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Fortress Re, Inc. v. Central National Insurance Co.: Application of the *Tate* Test to Notice Requirements in Reinsurance Contracts

Provisions requiring the insured to give the insurer prompt notice of the occurrence of an insured event are common in insurance contracts.[1] Because most insurance contracts also contain clauses requiring the insurer to defend claims brought against the insured,[2] the purpose of notice provisions is to give the insurer an opportunity to conduct a timely investigation so it may adequately defend these claims.[3] Most jurisdictions traditionally have taken a strict construction approach in breach of notice provision cases, absolving the insurer of liability under the contract if the notice requirement was not met.[4] In recent years, however, some courts have abandoned the strict construction approach in favor of the rule that for the insurer to escape its contractual obligations not only does the insured have to breach the notice provision, but this breach also must prejudice the insurer by actually frustrating its ability to adequately investigate and defend the claim.[5] This Note analyzes the recent decision of *Fortress Re, Inc. v. Central National Insurance Co.*[6] in which the United States District Court for the Eastern District of North Carolina applied this new "prejudice test" to a reinsurance contract. Also, this Note discusses the unsuitability of the prejudice test in the reinsurance context and proposes a new standard to be used in evaluating notice requirements in reinsurance contracts.

Until 1981 North Carolina courts followed the strict construction approach in their treatment of notice requirements in insurance policies.[7] This approach stemmed from the belief that because the terms of the insurance contract, including the notice requirements, were agreed upon by the parties, courts should not interfere with these terms.[8] Thus the courts had only one duty in interpreting insurance contracts: to ascertain and uphold the intent of the parties, always

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1. *See* 8 J. APPLEMAN, INSURANCE LAW AND PRACTICE § 4731, at 2 (1981); 13A G. COUCH, COUCH CYCLOPEDIA OF INSURANCE LAW § 49:2, at 227 (2d ed. 1982); Note, *Great American Insurance Co. v. C.G. Tate Construction Co.: Interpretation of Notice Provisions in Insurance Contracts*, 61 N.C.L. REV. 167, 167 (1982).

2. 7C J. APPLEMAN, *supra* note 1, § 4682, at 16; 14 G. COUCH, *supra* note 1, § 51:35, at 438.

3. 7C J. APPLEMAN, *supra* note 1, § 4681, at 2; 13A G. COUCH, *supra* note 1, § 49:2, at 227.

4. 8 J. APPLEMAN, *supra* note 1, § 4732, at 10-13; 13A G. COUCH, *supra* note 1, § 49:50, at 278. The notice provision often is phrased in terms of a condition precedent: if notice is late, the insurer is relieved of liability under the policy. Professors Appleman and Couch also note that even if policies do not specify that notice is a condition precedent, courts often interpret policies as if they did.

5. 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, 266-72 (1970); *see, e.g.*, Cooper v. Government Employees Ins. Co., 51 N.J. 86, 237 A.2d 870 (1968); Brakeman v. Potomac Ins. Co., 472 Pa. 66, 371 A.2d 193 (1977); Pickering v. American Employers Ins. Co., 109 R.I. 143, 282 A.2d 584 (1971).

6. 595 F. Supp. 334 (E.D.N.C. 1983).

7. *See, e.g.*, Fleming v. Nationwide Mut. Ins. Co., 261 N.C. 303, 134 S.E.2d 614 (1964); Muncie v. Travelers Ins. Co., 253 N.C. 74, 116 S.E.2d 474 (1960); Peeler v. United States Casualty Co., 197 N.C. 286, 148 S.E. 261 (1929).

8. Wachovia Bank & Trust Co. v. Westchester Fire Ins. Co., 276 N.C. 348, 354, 172 S.E.2d 518, 522 (1970).

giving effect to the clear and unambiguous meaning of the terms of the contract.[9] Therefore, if the contract called for notice to be given "immediately"[10] or "as soon as practicable,"[11] any unreasonable delay[12] abrogated the insurer's liability under the policy, regardless of whether the insurer's ability to defend the claim would have been aided by timely notice.

