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“No Prejudice Rule” Close to Being Outlawed in New York

By: Henry L. Goldberg & Mitchell B. Reiter

Both the New York State Senate and Assembly recently passed a bill that would prevent an insurance carrier from denying coverage merely as the result of a late notice of claim, unless the carrier suffered “material prejudice” as result of the late notice. If not for Governor Spitzer’s veto, the bill would have brought an end to the “no prejudice rule” pursuant to which insurance companies in New York State have for years, unfairly disclaimed otherwise valid claims.

New York is one of the last states to maintain this archaic, pro-insurance company rule. Currently, insurance companies in New York can disclaim coverage simply because a policyholder acted slowly in notifying its insurance company of the incident upon which its claim is based. This is true even if the tardy nature of the “occurrence” did not in any way adversely effect, prejudice or prevent the carrier from adequately responding to the claim. An insurer in New York need not look further for an excuse to avoid coverage and leave its insured without protection than late notification. Despite the Governor’s veto, the cause of premium-paying insureds, abandoned by their carriers and left to defend liability actions on their own, will no doubt be addressed again in Albany.

In light of the mostly receptive veto message from the Governor and with the support of the New York State Bar Association, the New York State Trial Lawyers Association, and numerous insurance broker groups such as the Independent Insurance Agents & Brokers of New

York and the Council of Insurance Brokers of Greater New York, Inc., (IIABNY) , Professional Insurance Agents of New York (PIANY) and the Tri- County Independent Insurance Agents Association, the “no prejudice rule” may soon be just a bad memory in New York.

For now, policyholders in New York must never simply accept a disclaimer by their insurer. We have been successful in defeating coverage disclaimers, even under the current law, using a number of techniques. One exception to the “no prejudice rule” requires the insured to affirmatively prove it had a reasonable belief of “non-liability” for the occurrence at issue. The vetoed legislation would make this challenge easier for an insured by reversing the burden of proof. Instead of the policyholder, it would be the insurance company that would have the burden of justifying its disclaimer in the first instance.

Under the vetoed bill, an insurer could not deny coverage based on the failure of timely notice of a claim unless it could demonstrate that it has suffered a “material prejudice.” In order to do so, the insurer would have had to satisfy this two part test by showing: (1) that it has suffered a prejudice, and, (2) that the prejudice was material in nature.

In addition to affirmatively proving both elements of the above two part test, an insurer would also have been required to refute a rebuttable presumption created by the bill. Evidence that the insurer had knowledge of the occurrence would have created the presumption that the insurer had not been prejudiced by the delayed notice. In other words, before an insurer would have been able to establish that it was prejudiced, it might first have had to rebut the presumption that it was not prejudiced where knowledge of the occurrence from any other source existed.

Evidence that would have raised this “presumption of no prejudice” included, among other things, any communication to the insurer regarding the occurrence from the claimant, claimant’s representative, claimant’s healthcare provider, an injured person, an injured person’s representative or an injured person’s health care provider. Likewise, any communication

regarding the occurrence from the insurer (or its licensed agent) to the insured would also have triggered the presumption.

Notably, the statute did not define “material” or provide a standard for determining whether or not the suffered prejudice was in fact “material.” However, there is ample legal precedent applying this term and each case would have required a fact-specific analysis.

Lastly, this legislation would have resolved an unfortunate divergence of opinion in existing case law as to the role of a licensed agent. The bill specifically provided that notice given to any licensed agent of an insurer shall be deemed sufficient notice.

While Governor Spitzer vetoed this version of the bill citing “drafting issues” and concerns with the speed with which the bill was passed which may have precluded adequate debate, he nevertheless stated his position is to abolish the “extreme hardship” to insureds caused by the technical disclaimers the “no prejudice rule” facilitates. In fact, Governor Spitzer proclaimed that he would have signed these bills had they “merely permitted late notices of claim where there is no prejudice to the insurer.”

The successful enactment of this legislation would mark an important and long overdue reform of insurance coverage law in New York – a reform now endorsed by both houses of the legislature and with which the Governor has expressed agreement in principle. If both houses pass a more streamlined version of this bill, integrating the guidance provided in the Governor’s veto message, Governor Spitzer would be hard pressed not to sign it.

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