

# New Jersey Law Journal

VOL. CXCIV - NO.8 - INDEX 511

FEBRUARY 23, 2009

ESTABLISHED 1878

IN PRACTICE

## INSURANCE LAW

### Lions and Tigers and Notice

Notice requirements under claims-made insurance policies

BY ROBERT D. CHESLER AND DAVID M. REINER

The New Jersey Appellate Division recently reaffirmed that it will strictly and rigorously enforce notice provisions under claims-made policies. Put simply, in New Jersey, failure to provide notice of claims under a claims-made policy will result in no coverage.

This may surprise many attorneys since New Jersey is known for using a “prejudice” standard with respect to notice. Under this standard, late notice will only forfeit coverage if the insurer can demonstrate appreciable prejudice, which has proven an extremely difficult standard for insurers. However, this prejudice rule only applies to “occurrence” based policies, typically general liability policies. It has no applicability at all to claims-made policies, which typically includes directors’ and officers’ policies, employment practices policies, and malpractice and errors and omissions policies.

In *Alpine Home Inspections, LLC v. Underwriters at Lloyd’s*

*Chesler is a member of and chair of and Reiner is an associate with the Insurance Practice Group of Lowenstein Sandler in Roseland.*

*London*, No. A-1402-07, 2008 WL 4963518 (App. Div. Nov. 24, 2008), a home inspector, Glen Woertz, was sued by a homeowner-client, Jeffrey Rotenberg, for failure to discover the presence of termites during an inspection of a home that Rotenberg subsequently purchased. When a post-purchase inspection revealed the presence of termites, Rotenberg’s attorney sent Woertz a letter advising him of the damage and providing a preliminary estimate of \$3,300 for repairs. In addition, the attorney asked Woertz for his liability insurance policy information. At the time, Woertz had a claims-made liability policy for a period of one year from Underwriters that included, in the definition of a claim, any “written demand.” Because the \$3,300 estimate was within Woertz’s deductible, however, he did not advise Underwriters of receipt of the letter.

To recoup the repair costs, Rotenberg filed a complaint in the Special Civil Part of the Law Division. At that time, Woertz provided notice of the complaint to Underwriters, who responded with a reservation of rights letter. Notably, at the time the complaint was filed and Woertz notified Underwriters, he was operating under a new one-year policy. In preparing

for the case, Rotenberg received an opinion from a real estate expert that there had been a 10-percent reduction in fair market value of his home, which was purchased for \$3,000,000. As a result, Rotenberg transferred his claim out of the Special Civil Part to pursue greater damages.

Woertz then filed a declaratory judgment action against Underwriters for coverage under the claims-made policy; Underwriters moved for summary judgment. The trial court granted Underwriters’ motion for summary judgment, finding that Woertz was not entitled to coverage due to his failure to notify Underwriters of the initial letter regarding damages sent by Rotenberg’s attorney.

On appeal, Woertz argued that a denial of coverage defeated his reasonable expectations. Specifically, he contended that the increased damages, and resulting transfer of the case from the Special Civil Part, constituted a new claim. The Appellate Division, however, found that argument to be “wholly inconsistent with the nature of a claims made policy of insurance” and affirmed the trial court’s ruling. The Appellate Division determined that the letter from Rotenberg’s attorney regarding damages was the first claim, and it arose during Woertz’s first policy period, which expired by the time Woertz provided notice of the complaint to Underwriters. The Appellate Division held that it could not “consider a claim for increased

damages a new claim that arose within the second policy period; it is simply a claim for enhanced damages for the same claim for which Woertz received notification during the first policy period.” Quoting a New Jersey Supreme Court case that involved similar facts, *Zuckerman v. National Union Fire Insurance Co.*, 100 N.J. 304 (1985), the Appellate Division stressed the importance of enforcing the notice period in claims-made policies: “[A]n extension of the notice period in a ‘claims made’ policy constitutes an unbargained-for expansion of coverage, gratis, resulting in the insurance company’s exposure to a risk substantially broader than that expressly insured against in the policy.”