In 1981, however, the North Carolina Supreme Court in *Great American Insurance Co. v. C. G. Tate Construction Co.*[13] overruled previous cases espousing the strict construction approach.[14] The court adopted a three-part test for determining whether the insurer should be relieved of its contractual obligations because of the insured's failure to comply with notice requirements.[15] First, a court must determine whether notice was in fact given as soon as practicable.[16] Second, if notice was not given in a timely manner, the insured must show that there was a good faith reason for the delay. Last, if the good faith standard is met, the burden shifts to the insurer to show that its ability to investigate and defend the claim was prejudiced by the delay. The court emphasized the prejudice component of the test, stating that the failure of an insured to give prompt notice pursuant to an insurance contract provision does not relieve the insurer's liability under the contract "unless the delay operates materially to prejudice the ability of the insurer to investigate and defend."[17]

The prejudice test adopted in *Tate* is consistent with the modern trend away from strict construction of notice provisions in insurance contracts.[18] The basis for the test lies in the courts' perception of the relationship between the parties to an insurance contract. Courts adopting this test have noted that an insurance contract is not usually the result of an arm's length bargaining process, but is an adhesion contract[19] issued by an insurer on a take-it-or-leave-it

9. *Id*; *see also* Duke v. Mutual Life Ins. Co., 286 N.C. 244, 247, 210 S.E.2d 187, 189 (1974) ("The intention of the parties is the controlling guide to [the] interpretation [of the insurance contract].").

10. *See, e.g.*, Mewborn v. Employers' Liab. Assur. Co., 198 N.C. 156, 150 S.E. 887 (1929).

11. *See, e.g.*, Fleming v. Nationwide Mut. Ins. Co., 261 N.C. 303, 134 S.E.2d 614 (1964); Muncie v. Travelers Ins. Co., 253 N.C. 74, 116 S.E.2d 474 (1960); Peeler v. United States Casualty Co., 197 N.C. 286, 148 S.E. 261 (1929).

12. North Carolina courts have never required that immediate notice be given; rather they have construed notice provisions to require that notice be given in a reasonable time considering the facts and circumstances of the particular situation. *See* Harris v. Nationwide Mut. Ins. Co., 261 N.C. 499, 135 S.E.2d 209 (1964); Mewborn v. Employers' Liab. Assur. Co., 198 N.C. 156, 150 S.E. 887 (1929); *see also* Ball v. Employers' Liab. Assur. Corp., 206 N.C. 90, 172 S.E. 878 (1934) (delay in giving notice due to inability to discern injury held excusable and not violative of notice requirement); Rhyne v. Jefferson Standard Life Ins. Co., 196 N.C 717, 147 S.E. 6 (1929) (delay in giving notice due to insured's incapacitation held excusable).

13. 303 N.C. 387, 279 S.E.2d 769 (1981).

14. *Tate*, 303 N.C. at 396, 279 S.E.2d at 774 ("[W]e hereby overrule the *Peeler-Muncie-Fleming* line of cases . . . ."). *See supra* note 7 and accompanying text.

15. *Id.* at 399, 279 S.E.2d at 776. For a thorough discussion of the *Tate* decision, see Note, *supra* note 1, at 168-73.

16. This initial prong of the *Tate* test ends the inquiry for courts adhering to the strict construction approach. *See* Comment, *supra* note 5, at 264.

17. *Tate*, 303 N.C. at 396, 279 S.E.2d at 774.

18. *See supra* note 5 and accompanying text.

19. An adhesion contract is a contract in which the terms are dictated largely by one party, rather than resulting from negotiation. *See infra* note 43 and accompanying text.

basis.[20] Thus, the danger exists that insurers may take advantage of their superior bargaining position to include provisions that heavily favor themselves. Notice requirements are such provisions, inasmuch as failure to comply relieves the insurer of liability and compliance with the provision affords no additional protection to the insured, but simply maintains the existing policy coverage.

In jurisdictions that have abandoned the strict construction approach, prejudice against the insurer determines whether insurers remain liable when notice does not comply with the policy provisions.[21] Since the main purpose of a notice requirement is to afford the insurer the opportunity to adequately investigate and defend the claim, the test is whether the late notice in any way prejudices the insurer's ability to do so. If not, there is no reason for the insurer to escape liability. In most jurisdictions that have abandoned the strict construction approach, including North Carolina under the test set forth in *Tate*, the burden of proof is on the insurer to show that it was prejudiced by the delay.[22]

Tate and all previous North Carolina cases involving insurance contract notice provisions dealt with notice requirements in original insurance contracts. Recently, however, the United States District Court for the Eastern District of North Carolina applied the test adopted in *Tate* to a reinsurance contract.[23] In *Fortress Re, Inc. v. Central National Insurance Co.*,[24] the court held that the insurer's excessive delay in notifying the reinsurer of the claim had prejudiced the reinsurer. Therefore the reinsurer was relieved of its obligation to pay under the contract.[25] *Fortress Re*, the first case to apply the *Tate* test, extended the scope of *Tate* from original insurance contracts to reinsurance contracts. In so ruling, the court departed from previous federal court decisions, applying pre-*Tate* North Carolina law, that had applied the strict construction approach to reinsurance contracts.[26]

