other type of policy, the claims-made policy, keys upon when the claim is asserted against the insured. If it is made against the insured during the policy period, the insurer has to perform under the contract regardless of when the conduct giving rise to the claim occurred.

City of Harrisburg v. International Surplus Lines Ins. Co., 596 F. Supp. 954, 960 (M.D. PA 1984), *aff'd without op*., 770 F.2d 1067 (3d Cir. 1985). *See also Central Illinois Light Co. v. The Home Insurance Co.*, 213 Ill. 2d 141, 173, 821 N.E.2d 206 (IL 2004)(occurrence-based policies indemnify against claims occurring in a certain time period, regardless of when claims are made, while claims-made policies indemnify against claims made during a certain period, regardless of when underlying incidents occurred).

An occurrence policy's notice provision allows the insurer time to investigate, defend, and settle a claim. *City of Harrisburg*, 596 F. Supp. at 962. The notice provision in a claims-made policy "provides a certain date after which an insurer knows that it no longer is liable under the policy, and accordingly, allows the insurer to more accurately fix its reserves for future liabilities and compute premiums with greater certainty." *Id*.

V. WHEN DOES AN INSURED'S DUTY TO GIVE NOTICE ARISE?

Some courts will require a "reasonably prudent insured" to give notice of all "occurrences" leaving the insured to determine if the facts implicate coverage. Other courts have held that the duty to provide notice does not arise until the insured has a reasonable belief that the occurrence may present a threat of legal liability to the insured. However, insureds must be careful to not usurp their insurers' rights to timely interpret the contents of any legal proceedings brought against the insured potentially impacting coverage. Whether or not an insured subjectively believes that the claims in a lawsuit are frivolous or without merit, courts rarely excuse an insured's untimely failure to forward complaints against the insured to the insurer. *See*, *e.g.*, *United States Fire*

Ins. Co. v. Vanderbilt University, 267 F.3d 465 (6th Cir. 2001)(insured's subjective belief in its non-liability was unfounded and objectively unreasonable).

The differing judicial interpretations of when an insured's notice obligation arises is further complicated by the fact that the phrase "as soon as practicable" is frequently not defined anywhere in a liability insurance policy. Nevertheless, courts appear to be moving in a common direction and typically interpret this phrase as requiring "prompt" or "as soon as possible" notice of an occurrence giving rise to an insurance claim. For example, some courts have interpreted "as soon as practicable" to mean "within a reasonable time." *Barrington Consolidated High School v. American Insurance Company*, 58 Ill. 2d 278, 282, 319 N.E. 2d 25 (IL 1974). In late notice cases, the concept of reasonableness is widely applied by courts throughout the United States. However, what is a reasonable amount of time for an insured to provide notice to its primary insurer is not necessarily the same as an insured's obligations to its excess insurer.

With respect to primary insurance policies, courts generally apply an objective standard and look to what a "reasonably prudent insured" would do. To illustrate, the Tennessee Supreme Court has held that when an insured is required to give notice of an occurrence "as soon as practicable," the insured has a duty to "give notice when [it] becomes, or should become, aware of facts which would suggest to a reasonably prudent person that the event for which coverage is sought might reasonably be expected to produce a claim against the insurer." *Reliance Ins. Co. v. Athena Cablevision Corp*., 560 S. W. 2d 617, 618 (TN 1977). The court stated that "'as soon as practicable' are not words of precise and definite import. They are roomy words. They provide for more or less free play. They are in their nature ambulatory subject under the guiding rule, to the impact of particular facts on particular cases." *Id*. (quoting *Transamerica Ins. Co. v. Parrott,* 531 S.W.2d 306, 312-13 (Tenn.Ct.App.1975)). The court stated that the words "must be construed as requiring the notice within a reasonable time under all the circumstances, to effectuate the objects and purposes of the notice clause." *Reliance Ins*., 560 S.W.2d at 618 (quoting *Transamerica*, 531 S. W.2d at 513.

