Portfolio Media. Inc. | 860 Broadway, 6th Floor | New York, NY 10003 | www.law360.com
Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

Colo. Justices Reject Expansion Of Notice-Prejudice Rule

By **Jeff Sistrunk**

Law360, Los Angeles (April 25, 2016, 11:50 AM ET) -- Colorado's high court ruled Monday that policyholders that settle presuit claims without an insurance carrier's permission can't win coverage, rejecting an expansion of the state's notice-prejudice rule, which requires liability insurers to show that they suffered prejudice from late notice of a claim before they can deny coverage on that basis.

In a 4-3 opinion, the Colorado Supreme Court overturned an intermediate appeals court's September 2013 decision in concrete company Stresscon Corp.'s insurance coverage battle with Travelers Property Casualty Co. of America stemming from a construction accident near Colorado Springs that killed one worker and seriously injured another. The suit focused on coverage for Stresscon's settlement with a general contractor over project delays caused by the accident, a deal that was struck before the contractor filed suit.

The appellate court had found that Colorado's notice-prejudice rule should be extended to cases where policyholders violate a clause in liability policies barring them from voluntarily settling claims or making payments without the insurer on board, but the state high court majority rejected that finding.

The notice-prejudice rule does not apply to "no-voluntary-payments" policy provisions such as the one at issue in this case, and Stresscon is not entitled to coverage for its deal with the contractor, the majority opinion said. It said an insurer's denial of coverage due to a policyholder's failure to comply with a no-voluntary-payment provision is not just a technicality.

"This so-called 'no voluntary payments' clause clearly excluded from coverage any payments voluntarily made or obligations voluntarily assumed by the insured without consent, for anything other than first aid," Justice Nathan B. Coats wrote for the majority. "The insurance policy emphatically stated that any such obligations or payments would be made or assumed at the insured's own cost rather than by the insurer."

Under the notice-prejudice rule, when a policyholder notifies an insurer of a claim only after settling the claim, there's a presumption that the insurer has suffered prejudice from that conduct. The policyholder then will lose coverage unless it rebuts the presumption, at which point the burden falls on the insurer to prove it suffered actual prejudice.

In Travelers' dispute with Stresscon, the primary issue was whether the rule should be extended to cases where a policyholder violates a no-voluntary-payments clause in a liability policy.

The intermediate appeals court said that the notice-prejudice rule does apply to such clauses, relying on the Colorado Supreme Court's 2005 decision in Friedland v. Travelers, in

which the court extended the rule to liability policies.

However, on Monday the high court said that the appellate court had misinterpreted the 2005 ruling, noting that, unlike the Stresscon case, the Friedland matter had dealt with a policyholder's failure to give timely notice of a claim. That decision does not implicitly extend the notice-prejudice rule to no-voluntary-payments or similar "consent-to-settle" provisions, it said.

The no-voluntary-payments clause is "far from a mere technicality" — rather, it fundamentally defines the limits and extent of coverage in Stresscon's policy, the majority found. If the court accepted Stresscon's arguments, insurers would effectively be denied the ability to have a say in defending their policyholders against third-party claims or negotiating settlements of those claims, the opinion said.

"Because our adoption of a notice-prejudice rule in Friedland did not overrule any existing 'no voluntary payments' jurisprudence in this jurisdiction, and because we decline to extend our notice-prejudice reasoning in Friedland to Stresscon's voluntary payments, made in the face of the no-voluntary-payments clause of its insurance contract with Travelers, the judgment of the court of appeals is reversed," it said.

In a dissent, Justice Monica Marquez disagreed that a no-voluntary-payments clause dictates the scope of coverage in Stresscon's policy.

"Instead, where, as here, the insured's breach of a provision deprives the insurer of adequate opportunity to defend or settle a claim, the insured should be afforded an opportunity to rebut a presumption that the insurer suffered actual prejudice," Justice Marquez wrote.

Stresscon filed suit against Travelers several months after reaching its settlement with general contractor Mortenson Construction, alleging that the insurer had unreasonably denied its claim for benefits in bad faith. The suit's filing was the first time that Travelers learned of the settlement, according to court documents.

A state jury found that Travelers had unreasonably denied Stresscon's claim, that the insurer hadn't been prejudiced by the settlement and that nearly $547,000 of an earlier jury award against two subcontractors was covered by the policy. An appellate court affirmed the judgment against the insurer.

Sean Connelly of Zonies Law LLC, who represents Stresscon, asserted that his client had been victimized by "bad faith insurance practices."

"Three dissenting justices and four lower court judges agreed with our client's legal position," Connelly said. "We are exploring options to preserve the jury's verdict."

An attorney for Travelers declined comment, while a Travelers representative did not immediately respond to a request for comment.

Stresscon is represented by Sean Connelly of Zonies Law LLC and by Bret Gunnell, Katherine Varholak and Brooke Yates of Sherman & Howard LLC.

Travelers is represented by Malcolm E. Wheeler and Evan B. Stephenson of Wheeler Trigg O'Donnell LLP.

The case is Stresscon Corp. v. Travelers Property Casualty Co. of America, case number 2013SC815, in the Supreme Court of the State of Colorado.

--Editing by Sarah Golin and Brian Baresch.