Chapter 5

Late Notice

§ 5:1 Introduction

Timely reporting of losses or claims that will or are likely to involve at least one reinsurance layer has always been central to the business of reinsurance, but the serious consequences of untimeliness have been at issue only since the 1970s.[1] Traditional reinsurance mechanisms operated on oral or informal understandings between cedents and reinsurers, so the time for reporting a claim or loss often was flexible, and the consequences of untimeliness either minor or waived. The modern era—in which the relationship between insurers and

1. Beginning with Sec. Mut. Cas. Co. v. Century Cas. Co., 531 F.2d 974 (10th Cir.), *cert. denied*, 429 U.S. 860 (1976), courts earnestly examined reinsurance late notice and distinguished it from direct insurance late notice. *But see* Keehn v. Excess Ins. Co., 129 F.2d 503 (7th Cir. 1942) (earlier case holding that prompt notice constituted condition precedent to reinsurer's liability in contract at issue).

their reinsurers or between reinsurers and their retrocessionaires has become more arm's-length and contractual, and in which the financial stakes are often enormous—finds reinsurers often litigating the position that late notice avoids coverage entirely, and insurers asserting that such a result is too harsh absent clear prejudice.

This chapter examines late notice by discussing the variety of notice provisions commonly used in reinsurance agreements, investigating how the courts have construed the notice provisions relative to the construction of what constitutes late notice, and noting important cases on the two main branches of reinsurance contract interpretation. Finally, this chapter reviews the various remedy theories available to the reinsured in a late notice scenario.

§ 5:2 Notice Provisions

As discussed in greater detail in chapter 2, the nature of reinsurance requires that the parties owe a duty of utmost good faith to each other.[2] In the context of notice, the duty of utmost good faith places a burden upon the cedent to keep in close communication with its reinsurer and disclose all aspects of the underlying risks and any material changes in them.[3] However, the traditional reinsurance arrangement typically did not set forth the specific notice that was required, presumably because the continuing relationship between the parties was expected to reveal possible claims on the reinsurance layer substantially in advance of any actual claim. Even modern reinsurance contracts do not require notice of the alleged facts likely to result in loss that is typical of direct insurance; instead, they usually state one of three types of notice provisions and require that the notice itself be in writing.[4]

In the first group of notice provisions are clauses in which notice is triggered by reference to an objective standard. This group includes clauses that refer to set dollar amounts[5]—for example, notice is required where a claim against the cedent "amounts to or exceeds" a stated sum,[6] or where the cedent reserves a claim "in excess of"

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2. *See generally* section 2:2; Am. Bankers Ins. Co. of Fla. v. Nw. Nat'l Ins. Co., 198 F.3d 1332, 1335 (11th Cir. 1999); Christiania Gen. Ins. Corp. v. Great Am. Ins. Co., 979 F.2d 269, 279 (2d Cir. 1992).
3. Unigard Sec. Ins. Co. v. N. River Ins. Co., 4 F.3d 1049, 1057 (2d Cir. 1993) ("Absent such disclosure, reinsurers would have to duplicate actuarial and claims handling efforts of ceding insurers . . . .").
4. *See* GRAYDON S. STARING, LAW OF REINSURANCE § 17:1 at 2 (1993).
5. *Id.*
6. *See* C. GOLDING, THE LAW AND PRACTICE OF REINSURANCE 248 (5th ed. 1987).

a particular retention amount.[7] This group also includes clauses requiring notice of every claim against the cedent of a specified injury or type of loss.

The second category relies a bit more on the cedent's judgment. In this category are triggers such as those claims against the cedent "probably to result in a loss involving" reinsurance,[8] "likely to involve" reinsurance,[9] or in which reinsurance "is or may probably be involved."[10]

In the final group are those clauses that rely on the reinsured's judgment,[11] such as those triggered by the cedent's "estimate"[12] or "judgment"[13] or "reasonabl[e] belie[f]" of those claims or losses or reserves likely to involve reinsurance.[14]

Based upon an analysis of the case law, courts will strive to uphold the literal meaning of the words where the notice trigger is more objective. Thus, clauses of the type contained in the first group have been litigated less often than those of the other two groups, perhaps because the triggering language of the former plainly places the notice duty on the cedent at a time and place that is subject to straightforward evidentiary determination.

