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## NEW JERSEY APPELLATE DIVISION ESTOPS INSURERS FROM DENYING COVERAGE BASED ON FAULTY RESERVATIONS OF RIGHTS

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**It is well-established in New Jersey that if an insurer agrees to defend an insured without reserving its rights, the insurer is estopped from denying coverage. In *Nazario v. The Lobster House, et al*, Docket No. A-3025-07T1 (App. Div. May 5, 2009), the Appellate Division expounded on that doctrine and held that two insurers were estopped from denying coverage because their reservation of rights letters were inadequate.**

The *Nazario* case involved a bodily injury claim by a contractor's employee against Cold Spring Fish & Supply Co., d/b/a The Lobster House. Cold Spring had two primary policies that could potentially provide coverage: one from Essex Insurance Company and one from Sirius America Insurance Company. Both insurers responded to the notice of claim by Cold Spring with reservation of rights letters. Essex advised Cold Spring that it was disclaiming coverage, but would investigate and defend while retaining its right to deny coverage. Essex appointed counsel, who filed an answer for Cold Spring and asserted

defenses and cross-claims. Shortly thereafter, Essex sued Cold Spring for a declaration that it had no duty to defend or indemnify.

Sirius responded by assigning counsel under a "full and complete reservation of any and all rights." Sirius further recommended to Cold Spring that it retain separate counsel. Several months later, Sirius also sued Cold Spring for a declaration of no coverage. The cases were consolidated, and Cold Spring, Essex and Sirius all moved for summary judgment. The court found that Essex and Sirius were both right, and that Cold Spring did not have coverage under either policy. However, the court held that both insurers were estopped from withdrawing coverage because both reservation of rights letter failed "to inform [Cold Spring] that the offer[s] (to defend) may be accepted or rejected."

The Appellate Division affirmed. Like the trial court, the Appellate Division relied on the simple rule that unless a reservation of rights letter specifically stated that the insured had the right to accept or reject the defense under those terms, it was inadequate. The court relied principally on the New

Jersey Supreme Court's decision in *Merchants Indem. Corp. v. Eggleston*, 37 N.J. 114 (1962) which, while clearly on point, had not been cited for this legal principle for many years.

The court dealt decisively with two defenses raised by the insurers. First, the insurers basically argued that they had done everything right. They had written timely reservation of rights letters. They had set forth that they might deny coverage. They had instituted coverage litigation to determine their rights. Sirius recommended that the insured retain separate counsel, which it did. From the insurers' perspective, they had done everything "by the book." The court was simply uninterested. Since the insurers did not inform the insured that it had the right to reject the defense that they offered, the court found that the insured was in the same position as though the insurers had assumed the defense without a reservation of rights.

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Second, the insurers asserted that Cold Spring had not incurred prejudice. The court dealt with this defense by holding that no requirement of actual prejudice existed, but rather that prejudice was presumed when an insurer defended without adequately advising the insured of its rights. "We find nothing in *Eggleston* or its progeny which suggests that the insured must prove actual prejudice to create coverage, or that the carrier may prove lack of prejudice to avoid coverage by estoppel, when a fully informed written consent is lacking."

*Nazario* is a major statement of the rights of insureds when an insurer seeks to impose a defense under a reservation of rights. Almost all insurers have acted in recent years as did Essex and Sirius, taking certain measures when reserving rights but not heeding the requirement of *Eggleston*. It is extremely rare for an insurer to advise an insured that it has the right to accept or deny a defense offered under a reservation of rights. As a result, in most current cases in which the insurer is defending under a reservation of rights, the insurer will be estopped from denying coverage.

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