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THE PROBLEM OF AN INSURED DELAYING NOTICE TO AN INSURER OF A CLAIM AGAINST THE INSURER: A PROBLEM WITH PRESUMED PREJUDICE

I. INTRODUCTION

The average insurance policy requires that notice be given to an insurer when the insured becomes aware of a claim arising under an insurance policy for which the insurer may be liable.¹ Notice is the means by which the insurer becomes aware that a claim may be presented and that the insured wants the proceeds from the policy.² The insurance policy or a statute may prescribe the time period in which the insured must give notice.³ No controversy arises when timely notice is given by the insured to

1. The standard condition found in the 1966 edition of a liability policy relating to notice provides as follows:

Insured's duties in the event of occurrence, claim or suit.

(A) In the event of an occurrence, written notice containing particulars sufficient to identify the insured and also reasonably obtainable information with respect to the time, place and circumstances thereof, and the names and addresses of the injured and of available witnesses, shall be given by or for the insured to the company or any of its authorized agents as soon as practicable.

2 R. LONG, *THE LAW OF LIABILITY INSURANCE* § 13.01, at 13-14 (1986).

Williston states that "[w]ith almost monotonous regularity, insurance policies of every kind and description stipulated that liability shall arise only when notice is given." 7 S. WILLISTON & W. JAEGER, *WILLISTON ON CONTRACTS* § 918 (3d ed. 1963) [hereinafter *WILLISTON ON CONTRACTS*]. Thus, the notice provision is a pervasive element in insurance policies and insurance coverage.

2. "The notice is not merely to tell the insure[r] that an accident occurred, but rather it is to alert the insurer that a claim against the policy will be forthcoming." 13A G. COUCH, R. ANDERSON & M. RHODES, *COUCH ON INSURANCE 2D* § 49:2, at 227 (rev. ed. 1982). *See also* 7 *WILLISTON ON CONTRACTS*, *supra* note 1, § 918. The controversy over whether the occurrence is to be decided from the viewpoint of the insured or the victim is treated in Rynearson, *Exclusion of Expected or Intended Personal Injury or Property Damage Under the Occurrence Definition of the Standard Comprehensive General Liability Policy*, 19 *FORUM* 513, 521-24 (1984) (generally speaking, the occurrence is to be viewed from the insured's standpoint before deciding if the occurrence was an accident).

3. *See* 2 R. LONG, *supra* note 1, § 13.01, at 13-14 for an example of a time period as stipulated in a policy provision. The following is an example of a statutory provision stipulating a time period for giving notice:

(5) A provision as follows: NOTICE OF CLAIM: Written notice of a claim must be given to the insurer within twenty (20) days after the occurrence or commencement of any loss covered by the policy, or as soon thereafter as is reasonably possible.

IND. CODE ANN. § 27-8-5-3 (West 1980) (Life, Accident and Health Insurance: Accident and

the insurer; but a problem arises when notice is received after the prescribed time period. The question, then, becomes whether to excuse the delayed notice.⁴ If the delay is excused, the insurer must assume liability for the claim. If the delay is not excused, the insurer will not be liable for the claim.⁵ However, some courts have excused the delay where they found that the insurer was not prejudiced by the delay.

In *Miller v. Dilts*,⁶ the Indiana Supreme Court stated that a presumption of prejudice arises against the insured when the insurer receives delayed notice. The presumption can be rebutted only if the insured shows that the delayed notice did not prejudice the insurer.⁷ This rule imposes a great burden on the insured to rebut such a presumption, and frequently results in the loss of his insurance coverage. This loss inequitably denies the insured the protection for which he contracted.

The courts have devised three general rules for evaluating whether to excuse a delayed notice. These three rules approach the problem with varying attitudes towards contract analysis and consumerism.⁸ The first, and oldest, rule applies a strict contractual approach; delayed notice is considered a breach of the insurance contract and the insurer is excused from performance as the non-beaching party.⁹ The second rule creates a rebutta-

Sickness Insurance Policy Provision).

4. Long describes the matter in this fashion:

Unreasonable delay precludes recovery under a liability policy which stipulates for notice as soon as practicable unless there are facts and circumstances which show that notice was given promptly after the disability has been removed. In making this inquiry, consideration must be given to all of the facts and circumstances in the case, especially those which tend to show a reasonable excuse for noncompliance or with delay in complying with the exact requirement for notice.

2 R. LONG, *supra* note 1, § 13.10, at 13-47-48.

Circumstances which have been used to excuse delayed notice are impossibility of giving notice within a fixed time, a reasonable belief that the insured was not covered, incapacity of the insured, ignorance of the insured as to the seriousness or extent of injury or loss. 13A G. COUCH, *supra* note 2, §§ 49:90, 49:91, 49:93, 49:94; 2 R. LONG, *supra* note 1, §§ 13.11-13.13, 13.15. Nevertheless, each excuse must be examined in connection with the specific facts, before deciding if the delay was reasonable. 2 R. LONG, *supra* note 1, § 13.10. Also, the insured will not be excused for being ignorant of the policy provision requiring notice. 13A G. COUCH, *supra* note 2, § 49:92; 44 AM. JUR. 2D *Insurance* § 1342 (1982) (ignorance of policy requirements as to notice and proofs of loss).

5. That is, if the excuse is reasonable, then whether an insured has acted reasonably is left to the trier of fact to decide. 2 R. LONG, *supra* note 1, § 13.01.

6. 463 N.E.2d 257 (Ind. 1984).

7. *Id.* at 265.

8. See generally Annotation, *Modern Status of Rules Requiring Liability Insurer to Show Prejudice to Escape Liability Because of Insured's Failure or Delay in Giving Notice of an Accident or Claim, or in Forwarding Suit Papers*, 32 A.L.R. 4th 141 (1984). See also *infra* notes 9-15 and accompanying text.

9. Annotation, *supra* note 8, at 146. "The following modern cases support a traditional proposition . . . upon reasoning that such conduct constitutes a breach of contract rendering

ble presumption of prejudice against the insurer.¹⁰ The third rule uses prejudice as an element in determining the reasonableness of the delay.¹¹ In general, the courts applying the second and third rules have excused a delay under the following circumstances: when the insured is ignorant of the policy's coverage;¹² when the insured is ignorant to the extent of the damage giving rise to the claim against the insurer;¹³ or when the insured could not reasonably know that the policy covered a particular event.¹⁴ The facts determine the result under the last two rules more than the operation of the rule for these are fact intensive cases.¹⁵

The purpose of this note is to examine the rules used in excusing

the presence or absence of prejudice to the insurer immaterial." *Id.* All that is required under this strict contractual approach is that the trier of fact find that the insured failed to give notice "as soon as practicable" and upon such a finding the insurer is relieved of responsibility under the policy. Comment, *The Materiality of Prejudice to the Insurer as a Result of the Insured's Failure to Give Timely Notice*, 74 *DICK. L. REV.* 260, 261 (1969-70). A majority of courts following this approach, however, allow an exception where the terms of the policy are ambiguous. *Id.* at 262. Also, this approach has had inconsistencies interjected into it by recognizing prejudicial effects of delayed notice to insurers. *Id.* at 263.

10. "[A]lthough prejudice to a liability insurer is not entirely immaterial in determining the consequences of an insured's delay in giving notice of an accident . . . there is nevertheless a presumption of prejudice raised by such delay." Annotation, *supra* note 8, at 152. This approach is meant to mitigate the harshness of the strict contractual approach. Comment, *supra* note 9, at 266. The insured is protected from inequitable forfeitures caused by the insurer labelling notice as a condition precedent. *Id.* at 267. The insured is given further protection by having the issue of prejudice made a jury question. *Id.*

11. The purpose of this rule is to avoid the inflexibility of the strict condition precedent concept. Comment, *supra* note 9, at 268. The insured has the burden to show compliance with the condition precedent of notice, the insurer has to introduce proof of prejudice, and if prejudice is not proven, then the insurer does not escape liability. *Id.* See also Annotation, *supra* note 8, at 156; 2 *R. LONG*, *supra* note 1.

12. See 44 *AM. JUR. 2D Insurance* § 1343 (1982). Insured is excused for his belief that the policy did not cover the accident of injury. However, the insured needs to have made a full investigation before this excuse is available. *Id.*

13. See 44 *AM. JUR. 2D Insurance* § 1345 (1982) (insured excused due to his ignorance of injury's or loss's seriousness or extent; trivial accidents or injuries). Notice is required once the injury's seriousness becomes apparent to the insured. *Id.*

14. See 44 *AM. JUR. 2D Insurance* § 1342 (1982) (insured's belief that accident or injury is not covered by policy). The general rule is that if the insured's ignorance about a notice provision is due to a failure to read the policy, or if read and then forgotten, then the insured is not excused. *Id.* In discussing the conflict between the duty to read and the reality of the insured's reading their policies, see *Graham v. Public Employees Nat. Ins. Co.*, 98 *WASH.2D* 533, 656 P.2d 1077 (1983), see also Comment, *Autopsy of a Plain English Insurance Contract: Can Plain English Survive Proximate Cause? — Graham v. Pemco*, 59 *WASH. L. REV.* 565, 579 n.70 (1984).

15. "The question of prejudice is ordinarily a factual issue which should be resolved by the trier of facts, unless the facts are undisputed and different issues cannot be reasonably drawn from them. Consequently, the ultimate conclusion in each case must depend on its own facts." 2 *R. LONG*, *supra* note 1, § 13.05, at 13-20. In accord with this is Comment, *supra* note 9, and 8 *J. APPLEMAN & J. APPLEMAN, INSURANCE LAW AND PRACTICE* § 4732 (1981).

delayed notice and to propose a rule which will aid in a better evaluation of whether a delayed notice should be excused. The starting point for the proposed rule is an analysis of Indiana's rule for excusing delayed notice and the application of that rule by the Indiana courts in these fact sensitive cases. The first section proposes that the current Indiana rule is unnecessarily burdensome and inequitably denies benefits conferred by an insurance policy. The following sections proceed to examine the three rules currently used in analyzing delayed notice;¹⁶ the second section will identify the concept of prejudice and its proper use,¹⁷ the third section will discuss the concept of notice,¹⁸ and the fourth section will present the contractual relationship of insured and insurer.¹⁹ The thesis underlying this examination is that a proper rule requires a clear understanding of each area, and that a proper rule requires that each area can be analyzed in an easily adaptable manner. The final section determines that the best standard for analyzing delayed notice is the reasonableness of the delay rule.²⁰ There are two reasons for this conclusion: this rule adequately and equitably analyzes the insured's reasonableness in delaying notice, and, unlike the test in *Miller v. Dilts*, properly measures the damage to the insurer's interests.²¹

II. THE INDIANA RULE

In *Miller v. Dilts*, the Indiana Supreme Court created the rule that an insured's delayed notice gives rise to a presumption of prejudice against the insurer. The insured can easily rebut any defense by the insurer by showing that the insurer was not prejudiced.²² *Miller* consolidated three cases from the court of appeals with issues involving cooperation clauses and notice provisions.²³ The Indiana Supreme Court differentiated between coopera-

16. See *infra* notes 62-87 and accompanying text.

17. See *infra* notes 88-104 and accompanying text.

18. See *infra* notes 105-19 and accompanying text.

19. See *infra* notes 120-38 and accompanying text.

20. See *supra* note 9 and the discussion there on the reasonableness of the delay rule.

21. *Miller v. Dilts*, 463 N.E.2d 257 (Ind. 1984). See also *infra* notes 22-58 and accompanying text.

22. *Miller*, 463 N.E.2d 257. One issue present in *Miller* was whether there was "no presumption of prejudice to an insurance company when an insured fails to give reasonable and timely notice, thus, imposing a burden on the insurance company to show actual prejudice created by late notice as well as actual prejudice caused by failure to cooperate in order to avoid liability under the policy." *Id.* at 261. This is the issue with which this note is principally concerned. The other issue was whether the notice provision and the cooperation clause both served the same purpose and had the same effect. For further discussion on this second issue, see *infra* note 24.