In addition, the Appellate Division rejected Woertz’s contention that the consecutive one-year claims-made policies issued by Underwriters constituted continuous coverage. Pointing to a previous case in which the Appellate Division rejected a similar argument, *Insite-Properties, Inc. v. Jay Phillips, Inc.*, 271 N.J. Super. 380, 385-86 (App. Div. 1994), the court held that “[s]uch an analysis flies in the face of a claims made policy.” Finally, the court rejected Woertz’s arguments that coverage should be found because the policy was ambiguous and for reasons of public policy. In response to those arguments, the court found that the policies clearly defined the effective dates, and that Woertz was not confused by the nature of a claims-made policy. Instead, “he simply chose not to report the claim when he received it.”

The Appellate Division’s decision in *Alpine Home Inspections* reaffirms that New Jersey courts will strictly enforce notice provisions in claims-made policies. Notably, the decision in *Alpine Home Inspections* comes just over a year and a half after the Appellate Division’s decision in *Apro Management, Inc. v. Royal Surplus Lines Insurance Co.*, No. A-3976-05, 2007 WL 1238574 (App. Div. Apr. 30, 2007), in which the court also rigorously enforced notice provisions in claims-made policies. In *Apro*

*Management*, the insured obtained two successive one-year claims-made policies from the same insurer. During the coverage period of the first policy, the insured was sued for fraudulent misrepresentation and violation of the New Jersey Consumer Fraud Act, and in addition, had a cross-claim filed against it. The insured was told by its insurance broker that the claims were not covered, and therefore, the insured did not notify its insurer. During the coverage period of the second policy, however, the insured was served with an amended complaint that included covered claims, and subsequently notified its insurer. The insurer denied coverage, citing late notice, but the trial court found that the insurer had a duty to defend and indemnify.

The Appellate Division reversed the decision of the trial court, finding that the insured had an obligation to notify the insurer of the initial complaint and cross-claim even though they did not include covered claims. The court reasoned that the insured should have known that the initial complaint and cross-claim could lead to additional claims that were covered by the policy, and held that the insured could not pick and choose which claims to report to the insurer under a claims-made policy.

Notice under general liability policies is relatively straight-forward. The insured must give notice of a “suit,” which usually means a complaint. As demonstrated by *Alpine Home Inspections*, though, a letter can be a claim under a claims-made policy. Moreover, while essentially all general liability policies use the undefined term “suit,” claims-made policies define the term “claim” in a variety of ways. The insured must review the policy for its definition of “claim.” One typical definition in D&O policies is “any written demand for monetary or non-monetary relief.” Pursuant to this definition, an angry letter to the company from a shareholder demanding that the company make changes in its governance structure is a demand for nonmonetary relief that the insured must notice. If

the insured does not provide notice of this letter, it may well be denied coverage if a class action seeking the same relief is filed in the following year.

The harshness of the decisions in *Alpine Home Inspections* and *Apro Management* may surprise insurance lawyers. In both cases, the equities favored the insured. Certainly, many insurance professionals would have agreed with the policyholder that early notice did not seem necessary. This is particularly so because for decades, New Jersey courts have indulged insureds who have given late notice, even extremely late notice, under general liability policies.

The jurisprudence of New Jersey courts regarding notice under claims-made policies is totally and dispositively different. The recent decisions in *Alpine Home Inspections* and *Apro Management* demonstrate that courts will strictly, even punitively, enforce notice provisions under claims-made policies. As a result, insureds must be aware of the type of policy they hold, the details of the notice provision in their policies, and what constitutes a claim under their policies. Most importantly, as demonstrated in *Apro Management*, those advising companies, whether insurance brokers, consultants or lawyers, must be aware of the details of both New Jersey notice law and the provisions of their clients’ insurance policies. Late notice under a claims-made policy might not only be fatal to the insured, but also to the party advising the insured.

To conclude, under claims-made policies, if a document looks or smells like it is a claim, or might morph into a claim at some future date, the policyholder must give timely notice. Companies often hesitate to give notice of potential claims to their insurers. They do not want to hang out their dirty linen publicly, and are afraid that notice of a claim will increase their premium. When advising clients in this area, a broker or lawyer must be absolutely clear to the client that failure to give notice could well mean that the insured will forfeit coverage. ■