Courts have struggled more with the language of the clauses in the latter two groups, and often retreat to finding a reasonableness requirement. For example, the court in *Christiania General Insurance Corp. of New York v. Great American Insurance Co.*,[15] interpreted the phrase "any occurrence or accident which appears likely to involve this reinsurance" to require the cedent to provide notice when there is a "reasonable possibility" of a claim involving the reinsurance "based

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7. *See* Sec. Mut. Cas. Co. v. Century Cas. Co., 531 F.2d 974 (10th Cir.), *cert. denied*, 429 U.S. 860 (1976).
8. *See* Robert F. Salm, *Reinsurance Contract Wording*, REINSURANCE 79, 107 (Robert W. Strain ed., 1987).
9. Unigard Sec. Ins. Co. v. N. River Ins. Co., 79 N.Y.2d 576, 582 (1992); Christiania Gen. Ins. Corp. v. Great Am. Ins. Co., 745 F. Supp 150 (S.D.N.Y. 1990), *aff'd in part*, *rev'd in part*, 979 F.2d 268 (2d Cir. 1992); Travelers Ins. Co. v. Cent. Nat'l Ins. Co., 733 F. Supp. 522 (D.C. Conn. 1990).
10. *See* Keehn v. Excess Ins. Co., 129 F.2d 503 (7th Cir. 1942).
11. STARING, *supra* note 4, at 7.
12. Ins. Co. of Pa. v. Associated Int'l Ins. Co., 922 F.2d 516 (9th Cir. 1990).
13. Sec. Mut. Cas. Co. v. Century Cas. Co., 531 F.2d 974 (10th Cir.), *cert. denied*, 429 U.S. 860 (1976).
14. Travelers Ins. Co. v. Buffalo Reinsurance Co., 735 F. Supp. 492 (S.D.N.Y. 1990), *vacated on reconsideration (on other grounds)*, 739 F. Supp. 209 (S.D.N.Y. 1990).
15. Christiania Gen. Ins. Corp. v. Great Am. Ins. Co., 979 F.2d 268 (2d Cir. 1992).

on an objective assessment of the information available."[16] It should be noted that the notice threshold outlined in *Christiania* is relatively low in that the court found that a "reasonable possibility" may exist even though certain factors indicate otherwise.[17]

The Ninth Circuit in *Insurance Co. of Pennsylvania v. Associated International Insurance Co.*[18] imputed to the cedent a duty to perform all of its obligations under a reinsurance contract reasonably, including the obligation to give notice to the reinsurer, despite a notice provision giving the cedent the subjective power to "estimate the value of the injuries or damages sought" by the direct claimant.[19] The court held that cedents are required to notify the reinsurer when there is an occurrence "that present[s] a 'reasonable possibility' of resulting in a claim under the reinsurance policy."[20]

§ 5:3 What Constitutes Late Notice?

The degree of promptness or lateness of notice to the reinsurer is addressed by reference to the reinsurance contract language, which must be read in conjunction with case law interpretations. Most reinsurance contracts state the temporal requirement clearly. For example, some contracts require the notice to be "prompt"[21] while others require the notice to be "immediate."[22] Unfortunately, this is not the end of the inquiry. An early case held, despite clear contract language, that "immediate" notice means notice within a reasonable time.[23] A more recent decision holds that evidence of custom and usage in the reinsurance business must be allowed as a factor in determining timeliness.[24] Two other cases find that "prompt" means that notice to the reinsurer must be given "within a reasonable time

16. *Id.* at 276 (*citing* Ogden Corp. v. Travelers Indem. Co., 924 F.2d 39, 43 (2d Cir. 1991); Commercial Union Ins. Co. v. Int'l Flavors & Fragrances, Inc., 822 F.2d 267, 272 (2d Cir. 1987)).
17. *Id.* (citing as direct support Trs. of the Univ. of Pa. v. Lexington Ins. Co., 815 F.2d 890, 896 (3d Cir. 1987); Liberty Mut. Ins. Co. v. Gibbs, 773 F.2d 15, 18 (1st Cir. 1985)).
18. Ins. Co. of Pa. v. Associated Int'l Ins. Co., 922 F.2d 516 (1990).
19. *Id.* at 521.
20. *Id.* at 522 (quoting *Gibbs*, 773 F.2d at 17).
21. *Ins. Co. of Pa.*, 922 F.2d. at 518; Fortress Re, Inc. v. Jefferson Ins. Co., 628 F.2d 860, 861 (4th Cir. 1980).
22. Sec. Mut. Cas. Co. v. Century Cas. Co., 531 F.2d 974 (10th Cir.), *cert. denied*, 429 U.S. 860 (1976).
23. Cashau v. Nw. Nat'l Ins. Co., 5 F. Cas. 270, No. 2499 (E.D. Wis. 1873).
24. Travelers Ins. Co. v. Buffalo Reinsurance Co., 739 F. Supp 209 (S.D.N.Y. 1990).

after the duty to give notice had arisen."[25] At least one commentator seems to side with the latter two cases, noting that the time measurement "all seems to come out to a reasonable time."[26]

§ 5:4 Must the Late Notice Prejudice the Reinsurer?

§ 5:4.1 Condition Precedent Versus Covenant

The issue of whether a reinsurance contract's notice provision is intended to be a condition precedent to performance or a mere contractual obligation, has received considerable attention in reinsurance disputes in the early 1990s. The debate originated from a rule, long applied to direct insurers, that prompt notice of an occurrence or claim is a condition precedent to coverage because of the important defense and settlement opportunities that may be lost if notice is untimely.

