Insurance Policy Notice and Cooperation Clauses Survive Challenge

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South Carolina's courts have long and consistently articulated that insurance policies are contracts, governed by the general rules of contract construction. Our courts have just as consistently held that insurers may include conditions in policies as long as they do not run afoul of public policy or are not violative of the law. Among allowable conditions are notice clauses, commonly found in insurance policies and grounded in the logic that an insurer must have notice of a claim in order to undertake investigation and defense thereof. Notwithstanding the evident purpose of notice and cooperation clauses, they have been the subject of more than a century of litigation. The trend continued with *Neumayer v. Philadelphia Indemnity Insurance Company, et al.*, 2019 WL 3310474 (July 24, 2019). *Neumayer* presented the South Carolina Supreme Court with the novel argument that S.C. Code §38-77-142(C) abrogates notice and cooperation clauses included in insurance policies.

Neumayer, a pedestrian, was struck by a bus belonging to a childcare center, being driven by the center's employee. He suffered significant physical injury and filed suit against the childcare center and its employee as a result. Neither defendant responded to the complaint as a result of which a substantial default judgment was entered. Eighteen months after the entry of the judgment, Neumayer's counsel sought payment of the judgment from Philadelphia, which had issued a policy to the childcare center that was in effect at the time of the accident. This request for payment was Philadelphia's first notice of the suit. Philadelphia rejected the demand to pay the full judgment, asserting its indemnification obligation was limited to the statutory minimum coverage as a result of its insured's failure to provide notice of the claim. Neumayer filed a declaratory judgment action and the matter came before the court on the parties' cross motions for summary judgment.

The *Neumayer* court provided an in depth look at South Carolina's jurisprudence as it relates to insurance policies, the notice and

cooperation clauses included therein and the ultimate consequence of mandatory coverage found in the Automobile Reparation Reform Act (the Act) that requires compulsory coverage in order to protect those injured by negligent drivers.[1]

While notice provisions have long been acceptable, South Carolina, like many other jurisdictions, eventually acknowledged the potential unfairness of allowing an insurer to avert responsibility to an innocent third party due to the failure of its insured to provide notice of an accident and otherwise cooperate. Thus, the state adopted a notice-prejudice rule that provides that an insurer has the burden of demonstrating it was substantially prejudiced by the failure of its insured to meet the requirements of the notice and cooperation provisions of a policy. Then, with the eventual shift from voluntary to mandatory coverage came the question of whether insurers could continue to rely on the failure of insureds to comply with notice clauses in order to defeat mandatory coverage. Grounding its decision in the legislature's intent to protect innocent parties by mandating minimum limits, the Court of Appeals ultimately determined an insurer must pay the statutory minimum coverage even upon proof of substantial prejudice.[2] On the heels of that determination, the Act was modified by the addition of §38-77-142. Section 38-77-142(C), at issue here, provides that any endorsement, provision or rider attached to or included in a policy that purports to limit or reduce mandatory coverage is void. The question remained, however, in the event of failure to comply with notice or cooperation provisions, whether an insurer is required to pay *more* than the mandatory minimum if the insured purchased additional coverage. It was that gap Neumayer hoped to close with a determination that all notice and cooperation requirements are meaningless, pursuant to subsection (C), thus requiring insurers to pay policy limits – not merely mandatory limits.

The South Carolina Supreme Court previously addressed subsection (C), finding a family step-down provision was rendered ineffective thereunder because it reduced the coverage available under the policy, contrary to public policy.[3] Refusing, however, to further expand the interpretation of subsection (C) so to enervate the historical treatment of notice clauses, the *Neumayer* court instead concluded it was not the intent of the legislature to reverse long standing law concerning such clauses and, had it so intended, it would have done so. Rather, the court reasoned subsection (C) does not violate public policy, but instead works in conjunction with the notice-prejudice rule to reflect the essential balance between an insurer's significant interest in receiving notice of a lawsuit, thus allowing for proper investigation, and the right of an injured party to recover against a negligent driver to the extent of statutorily required coverage. Consequently, rather than abrogating notice and cooperation clauses, the *Neumayer* court found the statutory provisions consistent with the legislative intent behind the Act.

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[1] Originally found in Title 56 of the SC Code, this Act was later recodified in §38-77-10.

[2] See *Shores v. Weaver*, 315 S.C. 347, 433 S.E.2d 913 (Ct. App. 1993).

[3] See *Williams v. Gov't Employees Inc. Co.*, 409 S.C. 586, 762 S.E. 2d 705(2014), addressed and distinguished in *Nationwide Mutual Fire Insurance Company v. Sharmin Christine Walls, et al.*, 2019 WL 2363539 (June 5, 2019). Read more here.

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