Reinsurance, as distinguished from original insurance, is a means of risk distribution whereby one insurer (the reinsured) contracts with another insurer (the reinsurer) for indemnity from all or a portion of the risk underwritten by the reinsured.[27] Even though reinsurance has been characterized as a separate

20. *See* State Farm Mut. Auto. Ins. Co. v. Milam, 438 F. Supp. 227 (S.D.W.Va. 1977); Cooper v. Government Employees Ins. Co., 51 N.J. 86, 237 A.2d 870 (1968); Brakeman v. Potomac Ins. Co., 472 Pa. 66, 371 A.2d 193 (1977); *see also* Note, *supra* note 1, at 171 ("[A]lmost all of the decisions [adopting a prejudice test] have been based on the adhesion contract rationale."). For a general discussion of the rationale behind courts' adoption of the prejudice test, see Comment, *supra* note 5, at 266-72.

21. *See* 8 J. APPLEMAN, *supra* note 1, § 4732, at 26-31; 13A G. COUCH, *supra* note 1, § 49:10, at 234.

22. *See* Note, *supra* note 1, at 172-73.

23. For a discussion of the distinction between original insurance contracts and reinsurance contracts, see *infra* notes § 27-30 and accompanying text.

24. 595 F. Supp. 334 (E.D.N.C. 1983).

25. *Id.* at 340.

26. *See* Fortress Re, Inc. v. Jefferson Ins. Co. of New York, 465 F. Supp. 333 (E.D.N.C. 1978), *aff'd*, 628 F.2d 860 (4th Cir. 1980). "Generally the rules which govern the construction of contracts and original policies of insurance are applicable to reinsurance contracts." *Id.* at 338 (quoting 13A J. APPLEMAN, *supra* note 1, § 7686, at 500).

27. Shulman, *Reinsurance: A Primer for the Practitioner*, L.A. LAW, Oct. 1980 at 34; *see also* 13A J. APPLEMAN, *supra* note 1, § 7681, at 480; 19 G. COUCH, *supra* note 1, § 80:1, at 624.

class of insurance,[28] contracts of reinsurance are governed by the same rules applicable to other insurance contracts.[29] Thus, even though most cases concerning notice requirements have involved original insurance policies, the same rules and terms are used in cases concerning reinsurance contracts.[30]

The controversy in *Fortress Re* arose out of a reinsurance contract executed by the parties in 1975.[31] In September 1978 the insurer was notified of a claim filed against its insured, a swimming pool manufacturer, for injuries sustained by an individual while diving into one of the insured's pools.[32] Because of the reinsurer's obligation under the contract to reimburse the insurer in the event of liability under the insurer's policy, it appeared likely that the claim would involve the reinsurer. Shortly after receiving notification of the claim, the insurer assigned the case to counsel. Upon investigation, counsel determined that "the claim was a serious one and excess carriers should certainly be notified."[33] In April 1980 counsel again advised the insurer of the seriousness of the claim.[34] On at least two occasions the insurer's internal memoranda indicated that it was aware of the need to notify the reinsurers.[35] Throughout this period, the insurer sought to reach a settlement agreement with the accident victim.[36]

The insurer finally notified the reinsurer, Fortress Re, of the suit on January 6, 1982, over three years after the claim arose.[37] Trial was set for January 12, which was only three working days following the initial notice. The insurer invited Fortress Re to attend a conference with the trial defense counsel on the eve of the trial.[38] Fortress Re did not attend this meeting, at which the claim was settled for $923,605.[39] Fortress Re then instituted a declaratory judgment action to obtain a declaration of its rights and obligations under the contract, alleging that the insurer had breached the notice requirement,[40] thereby absolv-

28. 19 G. COUCH, *supra* note 1, § 80:2, at 624.

29. 13A J. APPLEMAN, *supra* note 1, § 7686, at 500; 19 G. COUCH, *supra* note 1, § 80:1, at 623.

30. *E.g.*, Fortress Re, Inc. v. Jefferson Ins. Co. of New York, 465 F. Supp. 333 (E.D.N.C. 1978), *aff'd*, 628 F.2d 860 (4th Cir. 1980); Security Mut. Casualty Co. V. Century Casualty Co., 531 F.2d 974 (10th Cir.), *cert. denied*, 429 U.S. 860 (1976); Highlands Ins. Co. v. Employers Surplus Lines Ins. Co., 497 F. Supp. 169 (E.D. La. 1980); Stuyvesant Ins. Co. v. United Public Ins. Co., 139 Ind. App. 533, 221 N.E.2d 358 (1966).