How the notice provision is characterized determines whether a reinsurer must show that its interests have been prejudiced by the cedent's failure to provide timely notice in order to successfully disclaim all or some of the contract's indemnity requirement. If the notice clause is deemed a condition precedent, no prejudice need be shown. If the clause is treated as a contractual covenant, the reinsurer usually must establish that its interests have been sufficiently prejudiced by the untimely notice before it can disclaim liability.

Discussed below are cases supporting each view. The trend of case law supports the view that the notice clause should be treated as a contractual covenant unless the language of the specific clause explicitly indicates otherwise.[27] Accordingly, the courts increasingly require the reinsurer to show actual prejudice caused by the late notice before allowing forfeiture.

§ 5:4.2 Prompt Notice As a Covenant

The recent trend has found the courts avoiding forfeiture of coverage, in part, by holding that the prompt notice clause is a contractual covenant and thus a bilateral promise of the parties. The courts are

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25. Unigard Sec. Ins. Co. v. N. River Ins. Co., 4 F.3d 1049, 1065 (2d Cir. 1993), *citing with approval* Christiania Gen. Ins. Corp. v. Great Am. Ins. Co., 979 F.2d 268, 275 (2d Cir. 1992). *See also* Sec. Mut. Ins. Co. v. Acker-Fitzsimons Corp., 31 N.Y.2d 436, 441 (1972); Utica Mut. Ins. Co. v. Fireman's Fund Ins. Cos., 748 F.2d 118, 122 (2d Cir. 1984), which were both cited by the court in *Christiania*.
26. STARING, *supra* note 4, at 9.
27. *See Unigard*, 4 F.3d 1049.

seizing on real and perceived distinctions between primary insurance policies and reinsurance contracts, and upon the intent of the respective parties. Much of this development has come from courts interpreting New York law and its seminal case, *Unigard*.[28]

As recently as 1990, the law of New York remained unsettled in this regard. That year, one court found that a reinsurance contract's prompt notice provision was a condition precedent because "the New York rule treating notice as a condition precedent in the primary insurance context is unmistakably clear" and there was no "meaningful distinction between the notice provisions in a contract of primary insurance and a contract of reinsurance."[29] That same year, however, another judge in the same court came to the opposite conclusion, finding that "a reinsurer must show prejudice from late notice before it can be excused from its liability under the reinsurance contract" because the "policy considerations" underlying the primary insurance rule are not present in a reinsurance contract.[30]

In 1992, the Court of Appeals of New York, the state's highest court, recognized the split of authority and resolved it at the request of the federal courts. In *Unigard Sec. Ins. Co., Inc. v. North River Ins. Co.*,[31] the court answered the certified question "[m]ust a reinsurer prove prejudice before it can successfully invoke the defense of late notice of loss by the reinsured" in the affirmative.[32]

The opinion arose out of a declaratory judgment action commenced by Unigard against North River in connection with hundreds of asbestos-related claims against the underlying policyholder, Owens-Corning. North River wrote a $30 million excess liability policy for Owens-Corning that attached at $76 million of underlying primary and lower-level excess policies. Unigard and North River had negotiated a facultative reinsurance certificate for the excess policy that required "[p]rompt notice . . . of any occurrence or accident which appears likely to involve this reinsurance."[33] The certificate specified that Unigard had "the right and . . . opportunity to associate with

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28. *Id.*
29. Travelers Ins. Co. v. Buffalo Reinsurance Co., 735 F. Supp. 492, 499, *vacated on reconsideration (on other grounds)*, 739 F. Supp. 209 (S.D.N.Y. 1990).
30. Christiania Gen. Ins. Corp. v. Great Am. Ins. Co., 745 F. Supp. 150, 159 (S.D.N.Y. 1990), *aff'd*, 979 F.2d 268 (2d Cir. 1992) (affirmation concerned the notice prejudice portion of its ruling).
31. Unigard Sec. Ins. Co. v. N. River Ins. Co., 79 N.Y.2d 576 (1992).
32. *Id.* at 581.
33. *Id.* at 579.

[North River] . . . in the defense and control of any claim, suit or proceeding which may involve this reinsurance."[34]

The Court of Appeals began the analysis by noting that the "no prejudice" rule, which applies in New York to the notice provisions of primary insurers, is

> a limited exception to two established rules of contract law: (1) that ordinarily one seeking to escape the obligation to perform under a contract must demonstrate a material breach or prejudice; . . . and (2) that a contractual duty ordinarily will not be construed as a condition precedent absent clear language showing that the parties intended to make it a condition.[35]

The court found it useful to rephrase the certified question as: "[D]o the same reasons for adopting the 'no prejudice' exception to the general rules of contract for primary insurers apply to reinsurers?"[36]

The court first noted that the reinsurance certificate contained no language whatsoever expressing an intention that the notice provision be a condition precedent to the reinsurance.[37] Thus, the second limited exception noted above did not apply and, "[i]f the ordinary rules of contract were applied, the prompt notice provision in the North River certificate would not be construed as a condition precedent."[38]

The court then outlined factors distinguishing the function of reinsurance from that of primary insurance. A reinsurer has no duties to any insured, only to the cedent; thus, a reinsurer is not required to provide a defense, investigate the claim, take control of the claim, or settle it.[39] While these factors make it vitally important that the primary insurer be given prompt notice, they are of "substantially less significance" for a reinsurer.