23. *Miller*, 463 N.E.2d at 260. The cases consolidated for the *Miller* decision were: *Miller v. Dilts*, 453 N.E.2d 299 (Ind. Ct. App. 1983); *Kasonovich v. Meade*, 449 N.E.2d 1178 (Ind. Ct. App. 1983); *Indiana Ins. Co. v. Williams*, 448 N.E.2d 1233 (Ind. Ct. App. 1983). All three cases involved automobile accidents. *Miller*, 463 N.E.2d at 259-60. *Indiana Ins. Co.*

tion clauses and notice provisions based upon their respective objectives. Accordingly, the Supreme Court held that different rules apply.²⁴

The notice provision's objective is to inform the insurer of an adverse claim. Timely notice allows the insurer to adequately investigate and prepare for a defense against the claim.²⁵ Without notice, the insurer would not have the time to investigate the claim or the information needed to defend against the claim, activities essential to the duties the insurer assumed under the insurance policy.²⁶ In short, the notice provision is essen-

involved an insured who gave notice six months after the accident and one month after entering into a plea agreement in which the insured assumed responsibility for all damages. *Id.* at 259. *Kosanovich* involved an accident victim who attempted to garnish an insured's insurance proceeds and an insurer who had not received prompt notice of the accident. *Id.* The accident occurred on September 7, 1979; the insurer learned of the accident over a month later, and learned of the lawsuit on January 12, 1981, after a default judgment had been taken. *Id.* at 266. *Miller* involved a February 2, 1979, accident after which notice was not given until September 5, 1979, when a suit was filed. *Id.* at 260.

24. *Id.* at 265. The court of appeals held that cooperation clauses and notice provisions are alike in that they require the insured to assist the insurer in preparing for trial or settlement. *Indiana Ins. Co.*, 448 N.E.2d at 1237; *Kosanovich*, 449 N.E.2d at 1180 n.3 (citing *Indiana Ins. Co.*). (*Miller* was concerned solely with the notice provision. 453 N.E.2d at 300). The Indiana Supreme Court held that Indiana precedent supported the court of appeals on the issue of the requirement that the insurer show actual prejudice from an insured's noncompliance with a cooperation clause. *Miller*, 463 N.E.2d at 261-63. Nevertheless, the issue about whether prejudice was required whenever there was noncompliance with a notice provision had never been discussed by the Indiana courts. *Id.* at 262. The Indiana Supreme Court held that "[f]ailure to cooperate can come about in many ways, some of which may be technical and inconsequential, thereby resulting in no prejudice to the insurance company." *Id.* at 265. Notice was, however, a threshold requirement by which the insurer learned that there was a claim pending under the insurance policy. *Id.* The basic difference seems to be in timing; notice is a condition precedent to the cooperation clause. *Id.* at 264.

25. *Miller* states that "[t]he requirement of prompt notice gives the insurer an opportunity to make a timely and adequate investigation of all the circumstances surrounding the accident or loss." *Miller*, 463 N.E.2d at 265. This is supported by the leading insurance treatise writers, who also agree that an adequate investigation is important for several reasons: to prevent fraud and imposition upon the insurer; to allow the insurer to investigate while witnesses are easily available and memories are fresh; and for estimating rights and liabilities in order to settle or to defend adequately. 8 J. APPLEMAN & J. APPLEMAN, *supra* note 15, § 4731; 2 R. LONG, *supra* note 1, § 13.02; 13A G. COUCH, *supra* note 2, § 49:2. This last reason has, however, been disputed by some jurisdictions, and in those jurisdictions investigation is the only reason for prompt notice. *See* 8 J. APPLEMAN & J. APPLEMAN, *supra* note 15, § 4731 n.5, at 6 (Appleman and Appleman list Connecticut, Vermont and West Virginia as jurisdictions disputing this reason for prompt notice). *See also infra* note 89 (interrelationship of notice and prejudice).

26. *Miller* states that: "The notice requirement is 'material, and of the essence of the contract.' *London Guarantee, supra*, 35 Ind. App. at 345, 66 N.E. at 482." *Miller*, 463 N.E.2d at 265. *London Guarantee and Accident Co. v. Siwy*, 35 Ind. App. 340, 66 N.E. 481 (1903), involved an employer's liability insurance policy that contained a requirement for immediate notification of an employee's claim for an injury). Three months lapsed between the claim for an injury and notice to the insurer. *London Guarantee*, 35 Ind. App. at 346, 66 N.E. at 483. Also, the *Miller* decision gives the full quotation from which the above quotation was

tial to the contract.²⁷ Accordingly, the Supreme Court decided that notice was a condition precedent to the insurer's liability for the claim, and that the insured had the burden of showing that the insurer was not prejudiced by the insured's delayed notice.²⁸ When the insured fails to make such a showing, the presumption of the insurer's prejudice becomes conclusive and relieves the insurer of its responsibilities under the insurance policy.²⁹

The *Miller* decision contains a good analysis of Indiana case law on delayed notice, but two Seventh Circuit decisions cited in *Miller* need particular attention: *Hartford Accident and Indem. Co. v. Lochmandy Buick Sales, Inc.*³⁰ and *Ohio Casualty Ins. Co. v. Rynearson.*³¹ These two decisions require particular attention because they were essential to the Indiana Supreme Court's decision in *Miller.*³² *Lochmandy* stated that the general

excerpted at *Miller*, 463 N.E.2d at 263. The Indiana Supreme Court, however, did not emphasize the sentence following that from which the above quotation was excerpted. "A failure to give such notice immediately involves an absolute forfeiture, which cannot be relieved against in equity." *London Guarantee*, 35 Ind. App. at 345, 66 N.E. at 482. The obvious conclusion seems to be that the Indiana courts have retreated from the harshness of strict forfeiture, as have other courts. See Comment, *supra* note 9, at 268.

27. *Miller*, 463 N.E.2d at 265.

28. *Id.* That a contract is a conscious decision between the parties is bound in the phrase "freedom of contract." This freedom to contract reached its highest point in the nineteenth century, and in the twentieth century legislative restrictions were imposed on employment and insurance contracts. J. CALAMARI & J. PERILLO, *THE LAW OF CONTRACTS*, 5-6 (1987). There has also been common law restriction where the bargaining process has been limited, i.e. in contract by adhesion. *Id.* at 6. Calamari and Perillo outlined several philosophical foundations for contract law: a) the sovereignty of the human will; b) the sanctity of promise; c) private autonomy; d) reliance; and e) needs of trade. *Id.* at 7-11. For all their differences, each theory holds that the decision to contract is a conscious decision.

29. *Miller*, 463 N.E.2d at 265-66; *Milwaukee Guardian Ins., Inc. v. Reichhart*, 479 N.E.2d 1340, 1343 (Ind. Ct. App. 1985).

30. 302 F.2d 565 (7th Cir. 1962). *Lochmandy* is particularly important because it introduced a presumption of prejudice for unreasonably delayed notice.

31. 507 F.2d 573 (7th Cir. 1974).

32. The importance given to *Lochmandy* and *Rynearson* is made explicit in *Miller*: We give respectful consideration to them [federal court interpretations of Indiana law], however, as we do to decisions in other jurisdictions to aid us in coming to the ultimate conclusion of what the law is in Indiana on particular issue. In so doing, we find the opinions of the Seventh Circuit Court of Appeals in *Lochmandy* and *Rynearson* to be sound and well grounded in Indiana law.

Miller, 463 N.E.2d at 263.

The importance of *Lochmandy* and *Rynearson* was first pointed out in Judge Hoffman's dissent to *Indiana Ins. Co. v. Williams*, 448 N.E.2d 1233, 1239 (Ind. Ct. App. 1983) (Hoffman, J., dissenting). Judge Hoffman's dissent was favorably cited in *Miller*:

We agree with Judge Hoffman in his dissent to *Indiana Insurance* in which he found that notice given ten days after the suit was filed and almost seven months after the accident occurred "hardly constitut[ed] timely notice." Judge Hoffman further pointed out that late notice given to an insurer places it in a position that could have been avoided through timely notice, and that the "most cooperative insured cannot erase this prejudice suffered by the insurer" in situations where the scene of the accident changes, or witnesses move

rule for excusing delayed notice is a determination of whether the insured was acting as a reasonably prudent person.³³ *Rynearson* restated the rule and found that Indiana law created a rebuttable presumption of prejudice to the insurer.

In *Rynearson*, the insured was an insurance claims adjuster prior to the claim and a practicing attorney when the claim arose. Accordingly, *Rynearson* was held to a higher standard than the average insured and his excuse was disallowed.³⁴ The Seventh Circuit found that the Indiana precedent basically reinforced the contract law foundation for using the presumption that notice was a condition precedent to the insurer's performance under the insurance policy.³⁵ The presumption used in *Miller* is directly traceable to the *Rynearson* decision.³⁶

The first application of the *Miller* standard was *Milwaukee Guardian Ins., Inc. v. Reichhart*.³⁷ In *Reichhart*, the insured had changed a watercourse on his property so that the water flowed onto a neighbor's property. The neighbor then sued the insured, and the insured defended against this suit.³⁸ The defendant was successful at trial.³⁹ When the claim arose, the insured did not believe that his policy covered the claim and did not send notice to the insurer until a neighbor informed him that insurance should

away or have their memories lapse, due to the passage of time. 448 N.E.2d at 1238. *Miller*, 463 N.E.2d at 265. The Indiana Supreme Court also cited Judge Hoffman in support of its characterizing notice as a condition precedent: "as Judge Hoffman stated, '[n]otice is a threshold requirement.'" *Id.* Judge Hoffman seems to have been influential in finding a purpose for the notice provision and in ascertaining its nature as a condition precedent to the insurer's obligations. It should also be noted that Judge Hoffman wrote the opinion in *Milwaukee Guardian Ins., Inc. v. Reichhart*, 479 N.E.2d 1340 (1985).

33. "The general rule is that an insured will be excused, where, acting as a reasonably prudent person, he believed he was not liable for the accident." *Lochmandy*, 302 F.2d at 566. This rule is repeated in *Rynearson*, and the Seventh Circuit held that different factual situations created different fact patterns. *Rynearson*, 507 F.2d at 579. See *infra* note 86 for further discussion on how this rule was applied in *Rynearson*.

In *Lochmandy*, the insured was a Buick dealership whose president did not give notice that a claim had arisen against the dealership. *Lochmandy*, 302 F.2d at 566. The president delayed notice of the dealership's liability due to his belief that there was no liability against the dealership. *Id.* The court of appeals held that the insured had acted unreasonably in deciding not to fully investigate his liability. *Id.* at 578.

34. *Rynearson*, 507 F.2d at 579.

35. The leading Indiana case holding notice as a condition precedent was *London Guarantee and Accident Co. v. Siwy*, 35 Ind. App. 340, 66 N.E. 481 (1903). Other similar Indiana cases were: *Lomont v. State Farm Mut. Auto. Ins. Co.*, 128 Ind. App. 645, 151 N.E.2d 701 (1958); *Shedd v. Am. Credit Indem. Co.*, 48 Ind. App. 23, 95 N.E. 316 (1911) (credit insurance); *Baker v. German Fire Ins. Co.*, 124 Ind. 490, 24 N.E. 1041 (1890) (fire insurance). See *supra* note 26 for the discussion of how the *Miller* court treated *London Guarantee*.

36. *Rynearson*, 507 F.2d at 579.

37. 479 N.E.2d 1340 (Ind. Ct. App. 1985).

38. *Id.* at 1341.