It is widely recognized that notice to a primary insurer differs from notice to an excess insurer. This difference is based on the different functions of primary and excess liability insurance policies. Because a primary insurer has a defense obligation to its insured, the importance of "immediate" notice is more apparent. In contrast, an excess insurer typically does not provide a defense to the insured. Consequently, the excess insurer is not necessarily interested in every "occurrence," but rather only those that are likely to involve the excess layer of coverage.

When confronted with the question of whether an insured "could reasonably conclude" that an occurrence is likely to involve an excess policy, courts commonly apply an objective standard. *See*, *e.g*., Ostrager & Newman, *Handbook on Insurance Coverage Disputes*, §4.02[b] (13thEd. 2006). This necessarily results in a factual inquiry

to determine whether a policyholder's assessment of whether a claim will trigger an excess policy is reasonable. Not surprisingly, courts have conflicting interpretations of when notice to an excess insurer is appropriate. *Compare*, *e.g.*, *Olin Corp. v. Insurance Co. of N. America*, 743 F. Supp. 1044 (S.D.NY 1990) , ***aff'd***, 929 F.2d 62 (2d Cir. 1990)(notice untimely where circumstances known to insured would have suggested reasonable possibility of claim that would trigger excess insurers' coverages) and *Certain Underwriters of Lloyd's v. General Accident Ins. Co. of America*, 699 F. Supp. 732 (S.D. IN 1988), ***aff'd***, 909 F.2d 228 (9th Cir. 1990)(court rejected insurer's argument that a $10 million demand required policyholder to notify excess insurer that provided coverage in excess of $1 million).

VI. LEGAL CONSEQUENCES OF LATE NOTICE: IS PREJUDICE REQUIRED?

The "traditional" notice rule (sometimes referred to as the "old rule") interprets compliance with liability insurance policy notice conditions as a strict condition precedent to coverage. Under the traditional rule, breach of the notice requirement waives any rights that the insured might otherwise have under the policy. While several states continue to adhere to this traditional view, a majority of states have adopted a more liberal interpretation of notice provisions and follow one or more variations of the "modern" rule that focuses on whether the insured's conduct was demonstrably unreasonable or undermined the purpose of the notice provision. Most modern rule jurisdictions relieve an insurer of its policy obligations only when it can be proven that the insurer has been prejudiced by its insured's delay in providing notice.

While most states have moved away from a literal interpretation of notice provisions and have ruled that an insured's breach of its notice obligations will not defeat coverage unless the insurer is prejudiced by the untimely notice of claim, New York remains one of the few states that continues to follow the traditional rule that any breach of the notice requirement defeats coverage. New York's adoption of the traditional rule in liability insurance cases was recently reaffirmed in *Argo Corp. v. Greater N.Y. Mut. Ins. Co.*, 827 N.E.2d 762 (NY 2005). In *Argo Corp.*, the court held that in the liability insurance context, an insured's late notice of an underlying lawsuit against it was unreasonable as a matter of law and, therefore, the insurer did not need to show prejudice before denying coverage based on the late notice defense. *Id*. at 763. The policy at issue required the insured to notify the insurer "as soon as practicable" of an "occurrence" or offence that could result in a claim. However, the insured did not provide its insurer with notice until fourteen months after it was served with the complaint, until six months after it was served with a default motion, until more than three months after a default judgment was entered against the insured, and until nearly three months after Notice of Issue. *Id*. at 764. The court reasoned that because the liability insurer had a duty to defend along with its duty to indemnify, timely notice was necessary to afford the insurer an opportunity to "take an active, early role in the litigation process and in any settlement discussions and to set reserves. Late notice of a

lawsuit in the liability context is so likely to be prejudicial to these concerns as to justify the application of the no prejudice rule." *Id*.