31. Under the contract, the reinsurer was to reinsure one-half of the insurer's liability over $250,000 under a products liability insurance policy issued to a swimming pool manufacturer. The upper limit of the liability policy was $1,000,000. *Fortress Re*, 595 F. Supp. at 336 & n.1.

32. *Id.* at 336.

33. *Id.*

34. *Id.*

35. Internal memoranda indicating an awareness of this need were dated November 1980 and July 1981. The 1981 memorandum read, in part: " 'They [the reinsurers] must be put on notice . . . and get notice out to the facultative reinsurers.' " *Id.*

36. *Id.* at 337.

37. *Id.*

38. The correspondence extending the invitation read: " 'Consider this your invitation to attend [the trial]. We will be meeting with defense counsel . . . in New Jersey on Sunday evening [January 11].' " *Id.* at 337 (quoting Letter from Central National Insurance Co. to Fortress Re, Inc. (Jan. 6, 1982)).

39. *Id.* at 337.

40. The notice provision in the reinsurance contract read:

> Prompt notice shall be given to the Reinsurer by the Company of any occurrence or accident which appears likely to involve this reinsurance and while the Reinsurer does not

ing the reinsurer of liability under the reinsurance contract.

After noting that North Carolina law applied to the case,[41] the United States District Court for the Eastern District of North Carolina turned to the substantive issue raised—whether the reinsurer was relieved of liability because of the reinsured's violation of the notice requirement. The court assumed without discussion that *Tate* controlled the outcome of the case.[42] *Fortress Re*, however, is distinguishable from *Tate*, which dealt with a notice requirement in an original insurance contract. The considerations that led the court in *Tate* to adopt the prejudice test do not apply with equal force to a reinsurance contract. Prior federal cases interpreting North Carolina law that dealt with notice requirements in reinsurance contracts had applied a rule of strict construction. Even though courts in reinsurance cases generally apply rules applicable to insurance policies and other contracts, it is arguable that the *Tate* test should not be applied in the reinsurance context. One of the principal bases for the court's decision in *Tate* was the belief that the "terms of an insurance contract are not bargained for in the traditional sense"; rather, they are "offered on a take-it-or-leave-it basis" with the insured having little, if any, input.[43] This same belief pervades decisions in other jurisdictions adopting a prejudice test.[44] In cases arising out of original insurance contracts, some courts see a necessity to protect insureds from potentially unfair insurance contracts since insureds have no control over the terms of their contracts. Reinsurance contracts, however, typically are negotiated by the parties.[45] Thus, the need for protection of the insured does not exist in a reinsurance context. The parties to the contract presumably are aware of the law relating to insurance and reinsurance contracts, including the importance of prompt notice.[46] Accordingly, it would be reasonable to apply a stricter standard of compliance with the notice requirement to a reinsured than to an insured under an original insurance contract.[47]

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undertake to investigate or defend claims or suits it shall nevertheless have the right and be given the opportunity to associate with the Company and its representatives at the Reinsurer's expense in the defense and control of any claim, suit or proceeding involving this reinsurance, with the full cooperation of the Company.

Id. at 337 n.4.

41. *Id.* at 337.

42. *Id.* at 337-38.

43. *Tate*, 303 N.C. at 395, 279 S.E.2d at 774.

44. *See, e.g.*, Cooper v. Government Employees Ins. Co., 51 N.J. 86, 93, 237 A.2d 870, 873 (1968) ("[T]he terms of an insurance policy are not talked out or bargained for as in the case of contracts generally."); Brakeman v. Potomac Ins. Co., 472 Pa. 66, 72, 371 A.2d 193, 196 (1977) ("An insurance contract is not a negotiated agreement; rather its conditions are by and large dictated by the insurance company to the insured."); Pickering v. American Employers Ins. Co., 109 R.I. 143, 159, 282 A.2d 584, 593 (1971) ("An insurance contract is not the end result of the give-and-take that goes on at a bargaining table."). The *Tate* court relied on all three of these cases. *Tate*, 303 N.C. at 394-95, 279 S.E.2d at 773-74.

45. *See* Shulman, *supra* note 27, at 35. For example, the contract in *Fortress Re* was negotiated between the parties. *Fortress Re*, 595 F. Supp. at 336.