39. *Id.*

cover the claim.⁴⁰ When the insured discovered that coverage was available, he sent notice to his insurer, eleven months after the trial was completed.⁴¹ The insurer denied liability and refused to reimburse Reichhart's legal fees; Reichhart then sued.⁴² Since Reichhart had prevailed on the underlying claim, the trial court held that the insurer was not prejudiced, and therefore the insured had rebutted the *Miller* presumption.⁴³

The Indiana Court of Appeals reversed the trial court, and held that the insurer *had* been prejudiced as a matter of law.⁴⁴ The court of appeals reasoned that the insured's successful defense against the claim was not enough to show that no actual prejudice had resulted to the insurer. The court noted that the notice was delayed eleven months, that the insured had been in frequent contact with his insurance agent, and that the insured had years of experience in dealing with insurance, thus hinting that the delay was unreasonable.⁴⁵ The court of appeals characterized the prejudice to the insurer as the inability to choose its own defense counsel, the inability to guide the course of litigation, and the inability to take part in settlement negotiations.⁴⁶ In effect, the *Reichhart* decision increased the burden of proving that the delay did not actually prejudice the insurer. This decision

40. *Id.* There was some question as to whether notice was given to Reichhart's insurance agent. *Id.* at 1341 n.1. The court of appeals considered that the insured had an opportunity to consult with his insurance agent and to either discover that notice was due, or to give notice. *Id.* However, the communication that did exist between the insured and the insurance agent did not prevent a delay of the notice to the insurer as required by the insurance policy. *Id.*

The insurance agent was also discussed in the briefs filed in the Indiana Supreme Court. The issue was whether the agent knew the policy's coverage. Reichhart testified that the agent said that Reichhart "would be covered — *should* be covered under the home owner's policy." Brief for Defendant-Appellant in Opposition to Petition to Transfer at 9, *Reichhart*, 479 N.E.2d 1340 (No. 3-1284A349) (emphasis added). Some doubt could exist about how effective any amount of communication would have been with an agent who equivocates in this fashion.

41. *Reichhart*, 479 N.E.2d at 1341.

42. *Id.*

43. *Id.*

44. *Id.* at 1343.

45. *Id.*

46. *Id.* The court of appeals summarized as follows:

An insurance company cannot be forced to pay fees and expense incurred wholly without its knowledge or consent pursuant to an insurance contract when the insured has made no effort to fulfill his duties under that contract. . . . The trial court erred in finding that Milwaukee had not been prejudiced by Reichhart's delay.

Id. The decision could better be explained as a quasi-contract decision. This was the theory with which the insured sought to recover his attorney's fees from the insurer. *Id.* Indiana precedent was held to oppose an award based upon quasi-contract or quantum meruit; the party seeking to recover on such a basis must show a benefit rendered at the other's express or implied request. *Id.* (citing *Kody Eng'g Co. v. Fox Ins. Agency*, 153 Ind. App. 498, 303 N.E.2d 307 (1973)). However, the holding explicitly states that the prejudice suffered by the insurer precludes the insured's claim, and prejudice is the keystone of this decision. *Reichhart*, 479 N.E.2d at 1342.

is inequitable and is hard to reconcile with decisions from similar jurisdictions involving similar facts.

In *Hartford Accident and Indemnity Co. v. Phelps*,⁴⁷ for example, the Florida Court of Appeals applied the same rule used by the Indiana Supreme Court to find that delayed notice did not prejudice the insurer.⁴⁸ In *Phelps*, the insureds' delayed notice of damage done to their bursting pipe resulted in the insurer denying liability on two theories: that an exclusionary provision covered the occurrence, and that the insureds failed to give timely notice.⁴⁹ The insureds claimed that they were unaware of the policy coverage and hence gave an untimely notice of the injury.⁵⁰ The Florida Court of Appeals found two elements persuasive in its conclusion that the insureds had rebutted the presumption of prejudice: notice was given as soon as possible, and the insurer would probably have denied liability even if notice was timely.⁵¹

Reichhart is also difficult to reconcile with an Illinois Appellate Court decision, *Farmer's Automobile Insurance Association v. Hamilton*,⁵² where no prejudice was found in a one-year delay of notice to the insurer.⁵³ The insured shot a man at the insured's home and criminal proceedings against the insured followed.⁵⁴ One year after the shooting, the victim began a civil suit against the insured, and the insured gave notice to his insurer upon receiving notice of the civil suit.⁵⁵ The insurer argued that notice was due at the time of the criminal proceedings. The Illinois Appellate Court, in excusing the delay provision, held that the delay came within the reasonably prudent person exception in which the insured acted as a reasonably prudent person in not believing that notice was due.⁵⁶ Facts pertinent to the appellate court's decision were the insured's ignorance of a duty to notify his insurer of the occurrence, the insured's ignorance of the fact that the policy covered the occurrence, and the fact that notice was quickly given when a civil suit was initiated against the insured.⁵⁷

A more difficult reconciliation with the *Reichhart* decision is the *Mil-*

47. 294 So. 2d 362 (Fla. Dist. Ct. App. 1974) (involved a bursting water pipe and an "all-risks" homeowners policy).

48. *Id.* at 365.

49. *Id.* at 363. The Florida Court of Appeals does not mention how long notice was delayed.

50. *Id.* at 365.

51. *Id.*

52. 31 Ill. App. 3d 730, 335 N.E.2d 178 (1975).

53. *Id.* at 731, 335 N.E.2d at 179.

54. *Id.* at 733, 335 N.E.2d at 181.

55. *Id.* at 731, 335 N.E.2d at 179.

56. *Id.* at 732-33, 335 N.E.2d at 180.

57. *Id.* at 733-34, 335 N.E.2d at 180-81.

waukee Mutual Insurance Co. v. Butler decision.⁵⁸ In *Butler*, the District Court for the Southern District of Indiana held that the *Miller* rule is met when the insured shows that the insurer could not have taken any more action than was taken, even if the notice had been timely.⁵⁹ The district court found that the insurance policy was vague as to the time limits for giving notice to the insurer.⁶⁰ More important were the facts that the insurer conducted no investigation until a year after the notice had been received and that the police had conducted their own investigation. These two facts show that the late notice had not injured the insurer any more than timely notice would have benefitted the insurer.⁶¹ These three decisions, and particularly *Butler*, are hard to reconcile with *Reichhart* and bring into question the correctness of the *Reichhart* decision and the presumption of prejudice.

As was shown above, the *Reichhart* decision is a result outside the range of similar decisions applying the same rule. The real problem with *Reichhart* is the rule itself and how the rule was applied. The problem is caused by the underlying rationale for the rule, the concept of prejudice used by the courts in analyzing the notice provision, and the effect of delay on the insurer's obligation under the insurance policy. An examination of how the analysis of other courts approach the delayed notice issue will reveal the pitfalls of using a presumption of prejudice rule.

III. THE THREE RULES FOR EVALUATING WHETHER TO EXCUSE A DELAYED NOTICE

The decisions regarding delayed notice illustrate three rules.⁶² These rules are: 1) that notice is a contract provision which is breached by delay

58. 615 F. Supp. 491 (S.D. Ind. 1985). This case also involved delayed notice under an automobile insurance policy.

59. *Id.* at 494. The accident occurred on October 28, 1979, and the insurer was given notice on June 24, 1980, with additional telephonic notice given on July 1, 1980. *Id.* at 492-93. There is a similarity between *Phelps* and *Butler* in that both find that action by the insurer would not have been different even if notice had been timely. *Hartford Accident and Indem. Co. v. Phelps*, 294 So. 2d 362, 365 (Fla. Dist. Ct. App. 1974); *Butler*, 615 F. Supp. at 494.

60. *Butler*, 615 F. Supp. at 494. The ambiguity found in *Butler* between page three of the policy (a hit and run accident needed reporting to the police within 24 hours and a sworn statement to the insurer within thirty days) and page four of the policy (twenty days for giving notice to the insurer unless not reasonably possible) is found in *Miller v. Dilts*, 463 N.E.2d 257 (Ind. 1984). *Miller* states quite specifically that the policies in question had no ambiguity. *Id.* at 265.

61. 615 F. Supp. at 494. The insurance policy required that the insured notify the police of a hit-and-run accident. The Indianapolis Police Department and the Marion County Sheriff's Department conducted a "thorough investigation" but did not find the driver. On the other hand, Milwaukee Mutuals' claims manager opened a file upon receiving notice, but did not begin to investigate the claim until one year after receiving notice. *Id.*

62. See Annotation, *supra* note 8, at 146-52.

and the non-breaching party is excused from performance;⁶³ 2) that notice is a condition precedent to performance by the insurer in which a delay in notice creates a presumption against the insured that the insurer was prejudiced by such delay;⁶⁴ and 3) that the delay is not excused if the insured acted unreasonably and prejudice is an element in determining the reasonableness of the insured's actions.⁶⁵

The underlying rationale for applying a particular rule⁶⁶ depends on the contract theory used in interpreting insurance policies.⁶⁷ Those jurisdictions adhering to the strict contract rule consider an insurance contract to be a bilateral contract.⁶⁸ Hence, the insured, as the breaching party due to his delayed notice, cannot demand performance from the non-breaching party, the insurer.⁶⁹

The strict contract approach is modified by those jurisdictions that use the presumption of prejudice and reasonableness-of-the-delay rules. Those adhering to the presumption of prejudice rule have retained the concept of

63. *Miller v. Dilts*, 463 N.E.2d 257, 258 (Ind. 1984). "A strict contractual interpretation of the provision to give notice 'as soon as practicable' results in construction of the notice clause as a condition precedent to the insurer's liability under the policy." Comment, *supra* note 9, at 261. The insurer will not be relieved of liability if the trier of fact finds that the insured has not complied with the notice provision. *Id.* Prejudice is immaterial.

64. See *supra* note 7 and accompanying text for an example. The Indiana Supreme Court adopted this rule in *Miller*, 63 N.E.2d 257. See also *supra* note 10.

65. See Comment, *supra* note 9, at 268. See also *State Farm Mut. Auto. Ins. Co. v. Burgess*, 474 So. 2d 634 (Ala. 1985) (reasonableness of the delay measured by the reasons for the delay, the length thereof, and if insurer was prejudiced); *Cooper v. Gov't Employees Ins. Co.*, 51 N.J. 86, 237 A.2d 870 (1968) (similar to *Burgess*, but adds good faith requirement for insured); and *Great Am. Ins. Co. v. C.G. Tate Constr. Co.*, 303 N.C. 387, 279 S.E.2d 769 (1981) (adopting *Cooper* test).

Prejudice is a question of fact which must be left to the trier of fact. See *Wendell v. Swanberg*, 384 Mich. 468, 185 N.W.2d 348 (1971); Comment, *supra* note 9, at 267.

66. This note takes a normative approach to examining this aspect of insurance. That is, this note does not try to explain why a certain rationale is chosen. While a study into why a certain rationale is chosen could be undertaken, any such examination is outside the scope of this note and is of little practicality in regards to the problem of prejudice and timely notice.

67. See Comment, *supra* note 9, at 261-62; Annotation, *supra* note 8, at 146.

68. See *supra* note 66.

69. *Id.* The Indiana Supreme Court also reviewed cases in *Miller v. Dilts*, 463 N.E.2d 257 (Ind. 1984), which supported each theory: *Waters v. Am. Automotive Ins. Co.*, 363 F.2d 684 (D.C. Cir. 1966) (eight month delay in giving notice breached condition precedent language of policy and insurer did not need to establish prejudice); *Richmond v. Georgia Farm Bureau Mut. Ins. Co.*, 140 Ga. App. 215, 231 S.E.2d 245 (1976) (notice is a condition precedent and insurer need not show prejudice); *Diese v. Hartford Accident and Indem. Co.*, 205 So. 2d 328 (Fla. Dist. Ct. App. 1967) (insurer need not show prejudice but party seeking to impose liability must show a lack of prejudice); and *Allstate Ins. Co. v. Campbell*, 95 N.J. Super. 142, 230 A.2d 179 (1967) (the lack of prejudice considered in determining reasonableness of time). *Miller*, 463 N.E.2d at 264-65.

notice as a condition precedent to the insurer's performance.⁷⁰ The courts adhering to the third rule have modified the contractual approach further by recognizing the adhesive nature of insurance policies and the social policy served by insurance.⁷¹ However, none of the jurisdictions that employ the presumption of prejudice and reasonableness-of-the-delay rules have abandoned the concept of insurance as a contract. Rather, these jurisdictions recognize that there is a relationship between the parties in which the insurer has more power to protect its interests.⁷²

One commentator has noted that a judicial preference exists for the insurer.⁷³ The *Reichhart* decision shows that this preference is useless without guidelines on how the insured is to prove no prejudice. Notice is essential to the insurance contract because without notice the insurer cannot know that the time has come to perform his duties.⁷⁴ Yet, the rebuttable presumption creates a difficult evidentiary problem for the insured. The insured usually has neither the access to proof on how the insurer was prejudiced, nor the ability to disprove prejudice.⁷⁵ This evidentiary problem

70. *Miller*, 463 N.E.2d at 265, is an example of this second rule.