The Illinois Supreme Court recently handed down a pro-insurer decision in *Country Mutual Ins. Co. v. Livorsi Marine, Inc.*, 222 N.E.2d 303, 856 N.E.2d 338 (IL 2006) and granted a declaratory judgment in favor of an insurer determining that it had no duty to defend or indemnify the defendant policyholders. The Illinois Supreme Court held that (1) the presence or absence of prejudice to the insurer is one factor to consider when determining whether a policyholder has fulfilled any policy condition requiring reasonable notice and (2) once it is determined that the insurer did not receive reasonable notice of an occurrence or a lawsuit, the policyholder may not recover under the policy, regardless of whether the lack of reasonable notice prejudiced the insurer. In reaching its holding, the court refused to distinguish between notice of an occurrence and notice of a lawsuit. The Illinois Supreme Court refused to alter its holding in *M.F.A. Mutual Insurance Co. v. Cheek*, 66 Ill.2d 492, 363 N.E.2d 809 (IL 1977), where it held that unless a breach of the cooperation clause substantially prejudices the insurer, the insurer cannot rely on the breach to escape its obligations under the policy. *Cheek*, 66 Ill.2d at 498. The court emphasized that the conditions of notice and cooperation are not entirely similar and Illinois courts have not treated them similarly in the past.

In spite of the fact that the majority of states have ruled that late notice will only defeat coverage in the event that the delay has caused prejudice to the insurer, courts frequently disagree with respect to who bears the burden of proving or disproving whether or not the insurer has been prejudiced.

In jurisdictions where the burden of proving prejudice has been placed on the insurer, courts tend to look for ways to promote coverage whenever the facts permit. For example, some courts have held that broad assertions of prejudice are insufficient, particularly where the insurers were nonetheless able to find many reasons for denying coverage or where the claimed coverage defenses are primarily legal in character and not particularly fact-specific. *See*, *e.g.*, *Dover Mills Partnership v. Commercial Union Insurance Companies*, 740 A.2d 1064 (NH 1999); *Olds-Olympic, Inc. v. Commercial Union*, 129 Wash.2d 464, 918 P.2d 923 (WA 1996). Where, however, an insurer can demonstrate that it was prevented from participating in the defense of the underlying claim, including settlement negotiations, and statutes of limitations for pursuing third-party actions have expired, an insurer is likely to be able to satisfy its prejudice burden. Courts additionally attempt to determine if the defense of the underlying lawsuit was compromised due to the untimely notice. However, where the insured successfully defends the underlying lawsuit, courts have held that the insurer has no grounds to argue that it was prejudiced. *See*, *e.g*., *Kenworthy v. Bituminous Casualty Corp*., 28 Ill. App.3d 546, 328 N.E.2d 588 (IL 1975).

In determining whether an insurer has been prejudiced, courts often consider whether the late notice has resulted in the forfeiture of information essential for evaluation of the claim or defense of the underlying case. However, prejudice is often

difficult for an insurer to establish because it may be impossible for an insurer to show which facts or witnesses it would have discovered had notice been timely.

The consequences of an insured's failure to comply with liability insurance policy notice provisions differ from state to state. A review of various court decisions and legislation throughout the United States reveals that states' interpretation of the legal effect of an insured's late notice generally fall into one of four categories:

1. Prejudice is irrelevant. An insured's late notice defeats coverage without regard to the reason for it or its effect on the insurer.

2. Prejudice is relevant, but not determinative. A court will consider issues such as the length of the delay and whether an insured's delay was justified.

3. Prejudice is required, but will be presumed in cases of extreme delay. Coverage will be forfeited unless the insured can prove that the delay was harmless.

4. Prejudice is required and must be proved by the insurer.

Prejudice Irrelevant **[Traditional Rule]**	**Prejudice Relevant But Not Determinative**	**Delay Creates A Presumption of Prejudice: Policyholder Has Burden to Rebut Presumption**	**Prejudice Required: Insurer Has Duty To Prove Prejudice**
Georgia	Alabama	Colorado [*where notice is not provided until after the disposition of the underlying action; otherwise prejudice likely required*]	Alaska
Idaho	Illinois	Connecticut	Arizona
New York [NOTE: In January 2009, New York enacted Section 3420(a) of the New York Insurance Law to require that liability insurance policies covering bodily injury contain a		Florida	Arkansas

provision that provides, "that failure to give notice within the prescribed time will not invalidate any claim made by the insured, injured person, or any other claimant, unless the failure to provide timely notice has prejudiced the insurer." It is not clear where the burden lies.]			
Virginia	Wyoming	Indiana [*prejudice presumed if notice is late*]	California
		Ohio	Delaware
		Tennessee	Hawaii
			Iowa
			Kansas
			Kentucky
			Louisiana
			Maine
			Maryland
			Massachusetts
			Michigan
			Minnesota
			Mississippi
			Missouri

