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Alert

Prejudice Not Required For New Jersey Late Notice Defense Under Claims-Made Policies

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On February 11, 2016, the New Jersey Supreme Court held that an insurer is not obligated to establish prejudice when seeking to disclaim coverage to a sophisticated insured on the grounds of late notice under a claims-made policy. See Templo Fuente De Vida Corp., et al v. National Union Fire Ins. Co., 2016 N.J. LEXIS 144 (N.J. 2016).

Significantly, the Court held that even if notice is given within the policy period of a claims-made policy, a late notice defense can be successful, in the absence of prejudice, if notice was not provided "as soon as practicable."

In Templo Fuente, Templo Fuente De Vida Corporation ("Templo"), sought a loan needed to purchase land, utilizing Morris Mortgage, Inc. ("MMI") to assist in securing financing for the purchase. MMI advised that it had obtained financing from Merl Financial Group, Inc. ("Merl"). When the final closing date for the property arrived, however, Merl did not fund the loan to purchase the property and the sellers terminated the purchase agreement. As a result of the losses sustained in their attempt to purchase the property, Templo filed a complaint against Merl, among others, and first served Merl on or about February 21, 2006.

National Union issued a claims-made policy to Merl's successor, First Independent Financial Group ("First Independent"), for the policy period January 1, 2006 through January 1, 2007. The notice provision required First Independent to provide written notice of a claim "as soon as practicable." Despite this obligation, First Independent waited until August 28, 2006, more than six months, to give National Union notice of the amended complaint. As a result its breach of the notice condition, National Union disclaimed coverage to First Independent.

In the declaratory judgment action, First Independent argued that National Union was required to establish appreciable prejudice to disclaim coverage based on First Independent's breach of the notice condition of the policy. National Union, relying on Zuckerman v. National Union Fire Ins. Co., 100 N.J. 304 (1985), argued that no prejudice was required. In Zuckerman, the New Jersey Supreme Court declined to follow Cooper v. Government Employees Ins. Co., 51 N.J. 86 (1968) (prejudice required for a late notice defense under occurrence-based policies) and held that an insurer need not

establish appreciable prejudice under a claims-made and reported policy where the claim was made within the policy period but not reported until after the policy period expired. The Court's February 11, 2016 decision expands Zuckerman's application to circumstances when, although the claim was reported during the policy period, it was not reported "as soon as practicable."

The Templo Fuente Court sided with National Union primarily by focusing on the sophistication of the insured and the reasonable expectation of the parties to the contract. In discussing the difference between claims-made and occurrence policies, the court emphasized that occurrence policies are often-times contracts of adhesion between parties of unequal bargaining power, and therefore, requiring strict adherence to the terms of the notice provisions would be too harsh. On the other hand, this claims-made Directors and Officers policy involved sophisticated parties that used a sophisticated broker. In such a circumstance, the Court held it is appropriate to enforce the plain and unambiguous terms of the policy. Consequently, National Union was not obligated to establish prejudice.

In addition, although the Court held that a six month delay was not "as soon as practicable", it was careful to restrict its holding to the set of facts before it and not create a bright line rule for compliance with insurance notice provisions.

The impact of the Templo Fuente decision on claims-made D&O policies involving sophisticated insureds is clear. The Court has expanded the Zuckerman decision to allow a successful late notice defense, in the absence of prejudice, where a claim is reported within the policy period, but not "as soon as practicable." In light of Templo Fuente's expansion of the late notice defense, insurers should carefully examine the timing of notice by its policyholders under claims-made policies. Even if the claim is reported during the policy period, consideration should now be given to whether the claim was noticed "as soon as practicable."