71. The New Jersey Supreme Court has stated the matter thusly: "[t]he insurance contract not being a truly consensual arrangement and being available only on a take-it-or-leave-it basis. [sic] and the subject being in essence a matter of forfeiture."

Cooper v. Gov't Employees Ins. Co., 51 N.J. 86, 94, 237 A.2d 870, 874 (1968). The New Jersey Supreme Court described the purpose of insurance as "an instrument of a social policy that the victims of negligence be compensated." *Id.* See also Young, Lewis & Lee, *Insurance Contract Interpretation: Issues and Trends*, 625 INS. L.J. 71, 77 (1975) (the effect of using adhesion contract theories to interpret insurance policies). Young, Lewis, and Lee contend that if contract law is not the basis of insurance disputes, as is the case where adhesion contracts are judged according to social policies, then guidelines "other than the courts unfettered notion of what is just in a given situation" are needed. *Id.* The authors suggest a doctrine similar to the Uniform Commercial Code's "unconscionability" doctrine. *Id.* at 77-78.

72. 7 WILLISTON ON CONTRACTS, *supra* note 1, § 900.

73. Williston gives a detailed accounting of judicial preference for insureds: The fundamental reason which explains this and other examples of judicial predisposition toward the insured is the deep-seated, often unconscious but justified feeling or belief that the powerful underwriter, having drafted its several types of insurance 'contracts of adhesion' with the aid of skillful and highly paid legal talent, from which no deviation desired by an applicant will be permitted, is almost certain to overreach the other party to the contract. The established underwriter is magnificently qualified to understand and protect its own selfish interests.

74. 7 WILLISTON ON CONTRACTS, *supra* note 1, § 900, at 19. The judicial preference for insureds is borne out in the number and variety of categories used in Annotation, *supra* note 8, for the delayed notice issue: the view that the insurer need not show prejudice (broad view: lack of mutuality; qualified view: rebuttable presumption of prejudice); the view that prejudice is a factor in determining the unreasonableness of the delay itself; and the view that the insurer must show prejudice (generally, with exceptions and statutory requirement). *Id.* at 146-49.

75. See *infra* note 107.

76. See *infra* note 149, concerning access to proof as a factor when creating an evidentiary presumption. As to the difficulty of disproving prejudice:

Matters of fact, which are the second objects of human reason, are not ascertained in the

can unintentionally frustrate the insured's reasonable expectations of insurance coverage.⁷⁶ Hence, such problems in evidence impose a great burden on the insured and permits a preferential edge to the insurer.

Both the insurer's and the insured's interests are better protected by the reasonableness-of-the-delay rule. This rule concerns itself with the reasonableness of the delay.⁷⁷ An argument can be made that reasonableness is also at the root of the presumption of prejudice rule,⁷⁸ for prejudice is less likely to occur when the insured has acted reasonably.⁷⁹ Nevertheless, the insured's ability to rebut the presumption of prejudice has overshadowed any reasonableness aspect originally included in the rule.

One recurring factor in delayed notice cases is that vague insurance policy provisions often cause the delay.⁸⁰ Thus, the courts favoring the reasonableness-of-the-delay rule combine a dislike of forfeiture of insurance

same manner; nor is our evidence of their truth, however great, of a like nature with the foregoing. The contrary of every matter of fact is still possible; because it can never imply a contradiction, and is conceived by the mind with the same facility and distinctness as if ever so conformable to reality. . . . Were it demonstratively false, it would imply a contradiction and be never distinctly conceived by the mind.

D. HUME, *Inquiry Concerning Human Understanding*, in *THE EMPIRICISTS* 307, 223-33 (1961).

76. The reasonable expectation of the insured as used here is derived from Young, Lewis & Lee, *supra* note 71, at 78. These authors describe a species of reasonable expectations as being an entitlement to all the coverage under an insurance policy which the insured can reasonably expect, and in which coverage is not specifically foreclosed by a policy provision.

77. The reasonableness-of-the-delay rule does have one fault: an insured may have acted reasonably, and still the insurer is not liable due to prejudice from the delay. *See Cooper v. Gov't Employees Ins. Co.*, 51 N.J. 86, 93, 237 A.2d 870, 873 (1968).

78. The general rule that a delay is excused where the insured acted as a reasonably prudent person was stated in *Hartford Accident and Indem. Co. v. Lochmandy Buick Sales*, 302 F.2d 565 (7th Cir. 1962) and reiterated in *Ohio Casualty Ins. Co. v. Rynearson*, 507 F.2d 573 (7th Cir. 1974), and *Miller v. Dilts*, 463 N.E.2d 257 (Ind. 1984). *See also supra* note 33. In fact, the presumption of prejudice arises when the notice is unreasonably late. *Miller*, 463 N.E.2d at 263. Therefore, reasonableness forms the basis of the presumption of prejudice rule.

79. *But see Cooper*, 51 N.J. at 94, 237 A.2d at 874.

80. Vague insurance policies are a common factor in *Milwaukee Guardian Ins., Inc. v. Reichhart*, 479 N.E.2d 1340 (Ind. Ct. App. 1985), *Hartford Accident and Indem. Co. v. Phelps*, 294 So. 2d 362 (Fla. Dist. Ct. App. 1974), *Farmers Auto. Ins. Ass'n v. Hamilton*, 31 Ill. App. 3d 730, 335 N.E.2d 178 (1975), and *Milwaukee Mut. Ins. Co. v. Butler*, 615 F. Supp. 491 (S.D. Ind. 1985). In *Reichhart*, there was a doubt about coverage. 479 N.E.2d at 1342. This doubt seems to have been shared by Reichhart's insurance agent. *See supra* note 40. Likewise, the insureds in *Phelps*, 294 So. 2d at 365, and *Hamilton*, 335 N.E.2d at 181, were not aware that policy coverage existed in the specific instances at issue in their cases.

American Jurisprudence 2d states the general rule for this type of case as follows: "[a]n insured may be excused for a delay or failure to give the required notice were it appeared that he believed, acting as a reasonably prudent person, that the accident or injury was not covered by the liability policy." 44 AM. JUR. 2D *Insurance* § 1343, at 272 (1982).

Only *Butler* involved an ambiguity between notice provisions. 615 F. Supp. at 494. In this situation, the ambiguity is to be resolved against the insurer. *Miller*, 463 N.E.2d at 265.

policies and an adhesion contract approach.⁸¹ The insurer writes the policy provisions, and is released from liability if the insured cannot rebut the presumption of prejudice rule. As a result, the insured loses the protection from liability paid in premiums.⁸² Under the reasonableness-of-the-delay rule the insured loses his premiums only when the following conditions have been met: when the insured has acted unreasonably, the delay injures the insurer's interests, and no fault can be attributed to the insurer.⁸³

The reasonableness-of-the-delay rule is a better analysis of the relationship between the insured and the insurer and a proper balancing of the parties' interests. This relationship is that of an adhesion contract,⁸⁴ with the insurer as the superior party in the relationship.⁸⁵ By making reasonableness the essential feature of this rule,⁸⁶ the courts have shifted the balance of power within the relationship of insurer and insured. However, this rule does not strip the insurer of all protection because prejudice is kept as an element in determining the overall reasonableness of the delay.⁸⁷

81. See generally *supra* note 71.

82. Young, Lewis & Lee, *supra* note 71, at 74-75 (discusses the theory of adhesion contracts, the commercial uses of adhesion contracts, and their particular application to insurance policies).

83. See *Great Am. Ins. Co. v. C.G. Tate Constr. Co.* 303 N.C. 387, 396, 279 S.E.2d 769, 774 (1981).

84. See *infra* notes 120-38.

85. Young, Lewis & Lee, *supra* note 71, at 74-75; 7 WILLISTON ON CONTRACTS, *supra* note 1, § 900.

86. To return to the Indiana cases: there does not seem to be any derivation between the knowledge of the insured in *Ohio Casualty Ins. Co. v. Ryneerson*, 507 F.2d 573 (7th Cir. 1974), and *Milwaukee Guardian Ins., Inc. v. Reichhart*, 479 F.2d 1340 (Ind. Ct. App. 1985), on the subject of insurance. However, the insured in *Ryneerson* had been an insurance claims adjuster prior to the time that the claim arose and was a practicing attorney when the claim arose; because of this the court of appeals said he "possessed knowledge of insurance contracts far superior to that of the average insured." *Ryneerson*, 507 F.2d at 578. This description needs to be contrasted with the Indiana Court of Appeals' description of the insured in *Reichhart*:

Reichhart was knowledgeable in matters of insurance and had carried Milwaukee Guardian Insurance, both personal and business, through the Wegmann agency for twenty years. He and his family had submitted various claims for insurance prior to the Kenneek suit. Reichhart testified that Wegmann was an accessible insurance agent and Reichhart was normally in contact with Wegmann every two or three months.

Reichhart, 479 N.E.2d at 1342.

There is a difference here. Reichhart is certainly what Ryneerson was not: an average insured. Since the insured's knowledge is part of the reasonableness standard of *Ryneerson*, the insured's knowledge must be ascertained clearly. *Ryneerson*, 507 F.2d at 579. The *Reichhart* decision does not seem to have ascertained what specific knowledge the insured had about insurance, and hence, the reasonableness of the insured's actions.

87. See *infra* notes 88-104 for a discussion of the concept of prejudice. See also *Great Am. Ins. Co. v. C.G. Tate Constr. Co.*, 303 N.C. 387, 279 S.E.2d 769 (1981) for an example of a court adopting the third rule and how that court views prejudice.

IV. THE CONCEPT OF PREJUDICE

Prejudice is an elusive element and a difficult concept to prove.⁸⁸ The courts have not defined prejudice, but have functionally used it in relation to the purpose of notice.⁸⁹ Thus, prejudice occurs when the insurer cannot protect its interests under an insurance policy.⁹⁰ These interests would be harmed when the insurer is unable to investigate a claim adequately in preparation for trial or settlement,⁹¹ when the insurer would be unable to detect fraudulent claims,⁹² or when the insurer would be unable to litigate a claim as effectively as it would have been able to if notice was timely.⁹³ However, one court defined and limited prejudice to those situations where the delay causes the insurer to assume liabilities which the insurer did not assume under the insurance policy.⁹⁴

Defining prejudice in this way is reasonable when the basis of the in-

88. See 8 J. APPLEMAN & J. APPLEMAN, *supra* note 15, § 4732, at 26.

89. The North Carolina Supreme Court was succinct in its description of the interrelationship of notice and prejudice:

The clear purpose of the notice provision is to protect the ability of the insurer to prepare a viable defense by preserving its ability fully to investigate the accident. It follows, then, that if the delay in giving notice has not materially prejudiced the ability of the insurer to defend the claim, its obligations under the insurance contract should not be excused.

Great Am. Ins. Co. v. C.G. Tate Constr. Co., 303 N.C. 387, 397, 279 S.E.2d 769, 775 (1981). The Indiana Supreme Court made a similar, but narrower statement in *Miller v. Diltz*, 463 N.E.2d 257 (Ind. 1984), when it described the effects of delayed notice. 463 N.E.2d 257 (Ind. 1984). See also *supra* note 25.

The *Miller* decision relates notice to investigation of a claim. *Miller*, 463 N.E.2d at 265. This is to be contrasted with the *Reichhart* decision where the interests prejudiced by delayed notice may be best described as a litigation interest: the insurer did not select the insured, negotiate attorney's fees, guide the litigation, or participate in settlement negotiations. *Reichhart*, 479 N.E.2d at 1343. Instead, the *Reichhart* decision's use of the litigation context instead of the investigation interest as the area being prejudiced seems more akin to the rationale used in *Indiana Ins. Co. v. Williams*, 448 N.E.2d 1233, 1237 (Ind. Ct. App. 1983), and *Kosavonich v. Meade*, 449 N.E.2d 1178, 1180 (Ind. Ct. App. 1983), for treating notice provisions and cooperation clauses as the same. *Miller* specifically disapproved of this view; that decision made clear the distinction between cooperation clauses and notice provisions. 463 N.E.2d at 265.

