wiley

NEWSLETTER

Breach of Notice Provision Precludes Coverage Under a Claims-Made Policy, Even in Absence of Prejudice

March 2008

The United States District Court for the Western District of Pennsylvania, applying Pennsylvania law, has held that a D&O policy does not afford coverage where the insured failed to provide notice of a claim under the policy, irrespective of whether the insurer was prejudiced. *Dowdell v. Fed. Ins. Co.*, 2008 WL 163052 (W.D. Pa. Jan. 15, 2008). In addition, the court determined that notice provided to the insurer by the underlying claimant was insufficient to satisfy the policy's notice requirement because it did not come from the insured.

The insurer issued a claims-made D&O policy to a company providing drivers' education services to high schools. After the company went bankrupt, investors brought suit against the company's CEO for fraud and negligent misrepresentation in connection with the solicitation of capital. The investors sent letters to the insurer during the policy period purporting to serve as a claim and a notice of claim against the insured. The insured, however, never provided the insurer with notice of the claim or otherwise sought coverage under the policy.

In the underlying case, the investors obtained a judgment of more than $1 million dollars against the insured. They later sought to recover the judgment from the insurer. The insurer moved for summary judgment, arguing that it was not liable under the policy because neither a claim nor notice of a claim had been made under the policy.

The court first considered whether a breach of the policy's notice provision barred coverage under the policy. The court initially observed that notice requirements in claims-made policies should be strictly construed because the finite reporting period for claims allows insurers to fix reserves with more certainty and thus permits them to charge lower premiums. The court then explained that courts routinely refuse to impose a prejudice requirement when the insurer seeks to enforce the terms of a notice provision in claims-made policies. Accordingly, the court held that "lack of notice or late notice under a claims-made policy precludes coverage."

The court then considered the investors' argument that many of the notice-prejudice cases cited by the insurer

involved claims-made-and-reported policies, rather than simple claims-made policies. The investors contended that the policy at issue did not contain a reporting requirement in the declarations, arguing that this fact rendered the policy a claims-made policy rather than a claims-made-and-reported policy. The court disagreed, emphasizing that the policy contained a specific reporting requirement and holding that the failure to include the reporting requirement in the declarations did not render the policy a pure claims-made policy.

The court then determined that the investors' purported "notice" of the claim to the insurer was not sufficient to constitute notice under the policy because it was not from the insured. The court stated that the need for notice from the insured provides certainty to the process because: (1) a third party has no way of knowing whether the insured will invoke coverage for a particular claim; (2) an insured may choose not to report a claim because of concern over elevated premiums; and (3) the insured may choose to represent himself or may have alternate coverage. The court noted that "[t]he Policy was written for [the insured's] benefit, and it is up to him to decide whether to invoke its coverage."