

Notice of Circumstances Does Not Excuse Obligation To Provide Timely Notice of Claim

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The Appellate Division of the New York Supreme Court has held that an insured's failure to provide timely notice of a claim vitiated coverage under a claims-made D&O policy even though the insured previously had provided notice of circumstances during the policy period. *Penn Traffic Co. v. Nat'l Union Fire Ins. Co.*, 2010 WL 5396000 (N.Y. App. Div. Dec. 30, 2010).

The policy period ran from June 29, 2002 to June 29, 2004. The policy provided specified coverage for claims made during the policy period and reported within 60 days after the end of the policy period. The policy further provided that a claim made after the policy period will be deemed to have been made during the policy period if it relates to circumstances that were the subject of notice in writing to the insurer during the policy period.

Here, the insured supermarket chain learned in August 2002 that an employee of its wholly owned subsidiary was being investigated by federal authorities for making false accounting entries, which, due to overstated inventories, required the supermarket chain to restate its financial results for the years 1999 through 2002. By letter dated October 7, 2002, the insured provided notice of these circumstances to the insurer. The SEC subsequently issued subpoenas on March 31, 2004 to certain employees of the insured concerning its subsidiary's accounting improprieties. The insured provided notice of these subpoenas to the insurer and sought coverage for costs incurred in connection with the investigation two years later, on April 27, 2006. The insurer denied coverage based on the insured's failure to provide notice within 60 days of the end of the policy period.

In the coverage litigation that followed, the court found that the subpoenas constituted a claim made during the policy period and held that the obligation to provide notice of the claim within 60 days of the end of the policy period was a "condition precedent," the failure of which "as a matter of law, vitiat[e] the contract." The court therefore concluded that the insured was not entitled to coverage for any costs incurred in connection with the subpoenas. In so concluding, the court also rejected the insured's argument that its failure to realize earlier that the subpoenas were covered under the policy excused the insured's late notice. According to the court, a unilateral mistake in reading the policy is not a basis for expanding coverage.

In addition, the court rejected the insured's claim for coverage for an investigation launched in late-2004 involving the misuse of promotional allowances by two high-level executives employed directly by the insured. The court found that this investigation was separate and distinct from the investigation involving the subsidiary because it involved different employees, different accounting irregularities and different time periods. Therefore, according to the court, the October 7, 2002 notice of the subsidiary investigation could not be said to constitute notice of this later investigation such that it could be deemed a claim made during the policy period.