LATE NOTICE, VOLUNTARY PAYMENT, AND LACK OF COOPERATION

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General Liability – Occurrence

2. Duties In The Event of Occurrence, Offense, Claim or Suit

   a. You must see to it that we are notified **as soon as practicable** of an "occurrence" or an offense which may result in a claim. . . . [N]otice should include:

      (1) How, when and where the "occurrence" or offense took place.

      (2) The names and addresses of any injured persons and witnesses; and

      (3) The nature and location . . .

Notice of Claim

b. If a claim is made or suit is brought against any insured, you must:

(1) **Immediately** record the specifics of the claim or "suit" and the date receives; and

(2) **Notify us as soon as practicable**.

You must see to it that we receive written notice of the claim or "suit" **as soon as practicable**.

Notice of Suit

c. You and any other involved insured must:

(1) **Immediately** send us copies of any demands, notices, summonses or legal papers, received in connection with the claim or “Suit.”

Voluntary Payment

d. No insured will, except at that insured's own cost, voluntarily make a payment, assume any obligation, or incur any expense, other than for first aid, without our consent.

Cooperation

c. You and any other involved insured must:

(3) Cooperate with us in the investigation or settlement of the claim or defense against the “suit.”

The History of Prejudice

Members Mutual Insurance Company v. Cutaia, 476 S.W.2d 278 (Tex. 1972)

- Is duty to forward suit papers "immediately" a condition precedent to coverage?

- Court held no, but issue was more appropriately left to the legislature

Following *Cutaia*

January 26, 1973:

State Board Order 22582

Revision of Texas Standard Provision for Automobile Policies
Editions of April 1, 1955 and October 1, 1966

- *Amendatory Notice 158L applicable to TX standard auto policy forms written or renewed on and after March 1, 1973*

"As respects bodily injury liability coverage and property damage liability coverage, unless the company is prejudiced by the insured's failure to comply with the requirement, any provision of this policy requiring the insured to give notice of action, occurrence or loss, or requiring the insured to forward demands, notices summons or other legal process, shall not bar liability under this policy."

Following *Cutaia*

March 13, 1973:

State Board Order 23080

Revision of Texas Standard Provision for GL policies (approved ISO filing). *Amendatory Endorsement to be attached to all GL policies effective on or after May 1, 1973*.

"As respects bodily injury liability coverage and property damage liability coverage, unless the company is prejudiced by the insured's failure to comply with the requirement, any provision of this policy requiring the insured to give notice of action, occurrence or loss, or requiring the insured to forward demands, notices, summons or other legal process, shall not bar liability under this policy."

PAJ v. Hanover (2008)

- Acknowledged that Texas is a "notice-prejudice" state.

- "As soon as practicable" is a covenant, not a condition precedent. Insurer must show prejudice from breach.

Prodigy (2009)

- Notice-prejudice rule articulated in *PAJ* does not apply to a **claims-made** policy when the policy requires the insured, "as a condition precedent," to give notice "as soon as practicable, but in no event later than ninety (90) days after the expiration of the Policy Period or Discovery Period?"

- "As soon as practicable" is not essential part of bargained-for exchange.

Prodigy (2009)

- In Prodigy, the insured gave notice within the 90-day cutoff. The insurer was not denied the benefit of the claims-made nature of its policy.

- There is a difference in "as soon as practicable" and a hard cutoff in a claims-made policy.

EXCEPT …

There is a difference when notice is not just late, but is "wholly lacking." *Nat'l Union Fire Ins. Co. of Pittsburgh, PA. v. Crocker*, 246 S.W.3d 603 (Tex. 2008).

Default judgments constitute actual prejudice as a matter of law because insurer cannot answer, defend, conduct discovery, and fully litigate merits. This is *unchanged* by the insurer's actual knowledge of suit. *Liberty Mut. Ins. Co. v. Cruz*, 883 S.W.2d 164 (Tex. 1993).

Hernandez v. Gulf Lloyds (1994)

- UM/UIM. Fatality auto accident. Insureds settled liability case for $25,000 limit of the tortfeasor's policy without UIM carrier's consent. Insureds then sought to recover $100,000 in UIM benefits from Gulf Lloyds.

- Gulf Lloyds denied coverage because the insureds did not obtain its consent prior to settlement with the tortfeasor.

- There was no question that the insureds' damages would exceed all of the potentially available insurance.

Hernandez

Court held that settlement without consent clause is unenforceable unless insurer establishes it has been **actually** prejudiced.

Rationale: insurance policies are contracts. A fundamental principle of contract law is that when one party commits a material breach, the other is excused from performance. "The less the non-breaching party is deprived of the expected benefit, the less material the breach."

Hernandez

The court did not hold that voluntary payment *never* prejudices the insurer. ("In the context of an uninsured motorist claim, there may be instances when an insurer's settlement without the insurer's consent prevents the insurer from receiving the anticipated benefit from the insurance contract; specifically, the settlement may extinguish a valuable settlement right.")