46. Because both parties are insurance companies, it is reasonable to expect them to have knowledge of the law surrounding the interpretation of insurance contracts, including reinsurance contracts.

47. This idea has been applied in cases and endorsed by commentators. *See, e.g.*, Stuyvesant Ins. Co. v. United Public Ins. Co., 139 Ind. App. 533, 543, 221 N.E.2d 358, 360 (1966) (compared to individual insureds, insurance company held to a stricter standard of reasonable time to notify rein-

The court correctly decided under the first part of the test that the reinsured in fact had failed to give prompt notice of the claim to the reinsurer.[48] Under the second prong of the *Tate* test, the court held that the reinsured failed to meet its burden of proof that it had acted in good faith in giving notice at such a late date. The reinsured contended that good faith may be shown by an "absence of motive or specific intent not to notify the insurer."[49] The court rejected this contention, concluding that "[a] bad motive or specific intent is not required" for a showing of bad faith.[50] The court noted that even though the reinsured was aware of the necessity for notifying the reinsurers, it failed to do so until just before trial. The court also held that the delinquency of notice had prejudiced the reinsurer in its "ability to participate in the defense and control of the claim and its evaluation for settlement purposes."[51] The reinsured's conduct was "so lacking in reasonableness and fair dealing that it amount[ed] to a lack of good faith as a matter of law."[52] The court therefore granted the reinsurer's motion for summary judgment.[53]

The court was justified in reaching this conclusion. Under North Carolina law each party to a contract is "required to act in good faith and to make reasonable efforts to perform his obligations under the agreement."[54] This principle has been applied to contracts between business entities as well as to contracts between individuals.[55] It also has been held that good faith means more than an honest intention to act fairly; it includes an absence of knowledge of any information that would cause the action to be unfair.[56] Thus, as the court in *Fortress Re* concluded, "where two business entities deal at arms length, unreasonable or unfair dealings can amount to a lack of good faith."[57]

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surer of claim of loss due to its superior knowledge); 19 G. COUCH, *supra* note 1, § 80:71, at 681 ("Being an insurance company, the reinsured is held to a high degree of compliance with policy provisions which require prompt notice to the reinsurer when a loss occurs which may potentially be within policy coverage.").

48. The reinsured "waited for over three years before notifying the [reinsurer] and then [gave notice] only on the eve of trial," even though it was aware shortly after it received notice of the claim that the reinsurance was likely to be involved. The reinsured also was advised by counsel to notify the reinsurers well in advance of the time it actually gave notification. *Fortress Re*, 595 F. Supp. at 338. Internal memoranda reflected the reinsured's acknowledgement of its duty to give notification. *Id.*; *see also supra* notes 33-37 and accompanying text.

49. *Fortress Re*, 595 F. Supp. at 338.

50. *Id.* The court noted that the court in *Tate* had cited lack of knowledge that a claim had been filed as an example of good faith. *Tate*, 303 N.C. at 339, 279 S.E.2d at 776. Since in *Fortress Re* the reinsurer was aware of the claim for over three years before it gave notice, the court in *Fortress Re* must have concluded from the *Tate* example that actual notice of a claim followed by a delay in notifying the insurer/reinsurer amounted to a lack of good faith.

51. *Fortress Re*, 595 F. Supp. at 339.

52. *Id.*

53. *Id.* at 336.

54. Weyerhaeuser Co. v. Godwin Bldg. Supply Co., Inc., 40 N.C. App. 743, 746, 253 S.E.2d 625, 627 (1979); *see also* United Roasters, Inc. v. Colgate-Palmolive Co., 649 F.2d 985, 990 (4th Cir. 1981) ("North Carolina law does require that parties perform their contractual obligations in good faith.").

55. *See, e.g.*, United Roasters, Inc. v. Colgate-Palmolive Co., 485 F. Supp. 1049 (E.D.N.C. 1980), *aff'd*, 649 F.2d 985, 989-90 (4th Cir.), *cert. denied*, 454 U.S. 1054 (1981); Weyerhaeuser Co. v. Godwin Bldg. Supply Co., 40 N.C. App. 743, 746, 253 S.E.2d 625, 627-28 (1979).

56. *See* Jaudon v. Swink, 51 N.C. App. 433, 435, 276 S.E.2d 511, 513 (1981).

57. *Fortress Re*, 595 F. Supp. at 339.