90. Notice serves the purpose of alerting the insurer to possible claims, and giving the insurer time to investigate those claims in order to prepare an adequate defense and thwart fraudulent claims. 2 R. LONG, *supra* note 1, § 13.02, at 13-16. Without timely notice the insurer may be unable to have sufficient time to investigate. See also *Tate*, 303 N.C. at 397, 279 S.E.2d at 775.

91. 2 R. LONG, *supra* note 1, § 13.02, at 13-16; and 8 J. APPLEMAN & J. APPLEMAN, *supra* note 15, § 4731, at 2-4.

92. See 2 R. LONG, *supra* note 1, § 13.02, at 13-16.

93. See generally *supra* note 25.

94. "Because it takes prejudice into account, the new rule does not affect the *ability* of the insurer to investigate and defend. Thus, the *risk* undertaken by the insurer remains unchanged." *Tate*, 303 N.C. at 396, 279 S.E.2d at 774 (emphasis in the original).

insurance industry is considered. The insurance business is based upon what the insurer considers to be an acceptable risk as determined by actuarial tables.⁹⁵ The insurer does not accept all risks, the insurer accepts only those risks whose probability of occurring is low enough to make assuming liability for that risk profitable.⁹⁶ The probability of a risk occurring is incorporated into the insurance policy, and helps to determine whether an insurance policy should be given to the applicant.⁹⁷ Timely notice may also permit a prompt settlement which relieves the insurer of litigation costs.⁹⁸ Therefore, the insurer's business is not to assume liability for any and all risks, and timely notice is critical for the insurer to assume liability only for those risks that will provide a profit.⁹⁹

The importance of the above formulation of prejudice is apparent when we examine the insurance industry's method of calculating its risks. The insurer runs his business in regard to calculated risk.¹⁰⁰ Imposing an uncalculated risk on the insurer will cause it to suffer unprepared losses and

95. See 43 AM. JUR. 2D *Insurance* § 133.

96. R. MEHR & E. CAMMACH, *PRINCIPLES OF INSURANCE* 6 (6th ed. 1976).

97. An ideal rate allows the insurer exactly enough income to meet insurance losses and expenses attributable to each large group of risks of the same quality, and also provides the insurer with a reasonable margin. A. MOWBRAY & R. BLANCHARD, *INSURANCE* 372 (5th ed. 1961). However, this is an *ideal* rate; reality interjects less certainty. "What is done in a particular line of insurance depends on the attitude of the insurers, policies of state insurance departments, available data, and the state of actuarial science in that line." *Id.* Nevertheless, risk is not excluded from an insurer's calculation, but instead there is a difference in the accuracy of the rates. *Id.*

98. In addition, prompt notice for a liability insurance policy can aid in settlement negotiations. R. MEHR & E. CAMMACH, *supra* note 97, at 252.

99. Liability is assumed only where a profit is possible. See A. MOWBRAY & R. BLANCHARD, *supra* note 97. Mehr and Cammach substantially agree with Mowbray and Blanchard:

The adequacy of a rate is determined by comparing the actual loss ratio with the one assumed in computing the rate. The 'assumed loss ratio' is the estimated percentage of the total *earned premium* needed to pay *incurred losses*, including loss-adjustment expenses. The remainder is available for operating expenses, taxes and profits.

R. MEHR & E. CAMMACH, *supra* note 96, at 601. Earned premiums are the premiums allocated to the one year period that insurance coverage exists, and are to be differentiated from written premiums. Written premiums include all the premiums collected during the same period. Incurred losses include losses paid, those incurred but not yet reported, those reported but not yet paid, and any other losses incurred in the twelve month period; paid losses are those losses that are disbursed during the same time period. *Id.*

100. "The success of a cooperative plan such as insurance requires as equitable a distribution of costs among participants as possible. Maintaining a semblance of equity among policyholders is the job of the underwriter, who must classify and rate each loss exposure." R. MEHR & E. CAMMACH, *supra* note 96, at 6. Complete equity is impossible as this would require that no two insureds be treated the same, and thus wreck the principle of total loss values through large numbers of homogeneous loss units. *Id.* at 602. Thus, that the insurance business is a calculated risk business should be adequately demonstrated. See also *supra* notes 97 and 99.

the result will be financially embarrassing to an insurer unable to cover its losses.¹⁰¹ A financially embarrassed insurer will be unable to perform the socially beneficial task of spreading risk.¹⁰² Eventually, the loss will fall upon those who will be unable to obtain the services of an insurer, namely, those unable to pay the increased premiums the insurer requires for covering the uncalculated losses. This result is as undesirable as releasing the insurer from liability under the strict contract rule and leaving the insured to bear the liability alone.

Defining prejudice as the insurer assuming uncalculated liabilities also illuminates the insured's difficulty in proving prejudice. It is the insurer who knows how much its interests have been affected by the delayed notice, for the insurer has already calculated what the risk to those interests are.¹⁰³ The insurer, not the insured, has access to the information regarding how these calculations have been altered, and the insurer's access to this information eases the insurer's task of proving prejudice. Thus, the reasonableness-of-the-delay rule places the burden of rebuttal on the wrong party. The third rule makes prejudice more analogous to an affirmative defense upon the part of the insurer by using prejudice as an element in determining the delay's reasonableness.¹⁰⁴ Because the insurer has better access than the insured to the information concerning prejudice, it seems logical that the reasonableness-of-the-delay rule, which requires the insurer to prove prejudice, offers a more desirable approach.

V. THE PURPOSE OF NOTICE

The proper conception of notice is the crux of the problem in delayed notice cases. Notice is how the insurer learns that a claim has arisen under the insurance policy.¹⁰⁵ The courts consider a lack of notice prejudicial to the insurer's interests.¹⁰⁶ The common conception of notice is that notice is a condition precedent to the insurer's obligations under the insurance policy; if the insured does not give notice the contractual condition is not satis-

101. R. MEHR & E. CAMMACH, *supra* note 96, at 7.

102. *Id.*

103. *Id.*

104. *See* Great Am. Ins. Co. v. C.G. Tate Constr. Co., 303 N.C. 387, 397, 279 S.E.2d 769, 775 (1981); Comment, *supra* note 9, at 268.

105. *See supra* notes 1-2.

106. A look to the purpose of notice that has been assigned by the courts and commentators, the ability to investigate a claim, shows that the amount of prejudice is equivalent to the amount of time that notice is delayed. *Miller v. Diltz*, 463 N.E.2d 257, 265 (Ind. 1984), 2 R. LONG, *supra* note 1, § 13.02, at 13-16; 8 J. APPLEMAN & J. APPLEMAN, *supra* note 15, § 4731, at 2; 13A G. COUCH, *supra* note 2, § 49:2, at 227; R. MEHR & E. CAMMACH, *supra* note 96, at 252. This is particularly true with liability insurance that has been described as "defense insurance." R. MEHR & E. CAMMACH, *supra* note 96, at 252.

fied and the insurer need not perform.¹⁰⁷ This conception of notice as a condition precedent does not address realities underlying notice, namely, whether the insured had the requisite knowledge that the policy required notice of an event.¹⁰⁸ The better conception of notice recognizes that for notice to exist, the insured must know that an event is covered by the insurance policy and that notice is to be given for this event.

The distinction must be made between notice as knowledge and notice as notification.¹⁰⁹ Notice can be divided into two major subdivisions of cognitive notice and absolute notice.¹¹⁰ Knowledge exists when one is aware of

107. Generally, the insurer has no other means of acquiring knowledge that an event has occurred which leads to a claim against the insurer, other than notice from the insured. For this reason the courts have considered notice to be a condition precedent to the insurer's liability for the claim. 2 R. LONG, *supra* note 1, § 13.03, at 13-8 to -11. Notice may be given by one other than the insured (this may be the victim) for the insured's benefit, but only the insured is contractually obligated to give notice. *Id.*, § 13.06, at 13-28. It should be noted that notice is important and necessary for both insured and insurer. The insured wishes the insurer to defend claims against the insured, and prompt notice will lead to a better defense than delayed notice. *See Tate*, 303 N.C. at 397, 279 S.E.2d at 775. This note is concerned with a more practicable standard for reviewing delayed notice, one which preserves all interests to the insurance policy.

108. Consideration must be given to the type of policy that is involved in each factual situation. Each line of insurance — life, marine, inland marine, automobile, worker's compensation, and liability — have their rates made in a different manner. A. MOWBRAY & R. BLANCHARD, *supra* note 97, at 383-91. There is also a difference in the legislative treatment of the different types of insurance. *See Johnson Controls, Inc. v. Bowes*, 381 Mass. 278, 409 N.E.2d 185 (1980) (changed the rule for delayed notice in cases that are not covered by a statute that applies only to motor vehicle liability coverage). In *Farmers Auto. Ins. Ass'n v. Hamilton*, 31 Ill. App. 3d 730, 734, 335 N.E.2d 178, 181 (1975), the Illinois Appellate Court recognized in dicta that a homeowner's policy is more difficult than an automobile policy. Nor is the classifying of all liability as defense insurance to be taken as opposing this requirement for considering the specific insurance policy. *See R. MEHR & E. CAMMACH, supra* note 96. Such classifying goes only to the purpose of the policy; the requirement proposed here goes to the language of the policy, the methods used in rate-making for the policy, and to the expectations of the parties. *See also Hartford Accident and Indem. Co. v. Phelps*, 294 So. 2d 362, 365 (Fla. Dist. Ct. App. 1974); *Milwaukee Mut. Ins. Co. v. Butler*, 615 F. Supp. 491, 494 (S.D. Ind. 1985).

109. The generic sense of notice includes all forms of knowledge or the equivalent of knowledge, but judicial interpretation of statutory or other language has frequently interpreted notice to be synonymous with notification, excluding knowledge or inquiry. 1 M. MERRILL, *MERRILL ON NOTICE* § 12 (1952). This sort of judicial interpretation has led to a distinction between knowledge and notice. *Id.* "What is usually meant is that knowledge is but one form of notice and hence [the] want of knowledge does not preclude notice in some other way. . . . Ordinarily we should expect to find the term notice used in its generic sense." *Id.* § 2, at 2.

110. "The term cognitive notice, as employed herein, is used to denote those situations in which notice is dependent on the noticee's awareness, at the time the notice is to be effective, of the facts constituting it." *Id.* § 3, at 3. Cognitive notice does not require forgotten facts for notice, nor is knowledge gained from investigation required unless there is a duty to inquire. *Id.* Merrill considers knowledge to be a narrower term than notice: "Usually, it does not include that cognitive notice arising out of the knowledge of matters sufficient to arouse inquiry

a fact's existence;¹¹¹ absolute notice includes notification, unforgettable knowledge and facts which one is required to know.¹¹² In the insurance context, the insured is required, as is any party to a contract, to know the contents of the insurance policy. This requirement would seem to place notice to the insurer in the absolute notice category.¹¹³ Yet, a distinction must be made between reading an insurance policy and understanding the meaning of the policy's provisions. As long as the insured is the party that has the responsibility and ability for detecting and reporting events that will give rise to a claim under the insurance policy, the insured must know the

concerning the existence of the ultimate facts with notice of which one is to be charged." *Id.* § 4, at 4.

"Absolute notice is that notice the effectiveness of which is not dependent upon the noticee's continued awareness of the matters out of which it arises." *Id.* § 7, at 5. Included under absolute notice are notification, unforgettable knowledge, and facts which one is under a duty to know. *Id.* § 2, at 2. Merrill gives as examples of absolute notice a recorded instrument or a published notification which is not seen. *Id.* § 7, at 5.

