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Public Policy and the Art of Drafting Conforming Insurance Policies

When thinking about an insurance policy, the term "art" may not spring to mind. However, given the importance of insurance, coupled with the numerous considerations underpinning policy language, artful drafting is essential. This is not say that policies should be considered works of art. Instead, it is meant to highlight the need to articulate coverages and limitations in a clear, unambiguous, and fair manner regardless of the type of policy at issue.

Insurers interpose conditions precedent to coverage to limit exposure in a variety of scenarios. For example, providing notice of potential claims within a specified period is one such condition precedent. Illinois courts routinely enforce valid notice provisions to negate coverage. Yet, insurers seeking to limit coverage must be mindful to conform with public policy codified in Illinois statutes. Failure to conform with public policy considerations can be a death knell to an otherwise straightforward provision.

This article touches on drafting requirements necessary to comply with Illinois law and public policy considerations, as established by a well-developed body of case law. Specifically, this article highlights the manner that courts evaluate actions of insurers and insurance producers to determine whether they pass muster.

Clarity and Ambiguity

The rules for construction of an insurance policy are well established. An insurance policy is a contract and is subject to the general rules governing contracted station. *Progressive Premier Ins. Co. v. Cannon*, 382 Ill. App. 3d 526 (3d Dist. 2008). A court's primary objectives in construing the language of an insurance policy are: "to ascertain and give effect to the intentions of the parties as expressed by the language of the policy," and to give the policy's words their plain and ordinary meaning. *Valley Forge Ins. Co. v. Swiderski Elec., Inc.*, 223 Ill. 2d 352, 362-363 (2006).

Where the policy is clear and unambiguous, the job is easy. Courts will apply clear, unambiguous provisions as written to exclude or limit available coverage. *Cent. Ill. Light Co. v. Home Ins. Co.*, 213 Ill. 2d 141, 153 (2004). If the words in the policy are susceptible to more than one reasonable interpretation, however, the court must consider them ambiguous and construe the language strictly against the insurer that drafted the policy and in favor of the insured. *Outboard Marine Corp. v. Liberty Mut. Ins. Co.*, 154 Ill. 2d 90, 108 (1992). This maxim exists because there is little or no bargaining involved in the insurance contracting process, the insurer has control of the drafting process, and the policy's purpose is to provide coverage to the insured. *Pekin Ins. Co. v. Equilon Enter. LLC*, 2012 IL App (1st) 111529, ¶ 19.

To be sure, a contract is not rendered ambiguous just because the parties disagree on its meaning. *Cent. Ill. Light*, 213 Ill. 2d at 153. Additionally, courts are cautious not to distort the language of an insurance policy to create an ambiguity where none exists. *Dixon Distrib. Co. v. Hanover Ins. Co.*, 161 Ill. 2d 433, 441 (1994). Further, failure to define a particular policy term does not render that term ambiguous, nor is it ambiguous simply because the parties can suggest creative possibilities for its meaning. *Smith v. Neumann*, 289 Ill. App. 3d 1056, 1064 (2d Dist. 1997).

Moreover, courts must assume that every provision within the insurance policy was intended to serve a purpose. *Founders Ins. Co. v. Munoz*, 237 Ill. 2d 424, 433 (2010). Accordingly, the court must look at the policy as a whole, instead of reading terms in isolation, to determine whether an ambiguity exists.

These principles are intended to provide a level playing field for insurers and insureds. Based upon the foregoing principles, it may seem that determining the applicability of various insurance provisions should be relatively cut and dried. Not so. As the supreme court has ruled, parties to a contract may agree to any terms they choose unless their agreement is contrary to public policy. *Sulser v. Country Mut. Ins. Co.*, 147 Ill. 2d 548, 559 (1992). As discussed below, public policy concerns often come into play when a court is deciding the fate of a particular claim.

Limiting Insurance Restrictions with Public Policy

Under Illinois law, generally, when an insurer attempts to place limits on provisions governed by statute, such as uninsured motorist provisions, the limitations must be construed in favor of the policyholder and strongly against the insurer. Public policy considerations underlying insurance contracts go beyond the simple contractual relationship between insurer and insured, and seek to afford protection to members of the public.

Illinois courts have long recognized these types of public policy considerations underlying automobile insurance contracts. In *Gothberg v. Nemerovski*, 58 Ill. App. 2d 372 (1st Dist. 1965), the appellate court noted that automobile insurance policies have unique "connotations extending to the general public above and beyond the private interests of the two contracting parties" and concluded that "[a]utomobile insurance . . . is no longer a private contract merely between two parties." *Gothberg,* 58 Ill. App. 2d at 386.

