LAW360

Portfolio Media. Inc. | 230 Park Avenue, 7th Floor | New York, NY 10169 | www.law360.com
Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

NY Insurance Ruling Reveals Limits Of Contra Proferentem

By **John Ewell and Joanna Roberto** (August 5, 2022, 5:35 PM EDT)

John Ewell

Joanna Roberto

One can argue that status has never been the most appropriate means of judgment. However, most recently, at least one court has announced that status represents a triggering factor for considering the entirety.

The general contract rule, which applies to insurance law as well, is that ambiguities in a policy are generally construed in favor of the policyholder.[1] Yet, as with most things in life and law, there are exceptions to this rule, such as where a policyholder is a sophisticated entity, when the insurance policy was meaningfully negotiated, or when the policy results in the issuance of nonstandard forms due to negotiations between insurer and policyholder.[2]

The rule of contra proferentem generally provides that where an insurer drafts a policy, any ambiguity in the policy should be resolved in favor of the insured.[3] This principle becomes most prominent in insurance law when exclusions are narrowly construed against the insurer and forgivingly construed in favor of the policyholder.

Typically, if there is a coverage dispute and the interpretation of a policy provision becomes the source of the disagreement, the use of extrinsic evidence will be ripe for consideration. Contra proferentem is typically applied by the fact-finder as it considers extrinsic evidence bearing on the contract's meaning, not by the court as a matter of law.[4]

A party will want to resort to extrinsic evidence to establish a lack of ambiguity or to explain justification. If the extrinsic evidence does not yield a conclusive answer as to the parties' intent, a court may apply other rules of contract construction.

With this principle in mind, the Supreme Court of the State of New York, County of New York, recently held in Brooklyn Union Gas Co. v. Century Indemnity Co. that there is no need to construe an ambiguous policy against an insurer and in favor of a policyholder if there is evidence that the policyholder is a sophisticated company.[5]

The Brooklyn Gas decision lends itself to the obvious probing query such as what factors must be considered when determining whether a policyholder is in fact a sophisticated company.

In that case, one of the many issues litigated was how the defendant's per-occurrence limits should be applied to the covered losses. Brooklyn Union contended that because the policies were consecutively renewed, the renewal reset the policies' per-occurrence limits annually. Century countered that the policies each had one multiyear term, rather than a one-year term renewed annually several times, and therefore, the policies' per-occurrence limit applied once over the full multiyear term.

In furtherance of this argument, the plaintiff argued the contra proferentem doctrine requires resolution of the per-occurrence-limits ambiguity in Brooklyn Union's favor while Century contended the issue of the applicability of contra proferentem should not apply because Brooklyn Union is a sophisticated policyholder that maintained a large self-insured retention.

Summarized, the argument is that when a policyholder is sophisticated enough to negotiate a large self-insured retention, it signals the policyholder possesses more than just a fundamental understanding of insurance practice.

Eventually, the court held that contra proferentem does not apply in the circumstances of that action. While the result may not be particularly surprising in light of similar national case law, what's important is the court's two-prong probe, establishing that a policyholder's status and the existence of a large self-insured retention are dispositive factors.

Having a large self-insured retention is significant because it in effect renders the policyholder's status as a quasi-insurer. A larger retention is indicative of an entity with insurance experience that is, for example, prepared to fund and likely dedicate a risk management department to handle insurance-related matters.

Handling claims that fall under a large self-insured retention and even purchasing layers of excess coverage through the use of large corporate brokerage signals a sophisticated policyholder that has skill, knowledge and practice.[6]

Key also is whether there is true balance of bargaining power between the insurer and policyholder with regard to terms, scope of coverage and associated risk. When a policyholder retains some co-drafting responsibility, then contra proferentem would not apply as the policyholder is not placed in a take-it-or-leave-it position.[7] Though, the suggestion of such an inference alone is not enough. The majority of states require affidavits or deposition testimony to support the inference.[8]

At a minimum, courts cannot properly adjudicate the application of the doctrine without first weighing any evidence obtained through discovery on the construction of the disputed terms. To either support or overcome the application of the contra proferentem, experience and common sense are simply not enough to conclude that the parties had sufficient negotiation skills.

As the Appellate Court of Illinois, First District, First Division, stated in Baxter International Inc. v. American Guarantee and Liability Insurance Co. in 2006, "The anti-drafter rule is intended to aid the party with less bargaining power during the drafting process and is not appropriate where the parties are equally sophisticated."[9] Evidence of unequal bargaining comes in different forms such as gaps in coverage or uncommon limits in coverage.[10]

The construction of the ambiguous language should be addressed by applying the appropriate canons of contract law.

While construing an arguably ambiguous provision or term in favor of the policyholder is likely the least controversial alternative, contesting the application of contra proferentem is garnering more traction and dissension among courts. While the judicial trend seems to hint favoritism toward fairness and equity, it is no surprise that the doctrine of reasonable expectations remains controversial.

John Ewell and Joanna Roberto are partners at Gerber Ciano Kelly Brady LLP.

[1] PCVST-DIL LLC v. Lexington Ins. Co., 2016 NY Slip Op 31007(U), ¶ 14 (N.Y. Sup. Ct.).

[2] See Cummins, Inc. v Atl. Mut. Ins. Co., 56 AD3d 288, 290 (N.Y. App. Div. 2008).

[3] McCostis v. Home Ins. Co., 31 F.3d 110, 113 (2d Cir. 1994).

[4] See, e.g.,Pattern Instructions Kansas - Civil, Ch. 124.32 (Feb. 2016) ("When the terms of aninsurancepolicy. . . are susceptible of more than one meaning, thepolicyprovisions must be given the meaning which is most favorable to the policyholder.").

[5] Brooklyn Union Gas Co. v. Century Indem. Co., 2022 NY Slip Op 31514(U) (Sup. Ct.).

[6] Werner Indus., Inc. v. First State Ins. Co., 112 N.J. 30, 38 (1988) (declining to construe policy in favor of insured where the policy covered "commercial risks procured through a broker, and thus involved parties on both sides of the bargaining table who were sophisticated with regard to insurance").

[7] Northbrook Excess & Surplus Ins.Co. v. Proctor & Gamble Co., 924 F.2d 633 (7th Cir. 1991).

[8] See contra, Universal Cable Prods., LLC v. Atlantic Specialty Ins. Co., 929 F.3d 1143 (9th Cir. 2019).

[9] Baxter International, Inc. v. American Guarantee and Liability Ins. Co., 861 N.E.2d 263 (Ill. App. Ct. 2006). See also Templo Fuente v. National Union, 224 N.J. 189 (2016) (refusing to construe policy against insurer since policyholder had been a "particularly knowledgeable insured[]" and "much better able to deal with the insurers on an equal footing").

[10] Eley v. Boeing Co., 945 F.2d 276, 279-80 (9th Cir. 1991) ("althoughcontraproferentemis strictlyappliedin the interpretation ofinsurancecontracts, it isnotautomatically or universallyappliedto other contracts").