111. In the insurance context, the insured being charged with giving notice of an event which will give rise to liability is the party who must know that liability exists. The insured must know the policy's coverage before he can give notice. This rationale is implicit in *Ohio Casualty Ins. Co. v. Rynearson*, 507 F.2d 573, 578-79 (7th Cir. 1974), where the Seventh Circuit held that an insured who had been a claims adjuster and was an attorney was to be held to a higher standard. *Id.*

Notification is notice for performing an act which the law finds sufficient for notice; it is the act and not the awareness of the act which is important. 1 M. MERRILL, *supra* note 109, § 8, at 5. Unforgettable knowledge occurs when knowledge is gained and the law requires such knowledge be retained; once gained, the knowledge is considered to have created notice. *Id.* § 9, at 7.

What facts which one is under a duty to know depends upon the particular field of law at issue. *Id.* § 10, at 7. Ordinarily there is no such duty to possess knowledge. *Id.* § 472, at 437. A duty may be imposed when there is the means to secure knowledge plus there exists a danger of harming another, or the duty is imposed by contract, custom, or statute. *Id.* §§ 473-77, at 437-77. Because the insurer writes the insurance policy and it includes technical language, the insured will be in a difficult position if he is required to know facts which are not easily ascertainable under the policy. This problem is increased by having occurrence defined from the insurer's viewpoint. See *Rynearson*, *supra* note 2, at 521-24.

112. This knowledge may appear to fall within the presumption that the insured has read the insurance policy. See 7 WILLISTON ON CONTRACTS, *supra* note 1, § 906B, at 300; Comment, *supra* note 14, at 579; and Case Note, *Insurance — Charging the Insured with Notice of the Contents of the Policy*, 30 TEX. L. REV. 634 (1952) (criticism of the judicial presumption that the insured has read the insurance as being unrealistic).

113. Asking the insured to be fully knowledgeable about a policy's coverage is unrealistic as the insurer may not be fully knowledgeable about the policy's coverage. The plaintiff's insurance agent in *Milwaukee Guardian Ins., Inc. v. Reichhart*, 479 N.E.2d 1348 (Ind. Ct. App. 1985), was not absolutely certain that coverage existed. See Brief for Defendant-Appellant, *supra* note 40. Reichhart's insurance agent is a minor example compared with the problems Washington insurers faced with plain English policies and proximate cause; the result seems to have been confusion. See Comment, *supra* note 14, at 574-77, 582. If an insurer with all the technical and legal resources available to it is not able to meet these problems, then the insured will find the task impossible.

events that are covered by the insurance policy.¹¹⁴ This is particularly pertinent when a common factor in delayed notice cases involves vague policy provisions.¹¹⁵

The first step that the courts must take in overcoming the notice problem is to recognize the insurance policy as an adhesion contract.¹¹⁶ The insurer is the writer of the insurance policy and thus controls both the content and the wording of the policy's provisions.¹¹⁷ The insurer dictates the policy's terms to the insured.¹¹⁸ The insured should not be presumed to have knowledge of the policy's provisions in the same manner as a party to a bargained contract. Since the insured should not be presumed to have such knowledge, the insured's notice requirement should not be placed in the category of absolute notice.¹¹⁹ Furthermore, if we recognize the insurance policy as an adhesion contract, the insurer has the power to control and prevent delayed notice with its control of the policy's language. Such power

114. What constitutes an occurrence is defined from the insurer's viewpoint; the insured needs the ability to recognize a coverable event. *See* Rynearson, *supra* note 2, at 521-24.

115. *See*, for example: Hartford Accident and Indem. Co. v. Phelps, 294 So. 2d 362 (Fla. Dist. Ct. App. 1974); Farmers Auto. Ins. Ass'n v. Hamilton, 31 Ill. App. 3d 730, 335 N.E.2d 178 (1975); Milwaukee Guardian Ins., Inc. v. Reichhart, 479 N.E.2d 1340 (Ind. Ct. App. 1985).

116. A contract of adhesion is one where the seller or manufacturer presents a standard form which the other party has no choice other than to accept or reject. J. CALAMARI & J. PERILLO, *supra* note 28, at 6. *See also infra* note 118.

117. "[T]he insurance contract usually is a contract of adhesion. The agreement generally is prepared by lawyers and other representatives of the insurer, or perhaps by representatives of the state regulatory bodies and offered to the prospective insured on a 'take it or leave it' basis." R. MEHR & E. CAMMACH, *supra* note 96, at 162. *See also infra* note 118. In Indiana, a statute provides mandatory policy provisions, but no actual writing is done by a state agency.

118. Young, Lewis & Lee, *supra* note 71, at 74, note that:

Generally, [the insured] does not propose or draft a single clause or phrase in the policy.

He accepts that which has been written by the company or nothing at all. There is a likelihood, in fact, that the insured will not see the document evidencing his "agreement" until after he has paid his first premium.

An overwhelmingly important aspect of an adhesion contract is that the drafting party has the superior bargaining power over the non-drafting party. *See* Patterson, *The Interpretation and Construction of Contracts*, 64 COLUM. L. REV. 833, 856 (1964).

119. *See* Cooper v. Gov't Employees Ins. Co., 51 N.J. 86, 94, 237 A.2d 870, 874 (1968). Also, the insured should not be presumed to have the same general knowledge about insurance as the insurer. A distinction must be made between what the insured and insurer know about insurance; this distinction is analogous to the Uniform Commercial Code's implied distinctions between merchant and non-merchant. *See* U.C.C. § 2-104 (1978). The insurer fits the Uniform Commercial Code's definition of a merchant as "a person who deals in goods of the kind or otherwise by his occupation holds himself out as having knowledge or skills peculiar to the practices or goods involved in the transaction." *Id.* Applying this concept to the insurance context would mean that the insurer is to be held to a higher standard of knowledge than the insured, unless the insurer transmits such knowledge to the insured. Otherwise, the insured should not be presumed to have the same general knowledge about insurance as the insurer.

will be worthless where the court presumes that the insured understood the policy, even though the insured does not understand the policy.

VI. THE INSURANCE POLICY AS AN ADHESION CONTRACT

The classic contract consists of two parties bargaining at arms' length whose final agreement is embodied in the contract.¹²⁰ The contracting parties are able to impose their own goals and protect their own interests through the bargaining process.¹²¹ The process requires that the parties possess equal bargaining positions; where the parties do not have equal bargaining positions, an adhesion contract exists.¹²² The adhesion contract was so named because the weaker party had to adhere to the stronger party's terms.¹²³ The adhesion contract is most commonly embodied in the form contract.¹²⁴

Recall that the insurance policy is an adhesion contract.¹²⁵ There is no equality in the parties' bargaining power. The policy is dictated by the insurer, and, in short, the only choice left to the insured is to decide which insurer will receive his business.¹²⁶ The courts have recognized the unequal power between the insurer and insured, and have attempted to balance the parties' positions.¹²⁷ The courts' preference for the insured is in part traceable to the preference given to the traditional contract between two equal

120. J. CALAMARI & J. PERILLO, *supra* note 28, at 6.

121. "True freedom of contract only exists where the contract manifests two ingredients: the freedom to enter into the contract and the freedom to influence the terms of that contract. In truth, the average insured possesses none of the latter type of freedom and very little of the former." Trakman, *Adhesion Contracts and the Law of Insurance*, 13 MAN. L.J. 23, 24 (1983).

122. *Id.* See also *Great Am. Ins. Co. v. C.G. Tate Constr. Co.*, 303 N.C. 387, 397, 279 S.E.2d 769, 775 (1981); Kessler, *Contracts of Adhesion — Some Thoughts About Freedom of Contract*, 43 COLUM. L. REV. 628, 632 (1943). Trakman continues:

The insurance company dictates the terms of the contract, to these the insured must adhere. There is no real bargaining over contract clauses, there is no serious haggling over terms. From the insurance companies perspective, the entire arrangement is predetermined. For the insured, terms contained in liability exclusion or limitation clauses are standardized penalties encountered in meeting a very definite, and almost irreversible, need for insurance.

Trakman, *supra* note 121, at 24.

123. *Id.*

124. *Id.*

125. See Patterson, *supra* note 118, at 857.

126. Premising the concept of an insurance policy as an adhesion contract, the insurer is the more powerful of the parties to the insurance policy. The insurer has the power to correct the wording of the policy and the power to correct is also the power to prevent. Hence, the insurer should take upon itself the task of avoiding vague policy provisions. See Trakman, *supra* note 121, at 24; 7 WILLISTON ON CONTRACTS, *supra* note 1, § 900.

127. See generally *supra* note 73.

parties bargaining for a mutually acceptable agreement.¹²⁸ The courts' treatment of delayed notice is also influenced by the adhesive nature of insurance contracts.¹²⁹ Although courts recognize the adhesive nature of insurance contracts, they have failed to recognize that the insurer controls the policy's language, the vagueness of which is a common cause for delayed notice.¹³⁰

The courts use public policy for interposing themselves into adhesion contract situations. The courts that have dealt with delayed notice in an adhesion contract context have been principally concerned with the social policies represented by insurance and the forfeiture of insurance coverage caused by a reasonably delayed notice.¹³¹ The social policies served by insurance include optimum allocation of resources, acquisition of knowledge about causes for losses, indemnification for losses, and being a resource for credit.¹³² However, the most important social policy insurance serves is as a device for voluntary resource redistribution.¹³³ Insurance spreads the risk of injuries and their subsequent costs among a wide group. This risk spreading function is important to the courts and they have gone beyond the limitations of a strict contractual approach.¹³⁴ The alternative is to leave the risk of injury upon one person, and this alternative is becoming more unacceptable as the costs of paying for injuries continues to increase beyond a single person's ability to pay.

Courts have further protected the insured, and the risk spreading function, by disfavoring forfeitures of insurance coverage, unless no other alternative exists.¹³⁵ The courts' dislike of forfeiture has led to differences in how delayed notice is treated. The jurisdictions adhering to the strict contract approach find only a contract at issue. Those jurisdictions using the prejudice concept find more than a mere contract at issue, these courts recognize the need to protect the social policy served by insurance. Courts protect the social policy behind insurance by recognizing that the insurance policy is an adhesion contract in which the insurer has the controlling power. The courts act upon this fact by favoring the insured.

The insurer's superiority over the insured should be explicitly recognized in connection with the insurance policy's provisions.¹³⁶ The insurer's

128. *Id.*; see also J. CALAMARI & J. PERILLO, *supra* note 28, at 6-11 (philosophy of contract law centers around individuals).

129. See *supra* note 8.

130. See *supra* note 80.

131. See *supra* note 71.

132. R. MEHR & E. CAMMACH, *supra* note 96, at 11.

133. *Id.*

134. See *supra* notes 11, 71 and accompanying text.

135. See Comment, *supra* note 9, at 266.

136. The insured has imputed knowledge of the insurance policy. See 44 AM. JUR. 2D

superior bargaining position enables the insurer to cheaply and efficiently mass market insurance. The policy is then written in accordance with actuarial tables which present the average risks that the insurer must avoid to make a profit on the policy. It is the insurer who has the superior bargaining position, and so the insurer has control over what the policy provides and how the policy's provisions are written. Vague policy provisions clearly contribute to the insured's delay of notice.¹³⁷ Thus, courts should recognize the relationship between the insurer's control of policy provisions and the vagueness of those same provisions. The insurer should be given the responsibility to make the policy's provisions clear. Courts should recognize that vague policy provisions were created by the insurer, and that the responsibility for the policy's vagueness lies with the insurer and not with the insured. The insurer should not be allowed to hide behind vague provisions when notice is delayed. A vague clause should be interpreted against the drafter.¹³⁸ Therefore, for the reasons discussed, Indiana courts should reassess the current analysis of delayed notice, and eliminate the inequity resulting to the insured under the current notice rule.