When Does Voluntary Payment Amount To Prejudice?

When the insurer has been *actually prejudiced*.

How Does An Insurer Show Prejudice from Voluntary Payment?

"Under *Hernandez*, an insurer establishes prejudice from a settlement to which it did not agree **by showing that the insured's settlement was a material breach of the policy – that is, that it significantly impaired the insurer's position**."

Lennar Corp. v. Markel Am. Ins. Co., 413 S.W.3d 740, 754 (Tex. 2013).

What is a Material Breach?

1. Extent to which non-breaching party will be deprived of benefit it could reasonably have anticipated from full performance.
2. Extent to which injured party can be adequately compensated for part of benefit of which it will be deprived.
3. Extent to which party failing to perform or offer performance will suffer forfeiture.
4. Likelihood that party failing to perform or offer performance will cure the failure.
5. Extent to which behavior of the breaching party comports with standards of good faith and fair dealing.

What is a Material Breach?

Materiality is generally an issue of fact under Texas law.

United States v. Miles, 838 F.3d 621, 628 (5th Cir. 2016).

Prejudice in Claims Made Policies

- In occurrence-based policies, coverage is based upon the triggering event, not the notice.

- In claims-made and reported policies, notice is the event that triggers coverage. Insurers may deny coverage under claims made and reported policies without a showing of prejudice.

See Pogo Resources, LLC v. St. Paul Fire & Marine Ins. Co., 3:19-cv-2682, 2022 WL 286206 (N.D. Tex. Jan. 31, 2022)*; Komatsu v. United States Fire Ins. Co*., 806 S.W.2d 603 (Tex. App.—Fort Worth 1991, writ denied).

Prejudice Requirement in *Hernandez* has been Extrapolated to CGL and E&O Policies

Ins. Co. of N. Am. v. McCarthy Bros. Co., 123 F. Supp. 2d 373 (S.D. Tex. 2000) (general liability policy; settlement without consent)

Comsys Info. Tech. Servs., Inc. v. Twin City Fire Ins. Co., 130 S.W.3d 181 (Tex. App.—Houston [14th Dist.] 2003, pet. denied) (E&O policy; settlement without consent)

Who Has the Burden?

The insurer has the burden to establish prejudice. The insured does not have the burden to establish *lack of* prejudice.

Texas law does not presume prejudice. *Comsys Info Tech Servs., Inc. v. Twin City Fire Ins. Co*., 130 S.W.3d 181, 192 (Tex. App.—Houston 2003, pet. denied).

Other Prejudice From Late Notice

- An insurer may be actually prejudiced from the inability to investigate a claim. *Blanton v. Vesta Lloyds Ins. Co*., 185 S.W.3d 607 (Tex. App.—Dallas 2006, no pet.)

- An insurer may be actually prejudiced if it lost a valuable settlement right. *Clarendon Nat'l Ins. Co. v. FFE Transp. Servs., Inc*., 176 F. App'x 559 (5th Cir. 2006); *Motiva Enters., LLC v. St. Paul Fire & Marine Ins. Co*., 445 F.3d 381 (5th Cir. 2006)

Cooperation

Insured must cooperate with general liability insurer through several provisions in the policy.

- Cooperate in investigation or settlement of claim or defense against the suit
- Authorize insurer to obtain records and information
- Assist insurer to enforce rights against parties who may be liable to insured

Cooperation

Insured must cooperate with property insurer through additional provisions:

- As soon as practicable, give description of how, when and where loss or damage occurred
- Take all reasonable steps to protect covered property from further damage
- Provide signed, sworn proof of loss
- Provide inventory of damaged and undamaged property
- Permit inspection of property/permit insurer to take samples
- Submit to examination under oath

What is the Purpose of Cooperation?

The purpose of cooperation "is to make it possible for the insurer to make a determination regarding coverage and protect itself against fraudulent claims."

Cox Operating, LLC v. St. Paul Surplus Lines Ins. Co., No. H-07-2724, 2012 WL 290027 (S.D. Tex. Jan. 31, 2012).

"The cooperation clause is violated where the insured's conduct is not 'reasonable and justified under the circumstances.'" *Mid-Continent Cas. Co. v. Petroleum Sols., Inc.*, No. 4:09-0422, 2016 WL 5539895 (S.D. Tex. Sept. 29, 2016).

What If The Insured Doesn't Cooperate?

"It is well-established under Texas law that an insured's breach of a cooperation provision relieves an insurer of liability on the policy."

Vollandt v. Axis Ins. Co., No. 4:19-cv-311, 2022 WL 822020 (E.D. Tex. Mar. 17, 2022).

BUT…

An insurer must demonstrate that the insured's breach of a cooperation clause was material and resulted in actual prejudice to the insurer.

Martinez v. ACCC Ins. Co. 343 S.W.3d 924 (Tex. App.—Dallas 2011, no pet.) ("An insured's failure to cooperate will not operate to discharge the insurer's obligations under the policy unless the insurer is actually prejudiced.")