However, the court found many common interests between a reinsurer and its cedent concerning the handling of a claim, while finding that the interests of insureds and primary insurers are often adverse. For example, while under most reinsurance contracts the reinsurer cannot dispute the primary insurer's management of a claim, under direct insurance policies the insurer's claims management may be disputed by the insured or the insurer may dispute the

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34. *Id.*
35. *Id.* at 581.
36. *Id.* at 582.
37. *Cf.* Constitution Reinsurance Corp. v. Stonewall Ins. Co., 980 F. Supp. 124 (S.D.N.Y. 1997) (discussed *infra* note 50).
38. *Unigard Sec. Ins. Co.*, 79 N.Y.2d at 582.
39. *Id.* at 583.

insured's cooperativeness. These factors, too, make prompt notice to the primary insurer important but have "greatly diminished application to the reinsurer."[40]

In its conclusion, the court said that "[t]his is not to suggest that a reinsurer may never assert late notice as a ground for avoiding its obligations under a reinsurance contract . . . . [T]he reinsurer must demonstrate how [the late notice] was prejudicial and may not rely on the presumption of prejudice that applies in the late notice disputes between primary insurers and their insureds."[41] This answer to the certified question was later adopted by the Second Circuit in its subsequent ruling in the dispute between Unigard and North River.[42]

The *Unigard* opinion makes clear that New York and the Second Circuit will follow the lead of several other states and interpret most reinsurance certificates as ordinary contracts in which the reinsurer has the burden of proving prejudice before it is entitled to avoid liability because of late notice, presuming, of course, that the notice provisions do not include unambiguous condition precedent clauses. For example, cases interpreting the laws of Colorado, Connecticut, North Carolina, and California require the reinsurer to show prejudice.[43]

In 2003, the Third Circuit predicted that the New Jersey Supreme Court would extend to reinsurance contracts the rule requiring prejudice to support the defense of late notice.[44]

§ 5:4.3 Reinsured's Bad Faith As a Substitute for Prejudice

In the *Unigard* case, as discussed above, the Second Circuit found that the reinsurer failed to prove prejudice due to untimely notice, as mandated by New York reinsurance law. Nevertheless, the Second

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40. *Id.*
41. *Id.* at 584.
42. Unigard Sec. Ins. Co. v. N. River Ins. Co., 4 F.3d 1049 (2d Cir. 1993).
43. Sec. Mut. Cas. Co. v. Century Cas. Co., 531 F.2d 974 (10th Cir.), *cert. denied*, 429 U.S. 860 (1976) (Colo. law); Travelers Ins. Co. v. Cent. Nat'l Ins. Co., 733 F. Supp. 522 (D.C. Conn. 1990); Fortress Re, Inc. v. Cent. Nat'l Ins. Co., 766 F.2d 163 (4th Cir. 1985) (N.C. law); Ins. Co. of Pa. v. Associated Int'l Ins. Co., 922 F.2d 516 (9th Cir. 1990) (Cal. law). *See also* STARING, *supra* note 4, at 11–13; B. OSTRAGER & T. NEWMAN, HANDBOOK ON INSURANCE COVERAGE DISPUTES, § 16.02[b] (6th ed. 1993); *Should 'No Prejudice' Rule Be Abolished?* N.Y.L.J. (Jan. 13, 1997); A. Gang, *Developments in Litigation Involving Reinsurers, Cedents and Insureds*, REINSURANCE LAW AND PRACTICE, at 101 (PLI Litig. & Admin. Practice Course Handbook Series No. 546, 1996).
44. British Ins. Co. v. Safety Nat'l Cas. Corp., 335 F.3d 205 (3d Cir. 2003).

Circuit noted that "a [ceding insurer's] failure to provide prompt notice may entitle the reinsurer to relief without showing prejudice if the [ceding insurer] acted in bad faith."[45] The court in *Unigard* held that a reinsurer must demonstrate gross negligence or recklessness in the content of notice in order to prove bad faith. In explaining this standard, the court stated:

> If a ceding insurer deliberately deceives a reinsurer, that deception is of course bad faith. However, if a ceding insurer has implemented routine practices and controls to ensure notification to reinsurers but inadvertence causes a lapse, the insurer has not acted in bad faith. But if a ceding insurer does not implement such practices and controls, then it has willfully disregarded the risk to reinsurers and is guilty of gross negligence. A reinsurer, dependent on its ceding insurer for information, should be able to expect at least this level of protection, and, if a ceding insurer fails to provide it, the reinsurer's late loss notice defense should succeed.[46]

In *Unigard*, the Second Circuit found that North River's late notice was the result of mere negligence, as North River had a policy and practice that required notice of asbestos-related claims. Thus, Unigard was not relieved of its indemnity obligation to North River.