VII. A PROPOSED SOLUTION

This note proposes a solution that is grounded upon three premises. The first premise is that timely notice requires that the insured know that when an event occurs, the insurance policy covers the event and notice is due.¹³⁹ The second premise is that an insurance policy is an adhesion contract dominated by the insurer, with delayed notice due largely to vague and unconscionable policy provisions.¹⁴⁰ Finally, the third premise is that the proposed solution must not threaten the insurer's financial interests.¹⁴¹

Insurance § 1342, at 272 (1982). This imputed knowledge should be qualified as the courts have held that one experienced and trained in insurance has a superior knowledge of insurance and when notice is due. *Ohio Casualty Ins. Co. v. Ryneerson*, 507 F.2d 573, 578 (7th Cir. 1974). Also, a common occurrence in delayed notice cases has been a third party informing an insured that notice is due. *See Milwaukee Guardian Ins., Inc. v. Reichhart*, 479 N.E.2d 1340 (Ind. Ct. App. 1985); *Hartford Accident and Indem. Co. v. Phelps*, 294 So. 2d 362 (Fla. Dist. Ct. App. 1974).

137. *See supra* note 80.

138. "The terms of an insurance policy should be construed liberally in favor of the insured only if there is an ambiguity in the policy's language." *Miller v. Dilts*, 463 N.E.2d 257, 265 (Ind. 1984).

139. *See supra* notes 105-19 and accompanying text for a discussion on the concept of notice and how knowledge is needed for giving notice.

140. *See supra* notes 120-38 and accompanying text for a discussion on the insurance policy as an adhesion contract.

141. This premise is derived from the practical consideration of insurance as a business. If the insurer is forced to undertake uncalculated and needless liabilities then either the insurer can no longer function or will do so at too great a cost for the insured. *See supra* notes 97, 99, 100 for a discussion of how an insurer conducts its business.

Based upon these three premises and the reasoning below, the best solution is a balancing approach that would place upon the insurer the burden to show prejudice and place upon the insured the burden of showing that his actions were reasonable and in good faith.

The Indiana Supreme Court has ruled that delayed notice creates a rebuttable presumption of prejudice to the insurer.¹⁴² The Indiana Supreme Court imposes the burden on the insured to prove that the insurer did not suffer actual prejudice, without stating how the insured was to prove that the insurer was not prejudiced.¹⁴³ The Indiana Court of Appeals, however, gave substance to the question of how the insured was to prove that the insurer had not suffered any prejudice. The court of appeals held that the insured's success in defending himself, and hence the insurer, was insufficient to show that delayed notice did not prejudice the insurer. The court reasoned that the insurer lacked a choice in counsel, the ability to guide the litigation, and the ability to participate in settlement negotiations.¹⁴⁴ This decision differed from other jurisdictions applying the same rule in regard to similar facts,¹⁴⁵ and it also differed from another application of the same rule of rebuttable presumption in Indiana.¹⁴⁶ The *Reichhart* decision changed the rebuttable presumption created by the Indiana Supreme Court into an irrebuttable presumption. The rule's metamorphosis is due to how the rule is applied. This proposal to change the rule stems from faults in the *Reichhart* decision; the premises of this proposed change are derived from specific faults in the Indiana approach.

The first premise, that timely notice requires that the insured know when notice must be given, requires an examination of the insured's actual knowledge. Indicative of such knowledge are the insurance policy itself,¹⁴⁷ the insured's knowledge of and experience with insurance,¹⁴⁸ and the in-

142. *Miller*, 463 N.E.2d 257.

143. *Id.* at 265. The Indiana Supreme Court said that the insured could find some evidence that prejudice did not occur, and upon presenting such evidence, the question becomes one for the trier of fact. *Id.* at 265-66. The insurer is able to introduce evidence of prejudice. *Id.* at 266.

144. *Milwaukee Guardian Ins., Inc. v. Reichhart*, 479 N.E.2d 1340, 1343 (Ind. Ct. App. 1985). *See also supra* note 84.

145. *See supra* notes 47-57 and accompanying text.

146. *See supra* notes 58-61 and accompanying text.

147. In particular, the policy's language should be examined for determining how clearly an event is covered. For if notice requires that the insured knows when notice is due and if the delay is judged by a reasonableness standard, then the policy's language needs to be examined to determine if the insured's ignorance was reasonable in light of the policy's language. *See supra* note 106.

148. The best example of testing an insured's knowledge and experience is in *Ohio Casualty Ins. Co. v. Rynearson*, 507 F.2d 573 (7th Cir. 1974). There, the insured, who had been trained as a claims adjustor, was held to a higher standard of care than an ordinary insured. *Id.* at 579.

insured's reasonable expectations of coverage.¹⁴⁹ An excuse will fail if the insured knew from the policy that coverage existed, or if he has personal knowledge of coverage from training or experience in insurance. Yet, when the insured does not know that notice is due, and has no access to information before notice becomes untimely, the insured should be excused for delayed notice.¹⁵⁰ The conclusion that notice is delayed should be attributable to the manner in which the insurer has written the policy. The insured must know that notice must be given. Thus, the insured should only be penalized for delayed notice when the insured knows that notice was due.

The second premise, that the insurance policy is an adhesion contract and that vague policy provisions contribute to delayed notice, relates to the insurer's control over the insurance policy.¹⁵¹ The insurer controls what provisions the policy contains and the policy's language.¹⁵² The corollary to recognizing the insurance policy as an adhesion contract is that the insurance policy gives information in the manner in which the insurer wishes it to give information. Where the insurance policy is vague as to whether the policy's coverage extends to a specific event, and the insured gives delayed notice only after a third party informed him that coverage may exist, the failure to give timely notice should be excused. The insurer controls the policy's language, and has the ability to correct a provision's vagueness or to give explanations to the insured outside of the policy. Where prevention by the insurer is possible, the insurer should bear the burden for delayed notice. Courts recognize that insurance serves an important social function

149. The insured's reasonable expectations are to be considered indicative of what the insured thought he was buying with his premiums. The reasonable expectations doctrine has been defined as providing coverage when the reasonably objective expectations of applicants and intended beneficiaries would be negated by a specific provision. Keeton, *Insurance Law Rights at Variance with Policy Provisions*, 83 HARV. L. REV. 961, 967 (1971). As used here, the reasonable expectations doctrine would operate only when the insured is lacking real knowledge about the policy's coverage; real knowledge is defined as the explicit information about the policy's coverage derived from either the policy or the insurer. See Young, Lewis & Lee, *supra* note 71, at 78. In operation, an insured should be excused only when he did not reasonably believe coverage existed. *But see* Mayhew, *Reasonable Expectations: Seeking a Principled Application*, 13 PEPPERDINE L. REV. 267 (1986) (reasonable expectations doctrine as a covert judicial tool for reducing harshness in policy provisions).

150. The courts have interpreted an immediate notice requirement as meaning as soon as practicable. The requirement is that the circumstances did not allow for notice to be given earlier. 2 R. LONG, *supra* note 1, § 13.09; 8 J. APPLEMAN & J. APPLEMAN, *supra* note 15, § 4734; 13A G. COUCH, *supra* note 2, § 49:115. Yet, if the insured did not know that notice was due, but gives notice upon acquiring such knowledge, then the notice should be considered as having been given as soon as practicable.

151. See generally *supra* notes 120-27 and accompanying text for a discussion of adhesion contracts.

152. See Trakman, *supra* note 119, at 24; and K. ABRAHAM, *DISTRIBUTING RISK: INSURANCE, LEGAL THEORY, AND PUBLIC THEORY* 31-35 (1986) (discusses the inequitable balance favoring the insurer in terms of information and power).

via spreading risk. The courts have protected this social policy by disfavoring forfeitures when those forfeitures would injure the insured more than the insurer.¹⁵³ In this manner, the courts have given the insured the same protection that has been given to the parties to an adhesion contract.

The third premise, that a proper solution cannot ignore the insurer's interests, is necessary to protect the insured's interests and the social benefits of insurance. The insured is interested in having the protection of insurance; insurance which benefits society by spreading the risk encountered by individuals.¹⁵⁴ Neither the individual nor society will benefit from injuring the insurer's business. If the insurer incurs uncalculated losses, unassumed liability, then the cost of insurance will increase or the insurer will leave the marketplace.¹⁵⁵ The insured will not benefit if insurance is too costly, and society will not benefit from a mass of uninsured individuals. Therefore, the insurer must bear the responsibility for vague policy provisions. However, a limit must be established to maintain a balance between the insurer's liability and the insured's expectations.

The proposed solution following from these three premises is a variant of the reasonableness-of-the-delay rule. This solution is described best according to the parties' evidentiary burdens. The insured has the burden of showing that the event was not reasonably ascertainable from the insurance policy, from his own experiences, or from the insured's reasonable expectations concerning coverage. In short, the insured must show that he did not know that coverage existed and, hence, that notice was due.¹⁵⁶ The insured's reasonable expectations are relevant since the insured did not contribute to the drafting of the insurance policy, and since it is unlikely that the insured has read the policy or understood what he may have read.¹⁵⁷ The delay's length is relevant only in relation to how the insured discovered that coverage existed and that notice was due.¹⁵⁸ These factors are to be

153. See generally *supra* note 67.

154. See K. ABRAHAM, *supra* note 152, at 18-20 (philosophical bases and methods for distributing risk). See *supra* notes 97, 99, 100 and accompanying text for more business-oriented reasons and methods for risk distribution. See also *Cooper v. Gov't Employees Ins. Co.*, 51 N.J. 86, 90, 237 A.2d 870, 874 (1968) (specific purpose of compensating negligence victims).

155. This is a reasonable interpretation of the business methods of insurance. See *supra* notes 97, 99, 100.

156. Allocating the burden of proof entails two considerations: who desires to change the status quo, and which party has the access to the facts. C. MCCORMICK & E. CLEARY, MCCORMICK ON EVIDENCE 949-50 (3d ed. 1984) [hereinafter MCCORMICK ON EVIDENCE]. It is assumed that the insured is the party seeking to change the status quo, and there are facts lying peculiarly within the insured's knowledge. *Id.*

157. See also *supra* note 149 (discussing reasonable expectations).

158. It is logical to take into consideration the means by which the insured could have shortened the notice delay. The insured is acting unreasonably if he knew he had resources available to him and did not notify his insurer. The logical source for this information would

used by the trier of fact in determining whether the insured had a reasonable basis for his actions.

The insurer's burden is to show that its interests are prejudiced by the delayed notice. If the insurer cannot show actual prejudice, then its contractual obligations cannot be avoided. The proposed formulation of prejudice is that if an event occurs which alters the liability that the insurer assumed, prejudice occurs.¹⁵⁹ Thus, prejudice will depend upon each policy because variations exist between different types of policies. The insurer will need to show that delayed notice changes the basis upon which the risk of liability was calculated so as to transform the liability into an uncalculated risk. If, however, the delayed notice does not transform the liability into one that was uncalculated, but, instead, only delays a calculated risk, then the insurer should not be allowed to claim that its interests are prejudiced. Since the information needed to show prejudice is in the insurer's control, the insurer properly has the burden of proving prejudice.¹⁶⁰

Upon completion of the insured's and the insurer's evidentiary burden, the trier of fact will need to decide two issues. These issues are the delay's reasonableness, and what prejudice to the insurer resulted from the delay. While the facts of each case must determine the outcome for each issue, the important item is that the insurer cannot escape liability unless the insured acted unreasonably and in bad faith. In short, the insured will be protected unless he knew that notice was due.

A further examination of how the trier of fact is to treat these issues may be helpful. The first issue requires the use of the reasonably prudent person and good faith standards. Since these standards have long been used by the courts, their use in the delayed notice cases should not prove a conceptual or practical hardship. What the trier must specifically decide is if a reasonably prudent person — a person with the same knowledge of insurance, the same insurance policy, and the same reasonable expectations of coverage — would have made the same decision to not give notice. Here the reasons for the length of the delay are relevant, for if the insured should have obtained the requisite knowledge earlier than he actually did, then the reasonableness and good faith of his delay becomes more questionable.

Assuming that the trier finds that the insured acted as a reasonably

be the insured's insurance agent, and this criterion was implicitly used by the Indiana Court of Appeals. *Milwaukee Guardian Ins., Inc. v. Reichhart*, 479 N.E.2d 1340, 1342 (Ind. Ct. App. 1985). However, this inquiry is useless unless the insured had a reason to think that coverage existed. The insured should be faulted where an inquiry is made, a concrete answer is given, but the insured still does not take action.

