Case Alert

New Jersey Adopts a "No Prejudice" Rule for Sophisticated Insureds Under "Claims Made" Policies

On February 11, 2016, the New Jersey Supreme Court held that for "claims made" policies, the insurer does not have to show that it has been appreciably prejudiced by the insured's late notice before disclaiming coverage. The case is *Templo Fuente De Vida Corp. v. National Union Fire Ins. Co.,* 2016 N.J. LEXIS 144 (N.J. Feb. 11, 2016). Although this ruling does not affect New Jersey's current insured-friendly rule for "occurrence" policies, insurers may seek to extend the *Templo* reasoning to "occurrence" policies in the future.

Two Templo companies engaged Morris Mortgage to help them secure funding sources for the purchase of property. Morris Mortgage identified Merl Financial Group ("Merl") as a possible funding source. However, at closing, Merl was unable to fund the loan. Templo sued. Sometime before Templo brought the lawsuit, Merl was restructured and renamed First Independent Financial Group ("First Independent"). First Independent purchased a Directors and Officers policy from National Union Fire Insurance Company of Pittsburgh ("National Union") for the 2006 policy year. A "claims made" policy, it required, as a condition precedent to coverage, "written notice to the Insurer of any Claim made against an Insured *as soon as practicable"* (emphasis added).

First Independent learned of the Templo lawsuit in February, 2006, but did not notify National Union until six months later. National Union denied coverage, and First Independent filed an action seeking a declaration that National Union owed it coverage. The trial court granted summary judgment to National Union, finding that First Independent's claim for coverage was barred because it failed to provide the insurer with notice of claim "as soon as practicable" as the terms of the policy required.

The appellate court affirmed the trial court's ruling, holding that only "occurrence" policies required an insurer to show prejudice to disclaim coverage. The New Jersey Supreme Court reviewed the trial court's decision de novo. It found that there was a fundamental difference between "claims made" and "occurrence" policies which affects whether the insurer has to show that it has been "appreciably prejudiced" by the insured's late notice.

The Supreme Court discussed two older cases, *Zuckerman v. National Union Fire Insurance,* 100 N.J. 304 (1985) and *Cooper v. Government Employees Ins. Co.,* 51 N.J. 86 (1968). The *Cooper* case first identified New Jersey's public interest in protecting policyholders with "occurrence" policies. It stands for the principle that although an "occurrence" policy has an unambiguous notice provision, the public interest requires the insurance company to show prejudice before it can disclaim coverage based on late notice. In *Zuckerman*, the Court determined that while the Cooper rule of "appreciable prejudice" applied to "occurrence" policies, it does not apply to a "claims made" policy "that fulfills the reasonable expectations of the insured with respect to the scope of coverage." *Id.* at 324.

The Supreme Court also reasoned that "claims made" policies are different because the requirement of timely notice is closely tied to the insurer's ability to manage its risk when issuing such a policy (which is generally cheaper than an "occurrence" policy). Therefore, it is much more important that the insurer receives a notice of a potential claim under a "claims made" policy in a timely manner. The Court further noted that First Independent was not an individual policyholder with limited bargaining power, but instead a sophisticated company who engaged a broker to assist it with

purchasing the policy. Therefore, the Court reasoned, it had no need to be shielded by the public policy of protecting individual policyholders. The Court concluded that National Union was justified in declining coverage without having to demonstrate appreciable prejudice.

How will the *Templo* decision impact future coverage litigation in New Jersey? The holding is quite narrow – it directly only applies to D&O "claims made" policies, and only when the insured is a sophisticated party. In reality, the "no prejudice" rule will likely be extended to other types of "claims made" policies because of the fundamental difference between "claims made" and "occurrence" policies that the Supreme Court identified.

For policyholders with "occurrence" policies, the standard under New Jersey law remains the same – the insurer must show prejudice as a result of a delayed notice before it can deny coverage. However, we expect that attorneys representing insurance companies will cite Templo in support of an argument that the "no prejudice" rule should be extended to "occurrence" policies as well, at least in the case of "sophisticated companies."

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1. The Court's decision may also have been affected by the fact that First Independent's six-month delay in giving notice was unexplained.