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Illinois Appellate Court Finds that No Prejudice is Required to Deny Coverage for Late Notice

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In *Country Mutual Ins. Co. v. Gaffrig Performance Industries,* 2004 Ill App. LEXIS 1412 (Nov. 30, 2004; First Appellate District), the court addressed the issue of prejudice in a declaratory judgment action that was based upon late notice of a lawsuit. The court found that an insurer need not prove it was prejudiced by unreasonably late notice of a lawsuit in order to properly deny coverage.

In *Gaffrig,* two of County Mutual Insurance Company's insureds were involved in litigation against each other. Both the complaint and counter-complaint were filed on December 1, 1999, alleging trademark infringement, dilution, consumer fraud, and unfair competition. Neither insured notified County Mutual of the lawsuits until after the suits were tried, or about 21 months after the action was filed. Both insureds admitted that notice of the lawsuits was unreasonably late.

Illinois appellate courts have maintained varying views on whether an insurance company is obligated to prove prejudice to deny a claim based upon late notice. The First Appellate District has addressed this issue, answering the following question: "When an insured is required by its contract …to give timely notice of a lawsuit against it, but does not do so and has no excuse for doing it, does the insurer have to prove prejudice before it can avoid coverage?" In ruling that the insurer does not have to prove prejudice before avoiding coverage, the court distinguished a line of cases based upon the dictum of *Rice v. AAA Aerostar, Inc.* 194 Ill App. 3d 801; 690 NE2d 1067 (Feb. 9, 1998; Fourth Appellate District).

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The lack of a tender by the insured does not relieve the insurer of its duty to defend if the insurer had "actual notice" of the underlying suit. "Actual notice" means that the insurer knew both "that a cause of action has been filed and that the complaint falls within or potentially within the scope of the coverage of one of its policies." Thus, a carrier with knowledge of a claim may not deny coverage on the basis of late notice just because an insured fails to timely tender it.

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The court reasoned that the insurance contract controls the insured's duties, and that when the contract includes a provision requiring the insured to notify the insurer of a suit against it, that provision is a "condition precedent" to the triggering of the insurer's contractual duties. Thus, when the insured fails to comply with the notice provision, the insurer may be relieved of its duty to defend.

The Court's View of What is "Late:" When notice is to be given "as soon as practicable", notice must be given within a reasonable time. Prejudice to the insurer "is a factor to consider" when the issue is whether notice of an occurrence was reasonable. Specifically, the court held that while an insurer's failure to prove prejudice was a *factor* to consider in determining whether an insured's notice of either an occurrence or a lawsuit was unreasonably and inexcusably late, once it was determined that the notice was unreasonably late, the failure of the insurer to prove it suffered prejudice was irrelevant as to either type of notice, and coverage did not have to be extended. The court did differentiate between "notice of occurrence" and "notice of suit," implying that late notice of suit was a more serious matter as it deprived the insurer of "an opportunity to assess the loss and thereby protect its interests."

Gaffrig included a comprehensive review of other Illinois cases on this subject. It should prove to be persuasive authority to all circuit courts that address this issue. However, there may be tension between *Gaffrig* and the earlier Illinois Supreme Court case *Employers Insurance of Wausau v. Ehlco Liquidating Trust,* 186 Ill. 2d 127 (1999). The court in *Employers Insurance* held that a carrier that improperly fails to defend *waives all policy defenses, including late notice.*

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We welcome your questions and comments.

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