



NEW TEXAS COVERAGE CASE ALERT – March 8, 2011

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The Difficulty in Proving “Prejudice” from Late Notice of Claims and Suits

In most jurisdictions, Texas included, the insured’s breach of the policy’s notice requirements will only result in forfeiture of coverage if the insurer can prove that the late notice “prejudiced” the insurer. The Texas Supreme Court’s 2009 opinion in *Prodigy Comm. Corp. v. Agric. Excess and Surplus Ins. Co.*, 288 S.W.3d 374 (Tex. 2009), even extends the prejudice requirement to “claims made” policies (assuming, if required, that the claim is at least made and reported within the policy period). While Texas courts have easily found prejudice as a matter of law where notice of the suit is not provided until after there has already been a default judgment entered against the insured, most late notice scenarios are really just delayed notice situations and are not as clear.

What if there has not been a default judgment but the insurer can point to things in hindsight that it arguably would have done differently in directing or, at least, participating in, the insured’s defense had it been afforded the earlier opportunity to do so? A recent Texas federal district court opinion attempts to answer that question and is a reminder of how difficult it is for an insurer to prevail on a late notice defense.

In *East Texas Med. Center v. Lexington Ins. Co.*, Civ. Action No. 6:04-CV-165 (E. D. Texas—Tyler Division, Feb. 25, 2011), the insured hospital handled its own medical malpractice claims within a \$2 Million SIR but had a first-level excess policy that gave Lexington the right to “participate” in the defense of any suit that might implicate its coverage. The policy required written notice of medical incidents, claims or lawsuits “as soon as practicable” and that the hospital “immediately” send copies of legal process and suits. A malpractice suit was filed on May 27, 2003, two weeks before the policy expired. The hospital undertook its own defense and did not notify Lexington. In December 2003, three hospital nurses were deposed and conceded negligence. The hospital then provided first notice of the suit to Lexington in late January 2004, *i.e.*, 8 months after the suit was filed. Lexington denied coverage based on late notice. The court, in the malpractice case thereafter, ruled that the hospital was negligent as a matter of law and that such negligence caused plaintiff’s injuries. The hospital, Lexington (and excess carriers above Lexington) then settled the underlying case under a joint funding agreement that preserved Lexington’s coverage dispute.

Lexington argued prejudice from the loss of its right to “participate” in the defense before the nurses were deposed. It argued that it would have hired monitoring counsel to assist the insured’s counsel in the defense and in preparing witnesses for deposition, and would have made sure that the nurses were familiar with helpful information in the medical records. However, Lexington’s actual proof, in the form of internal memos and evidence from other cases where monitoring counsel had been hired, did not show that Lexington would have actually participated in witness preparation and instead showed only that Lexington would have closely monitored activity in the case. According to the court, even if Lexington’s counsel would have actively assisted in deposition preparation, it was still speculative as to whether Lexington’s participation would have, in fact, led to a different result. According to the court, Lexington had to show not only that it lost a valuable right to participate in the case in a timely manner, but that if it had, the outcome would have actually been different.



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PRACTICE POINTERS: Before a claim can be denied based on late notice, the insurer must be able to marshal strong and clear evidence of how the lack of timely notice has *actually* and *demonstrably* resulted in a less favorable outcome for the insured. Neither hypothesizing nor arguing about how things *might* have been different had notice been provided sooner is enough; nor is being able to point to some lost right that the insurer could have exercised. There must be an *actual, factual and provable* causation link between the late notice, the right to act that was lost and how that lost right to act caused actual harm to the case.

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