			Montana
			Nebraska
			Nevada
			New Hampshire
			New Jersey
			New Mexico
			North Carolina
			North Dakota
			Oklahoma
			Oregon
			Pennsylvania
			Rhode Island
			South Carolina
			South Dakota
			Texas
			Utah
			Vermont
			Washington
			West Virginia
			Wisconsin

VII. STATUTES AND REGULATIONS IMPACTING NOTICE OBLIGATIONS

Some states have enacted insurance statutes and regulations directly applicable to the meaning and application of liability insurance policy notice provisions. Some examples include:

- **California**

  Section 554 of the California Insurance Code provides that an insurer that receives untimely notice of a matter will waive its late notice coverage defense unless the insurer promptly and specifically objects on that ground.

- **Georgia**

  GA Code Ann. § 33-7-15 (1992): The Georgia Code removes the requirement to indemnify the policyholder if the policyholder fails to "send his insurer, as soon as practicable. . ., a copy of every summons or other process relating to coverage under the policy" provided the failure to cooperate is "prejudicial to the insurer".

- **Maryland**

  MD Ins. Code Ann., Ins. § 19-110 (2000) provides:

  > An insurer may disclaim coverage on a liability insurance policy on the ground that the insured or a person claiming the benefits of the policy through the insured has breached the policy by failing to cooperate with the insurer by not giving the insurer required notice only if the insurer establishes by a preponderance of the evidence that the lack of cooperation or notice has resulted in actual prejudice to the insurer.

- **Massachusetts**

  Common law rule changed by M.G.L. c.175 §112 which introduced requirement of prejudice from claims arising after 1977.

- **Missouri**

  Regulations adopted by the Missouri Insurance Commissioner prohibit the denial of coverage for failure to provide timely notice of a claim unless the insurer can establish prejudice from the late notice. 20 MO Code Regs § 100-1.020 (4).

- **New York**

  Insurance Law Section 3420(a)(3) requires that all policies issued or delivered in New York provide that "notice given by or on behalf of the insured, or written notice by or on behalf of the injured person or any other claimant, to any licensed agent of the insurer in this state, with particulars sufficient to identify the insured, shall be deemed notice to the insurer." Under Section 3420(d), an insurer must not only give timely notice of a disclaimer of coverage to the insured, but also to "the injured person or claimant." The statute is applicable to liability policies delivered or issued for delivery in New York, affording coverage for death or bodily injury and arising from an accident occurring within the state.

- **Texas**

  The Texas Board of Insurance has required that all policies issued after May 1, 1976 include an endorsement restricting application of late notice unless it results in prejudice.

- **Utah**

  Section 31-A-21-312(2) of the Utah Code expressly states that a delay in giving notice "does not bar recovery under the policy if the insurance company fails to show that it was prejudiced by the failure.

- **Wisconsin**

  Wisconsin Statute §632.26 requires:

  (1) (a)That notice given by or on behalf of the insured to any authorized agent of the insurer within this state, with particulars sufficient to identify the insured, is notice to the insurer.

  (b)That failure to give any notice required by the policy within the time specified does not invalidate a claim made by the insured if the insured shows that it was not reasonably possible to give the notice within the prescribed time and that notice was given as soon as reasonably possible.

  (2) Effect of failure to give notice. Failure to give notice as required by the policy as modified by sub (1) (b) does not bar

liability under the policy if the insurer was not prejudiced by the failure, but the risk of nonpersuasion is upon the person claiming there was no prejudice.

VIII. CONCLUSION

While courts uniformly recognize the importance of a policyholder providing timely notice to its primary and excess insurers, courts have adopted different approaches to interpreting the legal effect of late notice. It is important for policyholders to be aware of the ever-changing judicial interpretations of liability insurance policy notice provisions in the jurisdictions potentially applicable to their claims. Policyholders should not treat the notice requirement as the beginning of an adversarial relationship with their insurers. A prudent insured will view prompt and effective notice as a positive first step in the cooperative exchange of information consistent with the terms and provisions of the insurance contract.

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