The principal issue raised by *Fortress Re* is the application of the prejudice component of the *Tate* test to a delayed notice situation involving a reinsurance contract. Using the *Tate* test, the court in *Fortress Re* found that the reinsured acted in bad faith; and as a result, the reinsurer was relieved of its obligations under the contract. There was, therefore, no need to discuss prejudice since under the *Tate* test it is only when the good faith test is met that the issue of prejudice even arises.[58] Nevertheless, the court in *Fortress Re* addressed the prejudice issue. Noting the distinction between insurance and reinsurance, the court looked to the purpose of the notice requirement in a reinsurance contract to determine whether the reinsurer had been prejudiced by delayed notice. The court decided that the underlying purpose of notice requirements in both insurance and reinsurance contracts is to protect the bargain of the parties.[59] It then defined prejudice as "the irretrievable loss of the bargain."[60] Prejudice occurred in *Fortress Re* when the reinsured lost what it had bargained for—"the ability to participate in the defense and control of the claim and its evaluation for settlement purposes."[61] Because the reinsurer was given notice only three working days before trial, the purpose of the notice requirement was frustrated. Thus, the court held as a matter of law that the reinsurer had been prejudiced by the reinsured's tardy notice.[62]

The *Tate* test places the burden to prove prejudice on the insurer.[63] The *Tate* court apparently intended the prejudice issue to be a question of fact, decided on a case-by-case basis.[64] Thus, it is curious that the court in *Fortress Re* held that the reinsurer was prejudiced as a matter of law. The court candidly recognized the lack of case law in North Carolina interpreting the prejudice requirement.[65] Without case law to develop a standard of prejudice, it seems anomalous that a court would find prejudice as a matter of law in any situation.

The facts in *Fortress Re* justify the court's holding; the reinsured substantially delayed giving notice to the reinsurer. If, however, a case with a less compelling fact situation arises, the application of the *Tate* test could thwart the intention of the parties, who are aware of their duties and who often have negotiated their contract. Therefore, a modified version of the *Tate* test should be applied in reinsurance cases. Courts should hold the reinsured to a high standard of good faith and require only a low degree of prejudice to the reinsurer.

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58. *Tate*, 303 N.C. at 399, 279 S.E.2d at 776.

59. Although it noted that the *Tate* court discussed prejudice in terms of the insurer's ability to defend the lawsuit, the *Fortress Re* court nevertheless declared that prejudice as defined in *Tate* did not apply in the reinsurance context. The *Tate* approach was intended "to protect the bargain of the parties." *Fortress Re*, 595 F. Supp. at 339. The court reasoned that the reinsurer had bargained for the opportunity to participate in the case and the notice requirement was designed to protect that bargain. *Id.*

60. *Id.*

61. *Id.*

62. *Id.* at 340.

63. *Tate*, 303 N.C. at 397-99, 279 S.E.2d at 775-76.

64. "Circumstances which may cause prejudice to an insurer are as varied and as numerous as the circumstances surrounding automobile accidents. A more complete discussion of prejudicial factors will have to await a case-by-case development." *Id.* at 399, 279 S.E.2d 776.

65. *Fortress Re*, 595 F. Supp. at 339.

Such a test would emphasize the obligation of the reinsured to perform its duty of prompt notice under a bargained-for reinsurance contract, while retaining the notion of prejudice in the event that the reinsured shows a legitimate justification for the delayed notice. Good faith under this test should be limited to situations in which the reinsured lacks actual knowledge of a claim and lacks any information that should give rise to knowledge of the claim and to situations in which delay is caused by factors beyond the reinsured's control. Even if the good faith test is met, however, the burden on the reinsurer of showing prejudice should be light. A reasonable showing that timely notice might have made a difference in the ultimate liability of the reinsurer should be enough to show prejudice.

The court in *Fortress Re* followed a recent innovation in North Carolina original insurance law and applied it in a different context—reinsurance law. The reinsurer in *Fortress Re* was relieved of liability because of a bad faith delay in notice to the reinsurer and the prejudice that resulted. The application of the *Tate* test to the facts of *Fortress Re* resulted in a correct decision that upheld the intention of the parties. It remains to be seen whether this same test can continue to uphold the intention of parties in future reinsurance actions. Since no North Carolina cases have addressed the issue of notice requirements in reinsurance contracts, it is not possible to determine whether North Carolina courts will follow the rationale of the federal district court in *Fortress Re*. North Carolina courts should not strictly apply the *Tate* test to notice provisions of reinsurance contracts. Instead, they should adopt a modified version of the *Tate* test, as described in this Note. Such a test would protect the reasonable expectations of both parties to a reinsurance contract.

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