More recently, in *Certain Underwriters at Lloyd's London v. Home Insurance Co.*,[47] the New Hampshire Supreme Court adopted the *Unigard* rule that untimely notice due to gross negligence or recklessness relieves a reinsurer from liability. The court found that Home did not attempt to determine whether reinsurance was available until eleven years after it received notice of a potential loss. Apparently, Home had no formal guidelines for determining what claims should be reported to reinsurers. The court affirmed the trial court's determination that "Home acted in bad faith by failing to implement notification practices, procedures and controls."[48]

Clearly, in the aftermath of *Unigard* and *Home*, cedents should implement and enforce written policies and procedures with respect to claim notification to reinsurers. Those procedures should set forth

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45. *Unigard*, 4 F.3d at 1069 (quoting Christiania Gen. Ins. Corp. v. Great Am. Ins. Co., 979 F.3d 268, 281 (2d Cir. 1992)).
46. *Unigard*, 4 F.3d at 1069
47. Certain Underwriters at Lloyd's London v. Home Ins. Co., No. 99-473, slip op. at 3 (N.H. Sept. 6, 2001).
48. *Id. See also* Newcap Ins. Co. v. Emp'rs Reinsurance Corp., 295 F. Supp. 2d 1229 (D. Kan. 2003) (while the cedent failed to provide timely notice, a genuine issue of fact existed on the question whether prejudice should be excused by virtue of the cedent's alleged gross negligence or recklessness).

clearly what types of claims should be reported, to whom they should be reported, and how such reporting can be tracked and monitored.

§ 5:4.4 Prompt Notice As a Condition Precedent

Until 1997, no case answered the question left open by *Unigard*, in which a reinsurance contract expressly stated that prompt notice was a condition precedent to coverage. The *Unigard* court's response to the federal court's certified question was limited to the specific language contained in the North River reinsurance certificate, which did not contain explicit condition precedent language. The *Unigard* court strongly intimated that a different conclusion could have resulted had the certificate specifically provided that notice was a condition precedent.[49]

Well before *Unigard*, there were cases in which the reinsurer strenuously asserted that its contract's notice language was a condition precedent. In *Security Mutual Casualty Co. v. Century Casualty Co.*,[50] for example, the court rejected the reinsurer's assertion that its contract language was similar to standard condition precedent language found in primary insurance, stating that it was "significant . . . that none of the usual words indicating a condition precedent are present."[51] The court found that a notice provision will not be deemed a condition precedent "unless that intention is clearly and unequivocally stated in the contract;" it is safer to so construe ambiguous terms "because it avoids forfeitures."[52]

On the other hand, several cases held that the prompt notice clause was a condition precedent even in the absence of express language stating the condition. In one case decided under Illinois law, the reinsurer was deemed prejudiced by the reinsured's untimely notice because the reinsurer was deprived of its contract rights to cooperation from the reinsured and of the right and opportunity to associate with the reinsured in the defense of the underlying claim.[53]

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49. Unigard Sec. Ins. Co. v. N. River Ins. Co., 79 N.Y.2d 576, 582 (1992) (citing Liberty Mut. Ins. Co. v. Gibbs, 773 F.2d 15, 16–17 (1st Cir. 1985), where the certificate at issue provided that notice "is a condition precedent to any liability under this policy" and the court held that lack of prejudice did not preclude reinsurer's assertion of a late notice defense).
50. Sec. Mut. Cas. Co. v. Century Cas. Co., 531 F.2d 974 (10th Cir.), *cert. denied*, 429 U.S. 860 (1976).
51. *Id.* at 977.
52. *Id.* at 976–78. Note that the court then avoids making a prejudice analysis that, in later cases, would normally follow a finding that the late notice clause is a covenant of the contract.
53. Keehn v. Excess Ins. Co., 129 F.2d 503 (7th Cir. 1942). The contract at issue merely stated that "[t]he Company shall notify the Reinsurer immediately after it has had notice of any accident in which this reinsurance is or may probably be involved." *Id.* at 504.

Another reinsurance case, construing Massachusetts and Texas law, echoed this rationale, stating that "the notice provisions in both [direct insurance and reinsurance] contracts serve . . . to afford a company which may be ultimately liable on a claim the opportunity to participate in the defense of that claim."[54] The result in these cases has been that the reinsurer is entitled to deny coverage merely upon showing that it was given late notice under its contract. In such cases, the argument turns on sufficient proof of lateness or the absence of promptness to establish essentially, a finding of prejudice per se.