In light of the goal of protecting the general public in insurance matters, public policy considerations are not confined to the narrow scope of automobile policies. For example, Illinois courts recognize that an injured third party is deemed to have an interest in the adjudication of a coverage dispute between the insured and the insurance company. *Reagor v. Travelers Ins. Co.*, 92 Ill. App. 3d 99 (1st Dist. 1980). The *Reagor* court explained that "liability insurance abounds with public policy considerations" and, therefore, "injured members of the general public are beneficiaries of liability insurance policies." *Reagor,* 92 Ill. 2d at 102-103. Hence, those whose rights would be impacted by the resolution of an insurance coverage dispute in a declaratory action are generally deemed "necessary parties" to the action. *See* 735 ILCS 5/2-701, *Safeco Ins. Co. of Ill. v. Treinis*, 238 Ill. App. 3d 541 (1st Dist. 1992) (joinder may be excused if it is not feasible to join the party).

The courts' reasoning in *Gothberg* and *Reagor* has factored into recent cases that have seen courts attempt to clarify circumstances in which a duty is owed by insurance producers. In *Skaperdas v. Country Casualty Insurance Co.*, 2015 IL 117021, the Illinois Supreme Court held that a fiduciary or agency relationship between the insurance producer and the insured is not required to establish "a duty of ordinary care to all others to guard against injuries which naturally flow as a reasonably probable and foreseeable consequence of an act." *Skaperdas,* 2015 IL 117021, ¶ 25. Further, the *Skaperdas* court recognized that "such a duty does not depend upon contract, privity of interest or the proximity of relationship, but extends to remote and unknown persons." *Id*. Thus, if an insurance producer's action in choosing a policy creates a foreseeable risk of injury, the defendant has a duty to protect others from that injury. *Id*.

Following *Skaperdas*, the Northern District of Illinois held that the insurance producer for an ice hockey league owed a duty to exercise ordinary care towards a player who was injured during a league game. *Moje v. Federal Hockey League LLC*, 207 F. Supp. 3d 833 (N.D. Ill. 2016). The *Moje* court opined that an insurance producer's duty to supply adequate

liability coverage to the insured tortfeasor extended to the injured plaintiff because this case—involving a personal injury tort claim—bore "a closer relationship to the long line of Illinois cases placing a duty on an insurance producer in automobile accident cases." *Moje,* 207 F. Supp. 3d at 840.

In contrast, the Illinois Appellate Court, First District found no such parallel between business tort claims and automobile claims in *Central Mutual Insurance Co. v. Tracy's Treasures, Inc.*, 2014 IL App (1st) 123339. In *Tracy's Treasures*, the court found "no corresponding public policy requiring those who advertise their businesses through electronic transmissions to carry liability insurance to cover the possibility that those to whom the advertisements are transmitted have not consented to receive them." *Tracy's Treasures*, 2014 IL App (1st) 123339, ¶ 104. The *Tracy's Treasures* court did opine, however, that such reasoning "could also be extended to cases involving professions subject to mandatory insurance requirements, such as doctors or lawyers." *Id*.

Limiting Enforcement of Notice Provisions with Public Policy

Courts interpreting Illinois law have determined that a party must comply with conditions precedent to coverage to obtain coverage. If an insured fails to comply with a notice requirement, the insurer may deny coverage; prejudice to the insurer is not required. *Northbrook Prop. & Cas. Ins. Co. v. Applied Systems, Inc.*, 313 Ill. App. 3d 457, 464 (1st Dist. 2000) (see also *Allstate Ins. Co. v. Employers Reinsurance Corp.*, 441 F. Supp. 2d 865, 875 (N.D. Ill. 2005)). At first blush, this may appear to be unfairly one-sided in favor of the insurer. Yet, as many insurers have learned, application of the law to a particular provision is not as one-sided as it may appear.

