"Based On"… What Exactly? NJ Appellate Division Examines Phrase and Estops Insurer From Disclaiming Coverage for 20-Month Delay

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On May 28, 2019, the New Jersey Superior Court, Appellate Division examined the phrase "based on" in an assault-and-battery exclusion, finding that the phrase means "to make, form, or serve as the foundation of any claim, demand or suit." *C.M.S. Investment Ventures, Inc. v. American European Insurance Company*, No. A-2056-17T3, 2019 N.J. Super. Unpub. LEXIS 1215, at *8-9 (N.J. Super. Ct. App. Div. May 28, 2019) *(CMS)*. The *CMS* case is also notable because the Appellate Division held that a 20-month delay in disclaiming coverage was unreasonable and therefore warranted estoppel.

In *CMS*, the insured was allegedly warned by its tenant about a faulty ground-floor window that failed to lock properly. Afterward, an intruder broke into the tenant's apartment and sexually assaulted the tenant, who sued the insured on a premises liability claim. Before she filed suit, the tenant sought payment from the insured's CGL insurer directly. The insurer denied coverage based on the assault-and-battery exclusion and closed the file, but never informed the insured. Later, the tenant sued the insured, which sought a defense and indemnity from its insurer, which again denied coverage based on the exclusion. The insured then sought a declaration of coverage on grounds that the exclusion was ambiguous, and the insurer "was estopped from denying coverage, because it waited [20] months to inform CMS of its coverage decision." The trial court ruled in the insured's favor which led to the appeal in *CMS*.

The Appellate Division in *CMS* concluded that the assault-and-battery exclusion, which used the phrase "based on," "applies to claims, demands or suits where 'Assault and Battery' **forms or serves as the claim's foundation**." However, the court noted that New Jersey case law suggests that "an injury can have several proximate causes, and when one cause is excluded under the policy, **it does not necessarily mean all causes of the injury are excluded**." Thus, because the insured's tenant's claim was not "based ***only*** on the sexual assault," and instead sounded in premises liability, the assault-and-battery exclusion did not apply to preclude coverage. Notably, the Appellate Division stated that exclusions using the phrase "arising out of," instead of "based on," may "increase[ ] the type of claims subject to the exclusion."

Notwithstanding its finding of coverage, the Appellate Division in *CMS* also held that the CGL insurer was "**estopped** from denying coverage" because it **waited 20 months to disclaim coverage** after it received notice of the tenant's claim against the insured. According to the Appellate Division, an insurer is under a "duty to promptly inform its insured of its intention to disclaim coverage or of the possibility that coverage will be denied or question," once the insurer "has had a reasonable opportunity to investigate, or has learned of grounds for questioning coverage." Prejudice will be presumed, the court added, where "there has been a long lapse of time without any indication by the . . . carrier of a loss or rejection of coverage, during which the insured justifiably expects to be protected by the carrier." In *CMS*, the court concluded the insurer had enough time to investigate, and, because the insurer closed the file without notifying the insured, the insured was under the impression the claim had been resolved when it was not. The insured was "entitled to, but did not receive, fair warning [insurer] intended to disclaim coverage," the court concluded. The *CMS* case demonstrates the importance of a timely and adequate disclaimer.

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