159. See *Great Am. Ins. Co. v. C.G. Tate Constr. Co.*, 303 N.C. 387, 397, 279 S.E.2d 769, 775 (1981).

160. See *supra* note 156.

prudent person and in good faith, then the trier must address the issue of prejudice. The issue of prejudice has two components: the risk of liability assumed by the insurer and the actual damage caused by the delay to the liability assumed.¹⁶¹ If the trier finds that the insurer assumed liability for an event and the insurer was not actually damaged, then the insurer is not prejudiced. If the insurer is actually damaged by a reasonable delay, then the damages must be apportioned by the time notice was delayed.¹⁶²

The ordinary reasonableness-of-the-delay rule results in a conflict when both prejudice and reasonableness of the delay occur. The result is that the insurer might not be liable for the claim.¹⁶³ With the solution proposed in this note, the insurer will be liable so long as the delay was reasonable and in good faith. This result is justified because the test for reasonableness and good faith includes an examination of the insured's insurance policy, knowledge of insurance, and the reasonable expectations of the insured concerning coverage. The insurer has the ability to correct any mistaken belief held by the insured before the event requiring notice occurs. When the insurer does not prevent an insured's mistaken beliefs concerning coverage, the insurer should not escape liability, for the insured is relying upon the insurer to indicate when notice is due.¹⁶⁴

Principally there are four criticisms of the proposal: 1) that the proposed rule will be an onerous burden to the insurer; 2) that the established duties of the insured to read the policy¹⁶⁵ and to inquire about the extent of

161. By formulating prejudice as the change in risks assumed caused by the delay, then these factors are relevant to the issue of prejudice.

162. *Reichhart* provides a useful example. In *Reichhart*, the notice was delayed until after the insured won the claim for which he was seeking reimbursement of attorney's fees. 479 N.E.2d at 1341. Under this rule, the trier of fact would look to the fees and possible settlements which an insurer had calculated in assuming liability. The trier of fact would then compare the settlement offer actually made and the fees actually charged. The insurer would then be liable for the amount calculated or the fees charged, whichever would be the lesser.

163. See *Cooper v. Gov't Employees Ins. Co.*, 51 N.J. 86, 92, 237 A.2d 870, 873.

164. The author in his analysis of the expectation principle as a doctrine of equity notes: First, if the insurer knew or should have known of the insured's expectations, the equities weigh heavily in favor of holding it responsible for fulfilling them. . . . The policy would be reformed to conform to the insured's expectations. Second, if the insurer also created or helped create those expectations, equity would suggest even more strongly that those expectations be fulfilled. The insurer would be estopped to deny the truth of the expectations it had induced. Finally, the insured's expectations must be reasonable before equity should demand that they be honored. In most cases, this criterion will be met if one of the other two is.

K. ABRAHAM, *supra* note 152, at 119.

165. "Older decisions, often now more honored in the breach, are replete with language to the effect that an insured is under a positive duty to read the contract delivered to him, and, under this antiquated rule, he will be presumed to have done so." 1 J. APPLEMAN & J. APPLEMAN, *INSURANCE LAW AND PRACTICE* § 173, at 531-32 (1981). See also 13A G. COUCH, *supra* note 2, § 12:16; 43 AM. JUR. 2D *Insurance* § 218 (1982) (both agree with Appleman

coverage are ignored;¹⁶⁶ 3) that the burden of proof is changed to favor the insured; and 4) that the insured is being favored at the insurer's expense. In addressing the first three criticisms, the last and most general criticism will also be addressed. Refuting the particular criticisms will also refute the general criticism.

The first criticism, that the proposed rule is an onerous burden for the insurer, neglects the power and control which the insurer possesses as the dominant party to an adhesion contract.¹⁶⁷ The insurer's power must include responsibility; the courts have already addressed this issue by protecting the weaker party to the adhesion contract, the insured.¹⁶⁸ This proposal seeks to create an affirmative duty for the insurer to plainly inform the insured about which events require notice.¹⁶⁹ If the insured has been informed about what events the policy covers, then the insured is not excused when notice of an event is delayed. In short, this proposal only favors the insured who has a vague insurance policy, is not fully knowledgeable about insurance matters, and does not reasonably expect policy coverage, all of which the insurer can easily correct.¹⁷⁰

The first criticism ignores the insurer's power; the second criticism ignores reality. The duty to read is often not performed by the insured,¹⁷¹ and the language may be too technical to be understood.¹⁷² The duty to inquire

and Appleman).

166. "Mere belief the injured person would not present a claim is not an excuse. The insured must take some good faith steps to investigate the accident or there will be no valid excuse for not reporting the occurrence." 13A G. COUCH, *supra* note 2, § 49:14, at 239. See also 8 J. APPLEMAN & J. APPLEMAN, *supra* note 15, § 4744; 2 R. LONG, *supra* note 1, § 13.12; 44 AM. JUR. 2D *Insurance* § 1343 (1982).

167. An adhesion contract being by definition a contract with a dominant party, and an insurance policy being an adhesion contract, the insurer is the dominant party. See Trakman, *supra* note 121, at 24; Young, Lewis & Lee, *supra* note 71, at 74; Patterson, *supra* note 118, at 856; R. MEHR & E. CAMMACH, *supra* note 96, at 162.

168. See generally, 7 WILLISTON ON CONTRACTS, *supra* note 1, § 900; see also Young, Lewis & Lee, *supra* note 71, at 75 (judicial intervention to protect consumers based on an adhesion contract theory); and Mayhew, *supra* note 149, at 272 (reasonable expectation doctrine evolved from judicial concern for insureds).

169. Generally speaking, a plain English insurance policy uses non-technical language; hence the term "plain English." See Comment, *supra* note 14, at 581-83 (explanation of plain English insurance policies). See also 1 G. COUCH, R. ANDERSON & M. RHODES, COUCH ON INSURANCE 2D § 1:16 (rev. ed. 1982) (criticizes plain language policies as litigation breeders).

170. The plain language policy would be the most direct and efficient method to inform insured's about coverage. This would provide a written, standardized and relatively permanent memorial of coverage. *But see Id.* Auxiliary means, such as oral instructions or brochures, either do not have the benefits of a plain English policy, or may face difficulties with the parol evidence rule.

171. See generally Murray, *Standardized Agreement Phenomena in the Restatement, (Second) of Contracts*, 67 CORNELL L. REV. 735 (1982).

172. That technical language leads insureds astray has resulted in state statutes that require plain language in insurance policies. See 1 G. COUCH, *supra* note 169, § 1:16 (gives

is useless unless the insured has a cause to inquire.¹⁷³ In short, these duties operate as a trap for the unsophisticated insured.¹⁷⁴ Allowing these rules to trap the insured will ruin the judicial rule against needless insurance forfeitures. These forfeitures will be needless, since under this proposal the insurer's interest is in fully informing the insured about the extent of the policy's coverage.

Finally, the criticism that the burden of proof favors the insured exposes nothing more than did the first two criticisms. The insured simply cannot show reasonableness if the insurer has explained the policy's coverage or the policy is clear about its coverage. Nor is changing the burden of proof technically incorrect. Generally, the burden of proof is allocated according to which party is trying to change the status quo and which party has access to information.¹⁷⁵ The insured has the burden of proof concerning his reasonableness, while the insurer has the burden of showing how and what prejudice resulted from the delay. Each party has the needed access to the facts necessary to meet its evidentiary burden; the insurer knows how its calculated risk has been altered and the insured knows how and why he delayed notice. The insurer is protected further because he can rebut the insured with a showing that the insured was fully informed that a particular event was covered by the policy. The insurer will be in a more desirable position under this proposal than under the present rule if the insured has been fully informed of the policy's coverage.

These criticisms do not show that the proposed solution overwhelmingly favors the insured. On the contrary, if the insured has been fully informed that an event is covered by his insurance policy and such an event occurs but notice is delayed, then the insurer is not liable for the event. This

examples of such statutes).

173. "Insureds, however, will often unjustifiably delay notice to the insurer in an attempt to discern whether they are liable, rather than placing that burden upon the insurer. They don't want to risk antagonizing the insurer when no actual liability exists on their part." Comment, *supra* note 9, at 262-63. This behavior would be prevented if the insured was clearly informed about events creating liability. See also Comment, *supra* note 14, at 579 n.70 and accompanying text.

174. One writer notes:

It seems harsh for the court in the principal case to impute knowledge of the insurer's mistake to the insured since it appears to be customary and reasonable for an insured not to read his policy. However, the insurance company should be charged with notice of the contents of the issued policy since any mistake in issuing the policy would be due to its own negligence.

Case Note, *Insurance — Charging the Insured with Notice of the Contents of the Policy*, 30 TEX. L. REV. 634, 635 (1952) (oriented towards a particular case, but particularly enlightening as to its date and the recognition that insureds were unlikely to read their policies).

See also 1 J. APPLEMAN & J. APPLEMAN, *supra* note 165, § 173 (details the pitfalls of the duty-to-read rule).

175. See *supra* note 156.

proposal merely adjusts the equities of power and information between insurer and insured. This is accomplished by requiring that the insurer fully inform the insured concerning what events require notice, and by changing the burden of proof to avoid the problems that the Indiana rule has with access to information and proving a negative fact.

VIII. CONCLUSION

The Indiana Supreme Court created a difficult burden of proof problem for an insured who delays notice of a claim against the insurer. Specifically, the burden of proof problem is the presumption created by the delay: whenever notice is delayed a rebuttable presumption of prejudice to the insurer arises, which can only be rebutted by the insured's showing that the delay did not prejudice the insurer. This rule puts great emphasis upon the delay's length and the insurer's interests; this rule is rooted in the characterization of notice as a contractual condition precedent. Furthermore, the Indiana rule in *Miller*¹⁷⁶ fails to recognize the nature of insurance contracts, and fails to protect the insured.

The first application of the *Miller* rule by the Indiana Court of Appeals, in *Milwaukee Guardian Insurance, Inc. v. Reichhart*,¹⁷⁷ pointed out the problems with the rule. *Reichhart* shows that the rule inequitably favors the insurer over the insured. The *Miller* rule's inequity stems from a reluctance to view an insurance policy as an adhesion contract with the insurer as the dominant party, a reluctance to believe that delayed notice can be caused by vague policy provisions which are written by the insurer, and an outright refusal to place the burden of proving prejudice upon the insurer, the party best able to show prejudice. The *Reichhart* decision demonstrates the faults of the *Miller* rule.¹⁷⁸

The proposal is offered as a solution to the problems created by *Miller* and demonstrated in *Reichhart*. Specifically, the proposal is the means of evaluating whether a reasonable person would have understood the insurance policy's provision that requires notice for the particular event in question in a specific case. This change requires that timely notice be given only when the insured knows that notice must be given, and that the party generating the policy provisions, the insurer, should bear the burden of vague

176. 463 N.E.2d 257 (Ind. 1984).

177. 479 N.E.2d 1340 (Ind. Ct. App. 1985).

178. The *Miller* court believed that an "insured party can establish some evidence that prejudice did not occur in the particular situation." *Miller*, 463 N.E.2d at 265. Once the injured party has presented its evidence of no prejudice, the insurer is to present its evidence of prejudice, and the trier of fact will then decide the issue. *Id.* at 265-66. In *Reichhart*, the emphasis on the time elapsed before notice was given and how even successful litigation can cause prejudice turns the idea that "some evidence" can establish no prejudice jejune. *Reichhart*, 479 N.E.2d at 1343.

policy provisions. Likewise, the insured and the insurer are given production of evidence burdens appropriate to their knowledge and roles: the insured must produce evidence supporting his reasons for delay and the insurer must produce evidence proving that its interests have been prejudiced.

The reasonableness-of-the-delay rule is posed to solve the inequities and inadequacies of the present rule. Therefore, this note has been careful to limit the grounds for excusing delayed notice and to offer possible means for the insurer to further limit causes for delayed notice. The purpose for limiting the excuses for delayed notice and for offering preventative measures is to leave to the insurer, as the dominant party, the opportunity to make these appropriate changes and to permit continued functioning of the insurance industry. Therefore, the reasonableness-of-the-delay rule is intended to equalize a relationship which is currently unequal between insurer and insured and not to replace inequality with inequality.

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