In 1997, however, almost four years after *Unigard*, the District Court of the Southern District of New York answered the question *Unigard* left open. In *Constitution Reinsurance*, the court was presented with a reinsurance contract which expressly stated that prompt notice was a condition precedent.[55] Confirming *Unigard*'s limited scope, the court stated that where a prompt notice provision clearly indicates that it is intended to serve as a condition precedent, the reinsurer need not demonstrate prejudice.[56]

In *Pacific Employers Insurance Co. v. Global Reinsurance Corp. of America*,[56.1] the Third Circuit Court of Appeals considered whether to apply New York or Pennsylvania law to a reinsurance dispute. Applying New York law, the court found that the reinsurer was not required to demonstrate prejudice in order to prevail on a late notice defense. The reinsurance contract required prompt notice as a "condition precedent" to reinsurance coverage. Pennsylvania law likely would have required a showing of prejudice, suggesting that choice of law should be carefully considered during contract drafting.

§ 5:4.5 Where Prejudice Is Required, What Constitutes Prejudice?

Perhaps surprisingly, there are relatively few cases defining what constitutes prejudice or what level of prejudice must be shown by a

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54. Highlands Ins. Co. v. Emp'rs' Surplus Lines Ins. Co., 497 F. Supp. 169, 173 n.3 (E.D. La. 1980). The contract at issue merely required prompt notice, but went on to say that the reinsurer shall "have the right and be given the opportunity to associate with the Company and its representative at its own expense in the defense and control of any claim, suit or proceeding involving this reinsurance with full cooperation of the Company." *Id.* at 171.

55. *See* Constitution Reinsurance Corp. v. Stonewall Ins. Co., 980 F. Supp. 124 (S.D.N.Y. 1997) (contracting around *Unigard*, the Constitution Reinsurance policy stated: "As a condition precedent, the Company shall promptly provide the Reinsurer with a definitive statement of loss.").

56. *Id.* at 130. *See also* Christiania Gen. Ins. Corp. v. Great Am. Ins. Co., 979 F.2d 268, 273 (2d Cir. 1992).

56.1. Pac. Empr's Ins. Co. v. Global Reinsurance Corp. of Am., 693 F.3d 417 (3d Cir. Pa. 2012).

reinsurer seeking to avoid coverage on the grounds of late notice. Of these few, several have become dated as their rulings have been challenged and distinguished by more recent decisions in other jurisdictions.

More recent cases tend to require proof of a tangible harm resulting from the late notice in order for a reinsurer to prevail on the defense. The older cases, however, focus more on the prejudice of an involuntary forfeiture of a right without actual proof of harm. For example, one found that "the deprivation of [a reinsurer's right to associate in the defense of a case] would constitute prejudice without any actual proof that the results of the litigation would have been different."[57] In another, notice delayed eight months was deemed highly prejudicial, where the delay also had the effect of denying the reinsurer the right to assist the insurer and to negotiate a fair settlement.[58] *Fortress Re, Inc. v. Central National Insurance Co. of Omaha*,[59] held that the reinsurer must show both that it actually would have associated with the insurer had it received timely notice and that this association would have resulted in a more favorable ruling.[60] *Insurance Co. of Pennsylvania v. Associated International Insurance Co.*[61] required the reinsurer to demonstrate that there was a "substantial likelihood" that it could have either defeated the underlying claim or settled it more favorably, had it been given timely notice.[62] Another case interpreting Connecticut law found that, in order to establish prejudice, the reinsurer must show that the cedent's late notice adversely affected the reinsurer's reserving and its ability to obtain payment from its own retrocessionaires.[63] That case also found that the reinsurer must have the actual means to participate in the defense of the underlying case—for example, the facilities, the personnel, an established practice of such participation—before the court will entertain an argument that the insurer's late notice prejudiced the reinsurer's contractual right to "be given the opportunity to associate with [the insurer] and its representatives . . . in the defense and control of any claim, suit or proceeding involving this reinsurance."[64]

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57. Keehn v. Excess Ins. Co., 129 F.2d 503, 505 (7th Cir. 1942) (Ill. law).
58. Stuyvesant Ins. Co. v. United Pub. Ins. Co., 221 N.E.2d 358, 362 (Ind. Ct. App. 1966) (Ind. law).
59. Fortress Re, Inc. v. Cent. Nat'l Ins. Co., 766 F.2d 163 (4th Cir. 1985).
60. *Id.* at 166–67.
61. Ins. Co. of Pa. v. Associated Int'l Ins. Co., 922 F.2d 516 (9th Cir. 1990).
62. *Id.* at 524.
63. Travelers Ins. Co. v. Cent. Nat'l Ins. Co., 733 F. Supp. 522, 530 (D. Conn. 1990).
64. *Id.* at 524, 529–30.

