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Demystifying Procedural Conditions in Insurance Policies

October 30, 2025

Presented by

Shaun Crosner and Christopher Pasich

Policy Conditions – An Overview

- Conditions can impose procedural obligations on the insured.
  - May be viewed as a condition precedent to recovery under the policy.

- Conditions typically are found in a section labeled "Conditions," but they also can appear in other sections.
  - Conditions can appear in endorsements as well.

- Strict compliance is best, but substantial compliance may suffice

- Compliance can be excused in various circumstances
  - Waiver by the insurer
  - Estoppel
  - Lack of prejudice

Common Policy Conditions

- Conditions in First-Party Policies
  - Notice
  - Examinations Under Oath
  - Proof of Loss
  - Suit Limitations and Forum Selection Clauses

- Conditions in Third-Party Coverage
  - Notice and reporting of claims
  - Assistance & Cooperation
  - Consent Conditions
  - Suit Limitations and Forum Selection Clauses

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The Insurer's Burden of Proof

- Conditions are viewed as limitations on coverage
  - Insurers must draft clearly and place conspicuously
  - Ambiguities generally are resolved against insurers

- Insurer typically bears burden to prove that insured failed to comply with condition
  - Insurer generally must also establish that purported non-compliance resulted in "actual and substantial prejudice" to the insurer

- Burden of proof can vary in other jurisdictions
  - Burden-shifting states
  - Not all states require prejudice

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Notice Conditions in First-Party Policies

- Generally obligate the insured to advise the insurer upon discovering property damage or financial loss covered by policy
  - May require the insured to provide whatever details are known about the circumstances of the loss

- Notice generally provided by letter or e-mail
  - Details may be scant
  - Caution regarding unknowns
  - Importance of understanding coverage and limitations when providing notice

- Policy conditions often are silent on timing
  - However, some policies (e.g., cyber policies) require notice of certain types of losses within specified timeframe

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Notice Conditions in Third-Party Policies

- Often require notice of "claim" as soon as practicable, but may require notice within policy period or some other specified period of time after learning of "claim"
  - Specific deadlines in policies may require strict compliance, absent excuse

- Generally must provide copy of the "claim," without any need for elaboration

- Understanding the prejudice requirement
  - Applicability depends on type of policy
    - Claims-made-and-reported vs. other forms of liability coverage
  - Difficulty establishing actual and substantial prejudice
    - Must show that delay caused them to lose something essential to the defense

- Caution: Defense costs incurred prior to tender likely uncovered

Notice of Circumstance – Optional Reporting of "Claims"

- Condition found in many claims-made and claims-made-and-reported policies

- Allows insured to report a specific incident or situation that might lead to a future claim, even if a formal claim has not been made yet

B. Notice of Circumstance

As a condition precedent to their rights under this **Policy**, if during the **Policy Period** or the Extended Reporting Period that may apply, any **Insured** becomes aware of any fact, circumstance or situation which may reasonably be expected to give rise to a **Claim** being made against any **Insured** and shall give written notice to the **Insurer**, as soon as practicable (but prior to the expiration of or cancellation of this **Policy**), of:

1. the specific fact, circumstance or situation, with full details as to dates, persons, and entities involved; and
2. the injury or damages which may result therefrom; and
3. the circumstances by which the **Insured** first became aware thereof;

then any **Claim** subsequently made arising out of such fact, circumstance or situation shall be deemed to have been made when notice was first given to the **Insurer**.

- Consider reporting of potential claims towards end of policy period, particularly if changing insurers

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First-Party Policy Conditions: Proof of Loss

- Requires the submission of sworn statement attesting to the details of the loss
  - Some conditions require submission only if requested by insurer
  - Others may be interpreted to require submission even in absence of insurer request

- Insurers often provide form, which may not always give the insured the necessary latitude to elaborate

- Caution regarding insurer-prepared proofs of loss

- In California, delay or failure to provide certain information generally excuses performance only if insurer was actually and substantially prejudiced

- Extensions are commonly requested and almost always afforded

First-Party Policy Conditions: Examinations Under Oath

- Requires insured to appear for questioning under oath if requested by insurer
  - Not always requested
  - Examination requests may signal potential coverage dispute

- Similar to deposition, but without some of the formalities

- Questioning typically comes from insurer's outside counsel

- Witness generally permitted to be represented at examination, although other witnesses may not be permitted to attend

- Refusal to accommodate request may result in denial

- Request must be on reasonable terms

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Third-Party Policy Conditions: Assistance & Cooperation

- Requires cooperation by the insured in the conduct of the investigation, defense, or settlement of a claim

- Does not require waiver of privilege

- Insurers may attempt to expand scope, but condition generally requires very little of the insured
  - Cooperating throughout discovery
  - Providing defense counsel with authority to act
  - Accommodating document collection
  - Appearing for depositions, trial

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Third-Party Policy Conditions: Consent Conditions

- Rooted in insurer's right to participate in defense and settlement of claims

- Requires insured not to make admissions of liability or to settle a third-party claim without the insurer's prior approval

- May also require insured to obtain insurer's consent prior to incurring defense costs

- California courts have held that insurers need not establish prejudice to enforce consent conditions

- Insurer's unreasonable failure to provide consent may constitute bad faith

- Important for insureds to be mindful of consent conditions to avoid jeopardizing coverage

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Conditions Governing Suits Against Insurers

- May be found in first- and third-party policies

- May impose pre-suit mediation requirements

- May specify forums for dispute, as well as governing law

- Frequently purport to impose deadlines on filing suit
  - Often shorter than the governing statute of limitation
  - Deadlines typically will be enforced, depending on jurisdiction
  - Deadline may be tolled under certain circumstances
    - E.g., during pendency of underlying litigation or while insurer is investigating

- Insureds must be mindful to avoid losing right to pursue coverage
  - Tolling agreements

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Excuses for Non-Compliance: Waiver & Estoppel

- Waiver generally requires insurer's express statement excusing compliance

- Insurer's denial of coverage generally results in waiver of policy conditions
  - Insured retains right to pursue coverage and need not comply with conditions following denial

- Estoppel doctrine is equitable in nature
  - May be available when insurer's statements or conduct led insured to believe strict compliance was unnecessary
  - Insurer's failure to advise of policy conditions may support application of estoppel doctrine

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Policy Conditions: Key Takeaways

- Ambiguities in conditions generally will be construed against insurers

- Strive to comply, but understand that strict compliance may not be required
  - Substantial compliance may suffice
  - Waiver and/or estoppel may excuse compliance

- Invoke the prejudice rule when applicable

- Carefully scrutinize any adverse coverage positions based on supposed non-compliance with policy conditions

Questions?

Shaun H. Crosner

Co-Lead | Partner

scrosner@mcguirewoods.com

Los Angeles

Christopher Pasich

Partner

cpasich@mcguirewoods.com

Los Angeles

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