In a recently decided case, the court in *Smith v. American Heartland Insurance Co.*, 2017 IL App (1st) 161144, considered a seemingly simple provision that required written notice within 120 days of an accident. There was no dispute that the insured failed to provide notice within the specified time frame. Additionally, the court agreed there was nothing ambiguous about the timing requirement because the notice provision clearly and unambiguously required notice within 120 days of the accident. *American Heartland,* 2017 Ill. App. (1st) 161144, ¶ 26. Moreover, the court likened the 120-day notice requirement to requirements in many policies mandating written notice "as soon as practicable," which was interpreted by courts to mean "within a reasonable time." *Id.*

Yet, instead of ruling in favor of the insurer based upon the claimant's admission that she failed to provide written notice within 120 days of the accident, the court continued its analysis. In deciding whether a provision within an insurance agreement violates public policy, the court advised that it "must determine whether the agreement is so capable of producing harm that its enforcement would be contrary to the public interest." *Id.* at ¶ 28 (citing *Phoenix Ins. Co. v. Rosen*, 242 Ill. 2d 48, 54 (2009)). Pursuant to Illinois law, violation of public policy depends on the particular facts and circumstances of the case. *Kleinwort Benson North America, Inc. v. Quantum Fin. Servs., Inc.*, 181 Ill. 2d 214, 226 (1998).

Applying the general rule requiring construing in favor of the insured any attempts to limit uninsured motorist provisions, the court rejected the American Heartland 120-day notice provision. *American Heartland*, 2017 IL App (1st) 161144, at ¶ 29. Although the 120-day provision in the policy limited the time within which notification of the claim must be made, the uninsured motorist statute does not state a limit regarding when an uninsured motorist claim may be brought. *See* 215 ILCS 5/143a (West 2014). Accordingly, the court relied on *Severs v. Country Mutual Insurance. Co.*, 2017 IL App (1st) 161144, in concluding that uninsured motorist statutes "cannot be circumvented by the insertion of a contrary or restricting provision in an insurance policy." *American Heartland* at ¶ 29 (citing *Severs v. Country Mut. Ins. Co.*, 89 Ill. 2d

515, 520 (1982)). The *American Heartland* court employed the same rationale used in numerous cases interpreting the Illinois uninsured motorist statute, wherein an insurer sought to dilute or diminish the intent of the legislature.

For example, in *Coronet Insurance Co. v. Ferrill*, 134 Ill. App. 3d 483, 484 (1st Dist. 1985), a provision in the auto policy required an insured to notify Coronet of an uninsured motorist claim within one year of the insolvency of the tortfeasor's insurer.. Coronet rejected the policyholder's uninsured motorist claim because the insured filed his claim more than one year after the tortfeasor's insurer was declared insolvent. *Ferrill*, 134 Ill. App. 3d at 485. The court held that the challenged one-year notice provision, as applied, "impermissibly limits the time within which the policyholder may assert the insolvency of his opponent's insurer to one year, whether the policyholder knows of it or not." *Id.* at 487. The court found application of the discovery rule would give full, fair, and reasonable effect to the policy terms as written. *Id.* at 488. Under this rule, the notice period requirement would not begin to run until the claimant knew or, reasonably should have known, of the insolvency of the other motorist's insurer. *Id.*

Similarly, courts have deemed one-year limitations periods for demanding arbitration violative of uninsured motorist claims. *Burgo v. Illinois Farmers Ins. Co.*, 8 Ill. App. 3d 259, 264 (1st Dist. 1972). In *Burgo*, the uninsured motorist provision required the policyholder to demand arbitration within one year of the date of the accident. The court held that if the practical effect of the one-year limitation provision was to deny the insured the contracted uninsured motorist coverage required by statute, then the provision is void and without effect. *Burgo*, 8 Ill. App. 3d at 263. The court found that, in this situation, the insured would be defeated by the one-year provision without having the opportunity to invoke the coverage he had been paying for, because the insured plaintiff had no way of knowing the tortfeasor defendant would become an uninsured motorist. *Id*.

Conversely, the Illinois Supreme Court has upheld two-year limitations periods for statutorily governed underinsured motorist claims. *Country Preferred Ins. Co. v. Whitehead,* 2012 IL 113365. In *Whitehead*, the Supreme Court ruled that the two-year period allowed the plaintiff "what our legislature has deemed a sufficient amount of time to ascertain the basis for, and dimensions of, her uninsured-motorist claim, and, if necessary, to take steps to initiate dispute resolution procedures." *Whitehead,* 2012 IL 113365, ¶ 39.

Conclusion

Illinois courts have made it clear that insurance policies of many types must adhere not only to statutes, but to fundamental considerations of public policy and fairness. Courts have consistently looked beyond the express language of policies to the public policy underpinning the policies. Effective, artful drafting of policy provisions must reflect an understanding of not only the governing statutes, but the public policy considerations at play.

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