Unigard appears to be the most recent case to define what prejudice must be shown. The reinsurer argued that its loss of the right to associate with the insurer constituted the requisite prejudice, though it conceded that it could not show an actual economic loss. Relying on the New York Court of Appeals' prior opinion that answered a certified question in the case, the Second Circuit found that the reinsurer "bears the burden of showing that it suffered tangible economic injury" as a result of the untimely notice.[65] What constitutes tangible economic injury was not addressed.

More recently, a New York federal court rejected a reinsurer's claim of tangible economic harm to support a showing of prejudice.[66] First, the court ruled that the reinsurer's alleged inability to provide prompt notice to its retrocessionaires did not constitute tangible economic harm, particularly since the retrocessionaires themselves did not assert late notice as a defense. Second, the court rejected a claim that the cedent's late notice caused it to post untimely reserves. The court found any such reserve deficiency was inconsequential. Third, the court dismissed the argument by the reinsurer's that its relationship with the broker and cedent was harmed by virtue of the untimely notice.

One commentator warns that "results will differ radically, according to the state in which a notice clause falls to be interpreted and applied."[67] Clearly this is so. While states such as Illinois appear to presume prejudice from a showing of mere lack of opportunity to associate with the insurer, other states, such as California, seem to require the reinsurer to prove the impossible, for example, that a case would have been successfully defended or settled more cheaply had it been given timely notice. The commentator suggests that these cases ignore a middle ground,[68] which he finds best considered by *Christiania General Insurance Corp. of New York v. Great American Insurance Co.*[69] The court in *Christiania*, construing New York law, did not directly decide whether the reinsurer was prejudiced by late notice. However, in dicta that discuss the notice requirement, the court implied that the reinsurer would be prejudiced if it could show

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65. Unigard Sec. Ins. Co. v. N. River Ins. Co., 4 F.3d 1049, 1069 (2d Cir. 1993).
66. Folksamerica Reinsurance Co. v. Republic Ins. Co., 2003 WL 22852737 (S.D.N.Y. Dec. 2, 2003).
67. STARING, *supra* note 4, at 16.
68. *Id.*
69. Christiania Gen. Ins. Corp. v. Great Am. Ins. Co., 979 F.2d 268 (2d Cir. 1992).

that late notice deprived it of the opportunity not only to associate in the defense of a matter, but also to set reserves properly on a portfolio of claims (if treaty reinsurance) or on a particular claim (if facultative reinsurance), and to set its own premiums.[70]

The prejudice standard implied in *Christiania* appears not to require the "tangible economic injury" required by the Second Circuit in *Unigard*. However, while New York law may be somewhat unsettled until some future case resolves this conflict, a general trend may be seen arising from these two cases. The utmost good faith doctrine continues to be eroded; reinsurers with contracts interpreted under New York law or under the law of similar jurisdictions must be prepared to demonstrate economically based injuries or, at a minimum, something more than mere loss of opportunity to associate in the defense of the matter, if they hope to successfully deny coverage from a cedent for untimely notice or bad faith by the cedent. While this trend appears to be adverse to the interests of reinsurers, it may result in better opportunities for them to be informed earlier, even if incompletely, of matters or portfolios that may impact the reinsurance layer.

§ 5:5 Reinsurer's Remedies for Late Notice

Once late notice is established, the courts have generally not hesitated to follow the terms of the reinsurance contract at issue. This is demonstrated in several ways.

In those states where the prompt notice clause is deemed a condition precedent to recovery, summary disposition in favor of the reinsurer has been the result. For example, a court presented with a notice clause explicitly stated to be a condition precedent to liability found the wording unambiguous and upheld the trial court's jury instructions. "We see no basis for rewriting the contract whether or not, as an original proposition, it could have been better written . . . ."[71] Under an earlier interpretation of North Carolina law, another opinion found that "[the cedent] should be held to a higher standard of compliance with the importance of fulfilling its contractual notice requirements . . . . The unexplained delay is therefore fatal . . . and . . . plaintiff's summary judgment motion must be granted."[72]

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70. *Id.* at 277.
71. Liberty Mut. Ins. Co. v. Gibbs, 773 F.2d 15, 17 (1st Cir. 1985).
72. Fortress Re, Inc. v. Jefferson Ins. Co., 465 F. Supp. 333, 338 (E.D.N.C. 1978), *aff'd*, 628 F.2d 860 (4th Cir. 1980). Note that North Carolina law now requires the reinsurer to show prejudice. *See* Fortress Re, Inc. v. Cent. Nat'l Ins. Co., 766 F.2d 163 (4th Cir. 1985).

Similar results occur in those jurisdictions where prejudice, which is nominally required by the court to be shown by the reinsurer, is deemed proven without evidence of actual harm.[73] In one such case, a judgment of no liability was upheld even though the reinsurance contract contained no declaration of forfeiture for noncompliance.[74]

In contrast, those jurisdictions requiring the reinsurer to prove some tangible prejudice have not yet had occasion to rule on the reinsurer's remedy once prejudicially late notice is established. There is reason to believe, however, that at least some such jurisdictions would follow the terms of the reinsurance contract and deny liability to the cedent. The New York Court of Appeals in *Unigard* said that "a breach will excuse performance only if it is material or demonstrably prejudicial . . . . This is not to suggest that a reinsurer may never assert late notice as a ground for avoiding its obligations under a reinsurance contract . . . ."[75]

On the other hand, perhaps to avoid forfeiture, courts in these jurisdictions have recently begun to consider recasting the language of the reinsurance contract in favor of granting damages. As early as 1976, one court said, in dicta, that "[h]ad [the reinsurer] shown any pecuniary injury from [the cedent's] failure to give [the reinsurer] notice, we believe damages would have been an adequate remedy. Our construction of the contract does not deny the reinsurer the protection it needs, and it does give the reinsured the security and returns for which it paid."[76] Lastly, the Second Circuit's opinion in *Unigard* also appears to entertain damages as a proper remedy. The "tangible economic injury" prejudice standard set forth in the case clearly implies that any reinsurer demonstrating such an injury would be entitled to recover damages from the cedent in lieu of avoiding coverage.[77]

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73. Keehn v. Excess Ins. Co., 129 F.2d 503 (7th Cir. 1942) (Ill. law) (affirming trial court's judgment for defendant); Stuyvesant Ins. Co. v. United Pub. Ins. Co., 221 N.E.2d 358 (Ind. Ct. App. 1966) (Ind. law) (reversing and remanding for new trial).
74. *Keehn*, 129 F.2d at 504.
75. Unigard Sec. Ins. Co. v. N. River Ins. Co., 79 N.Y.2d 576, 582 (1992).
76. Sec. Mut. Cas. Co. v. Century Cas. Co., 531 F.2d 974, 978 (10th Cir.), *cert. denied*, 429 U.S. 860 (1976) (Colo. law). Note, however, that the reinsurance contract did not contain language deeming timely notice to be a condition precedent. *See also* Ins. Co. of Pa. v. Associated Int'l Ins. Co., 922 F.2d 516, 525 (9th Cir. 1990) (Cal. law).
77. Unigard Sec. Ins. Co. v. N. River Ins. Co., 4 F.3d 1049, 1069 (2d Cir. 1993).

Thus we see that courts may find that complete forfeiture of coverage is too harsh. One commentator observes that the English courts have begun requiring the reinsurer to pay the full amount due under the reinsurance contract, but then allow the reinsurer to recover damages from the reinsured for the harm it suffered.[78] The American cases do not appear to appreciate the difficulty of assessing the value of the damages or the harm suffered by the reinsurer.[79]

§ 5:6 Conclusion

The recent decisions concerning late notice to the reinsurer, including both of the *Unigard* decisions and their predecessors, support the observations that reinsurance is certainly becoming more contractual in nature and is losing its clubby informality. While there will be as many who view this development with alarm as with satisfaction, it can safely be predicted that this development will continue to evolve. As discussed above, this evolution seems based on the courts' desire to see concrete language in reinsurance contracts. The notice that is triggered by reference to a set dollar amount or a specific event is less likely to be deemed ambiguous than other constructions. Likewise, the contract that fails to specify that timely notice is a condition precedent to coverage in a particular circumstance clearly invites a court to require the reinsurer to show some tangible prejudice.

However, there are few endeavors less amenable to clear prediction than judicial decision-making, particularly in the field of reinsurance. It is not clear that the insertion of specific condition precedent wording into the notice requirement will always insure that untimely notice forfeits coverage. The question of "timeliness" is unpredictable, and even if forfeiture of coverage is quite clearly stated to be the remedy for untimely notice, courts may search for ways to recast the remedy as one for damages.

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78. J. BUTLER & R. MERKIN, REINSURANCE LAW § C.4.2 at 3 (Revised ed. 1994).

79. STARING, *supra* note 4, at 16. The commentator notes:

> Whether the records in [these cases] provide support for the idea that damages could be a plausible remedy is hard to say . . . . In the ordinary, simple case, such damages lie somewhere between zero and the amount of the loss, less the litigation expense of the reinsured in contesting the claim. Experienced trial counsel will recognize the difficulty in showing what degree of improvement or advantage might have been achieved as between those two figures by the timely counsel of the reinsurer . . . . There is undoubtedly great damage in the financial disorder and loss of confidence that results from being grossly underreserved but the proof of it will be complex and probably expensive.

Clearly, reinsurers must become sensitized to these trends and consider meeting them with firmer contract language, greater vigilance in monitoring their cedent's communications, and attention to establishing prejudicial injury. If reinsurers accept these challenges, there is growing evidence that the courts will begin to demand earlier and more thorough notice from cedents.