CHAPTER 1

INTERPRETATION OF INSURANCE POLICIES

A policy of insurance is a contract entered into between the insured and the insurance company.[1] Thus, for the most part, the general rules of contract construction apply to the interpretation of insurance policies. Unlike traditional contracts, however, insurance policies are subject to specialized rules of interpretation.[2] In addition, insurance policies are subject to "special scrutiny" by courts. Courts apply such specialized rules and scrutiny because, given the perceived disparity in bargaining power between the insured and the insurance company, insurance policies are viewed as "contracts of adhesion."[3] These special rules and scrutiny apply to all types of insurance policies.[4] They also apply to both large, sophisticated commercial insureds as well as individual insureds as long as neither the insured nor its agent was involved in drafting the insurance policy.[5] As discussed below, the justification for applying strict scrutiny arguably does not apply when the insured is a sophisticated commercial entity represented by an insurance broker that is involved in the drafting of the policy. The New Jersey Supreme Court has cautioned, however, that these rules of construction should be used "sensibly"[6] and that a court should not

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[1] *Selective Ins. Co. of Am. v. Hudson E. Pain Mgmt. Osteopathic Med. & Physical Therapy*, 210 N.J. 597, 605 (2012).

[2] *Zacarias v. Allstate Ins. Co.*, 168 N.J. 590, 595 (2001); *see also Doto v. Russo*, 140 N.J. 544, 556 (1995) ("because of the unique nature of contracts of insurance, courts assume 'a particularly vigilant role in ensuring their conformity to public policy and principles of fairness'") (quoting *Voorhees v. Preferred Mut. Ins. Co.*, 128 N.J. 165, 175 (1992)).

[3] *Zacarias*, 168 N.J. at 594 ("We give special scrutiny to insurance contracts because of the stark imbalance between insurance companies and insureds in their respective understanding of the terms and conditions of insurance policies."); *Nav-Its, Inc. v. Selective Ins. Co. of Am.*, 183 N.J. 110, 118 (2005) ("Because of the complex terminology used in the policy and because the policy is in most cases prepared by the insurance company, we recognize that an insurance policy is a 'contract[] of adhesion between parties who are not equally situated.'") (quoting *Doto*, 140 N.J. at 556)); *Gibson v. Callaghan*, 158 N.J. 662, 669 (1999) ("Insurance policies are contracts of adhesion and, as such, are subject to special rules of interpretation."); *Meier v. N.J. Life Ins. Co.*, 101 N.J. 597, 611 (1986) ("while insurance policies are contractual in nature, they are not ordinary contracts but contracts of adhesion between parties who are not equally situated").

[4] *Wakefern Food Corp. v. Liberty Mut. Fire Ins. Co.*, 406 N.J. Super. 524, 539 (App. Div.) ("we have applied these general principles of construction to first-party insurance policies, including all-risk policies, as well as third-party liability policies"), *certif. denied*, 200 N.J. 209 (2009).

[5] *Id.* at 540 ("these principles apply to commercial entities as well as individual insureds, so long as the insured did not participate in drafting the insurance provision at issue"). In *Oxford Realty Group Cedar v. Travelers Excess & Surplus Lines Co.*, 229 N.J. 196, 208 (2017), the Court stated, albeit in *dicta*, that "[s]ophisticated commercial insureds . . . do not receive the benefit of having contractual ambiguities construed against the insurer." The Court went on to note that the doctrine of *contra proferentum* "is a consumer-protective doctrine" that does not apply to sophisticated parties. *Id.* The Court also noted that "the doctrine of reasonable expectations is less applicable to commercial contracts." *Id.* There was no evidence in that case that the insured participated in the drafting of the policy. *Id.* at 216 (Albin, J., dissenting).

[6] *Broadway Maint. Corp. v. Rutgers*, 90 N.J. 253, 271 (1982).

rewrite a contract of insurance to provide an insured with more coverage than it reasonably expected to purchase.[7]

Addressed below are some of the most common rules of interpretation that courts have developed.

A. THE PLAIN AND ORDINARY MEANING

As a general rule, the insured has the burden of establishing that its loss falls within the coverage provided by its policy.[8] In the absence of fraud or unconscionable conduct on the part of the insurance company, an insured is chargeable with knowledge of the terms and conditions of its policy, even if the insured has not read the policy prior to a loss.[9] Of course, there are certain exceptions to this rule. One such exception, which is discussed below, provides that changes to the coverage provided by certain type of policies on renewal will not be effective unless brought to the attention of the insured.[10] In construing an insurance policy, like other contracts, courts try to determine the common intent of the parties.[11] All rules of interpretation "must be subordinated to the common intent of the parties which governs."[12]

Courts first look to the insurance policy's language to determine the extent of coverage. In the absence of any ambiguity, the terms of an insurance policy will be interpreted in accordance with their "plain and ordinary meaning."[13] It is well established under New Jersey law that "[i]n the absence of any ambiguity, courts should not write for the insured a better policy of insurance

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[7] *Tomaiuoli v. U.S. Fid. & Guar. Co.*, 75 N.J. Super. 192, 207 (App. Div. 1962) (rules of construction "should not be used as an excuse to read into a private agreement that which is not there, and that which people dealing fairly with one another could not have intended"); *Werner Indus., Inc. v. First State Ins. Co.*, 112 N.J. 30, 39 (1988) (quoting *Tomaiuoli*).

[8] *Arthur Andersen LLP v. Fed. Ins. Co.*, 416 N.J. Super. 334, 347 (App. Div. 2010).

[9] *Merchants Indem. Corp. v. Eggleston*, 37 N.J. 114, 121 (1962) ("In general, an insured is chargeable with knowledge of the contents of a policy, in the absence of fraud or unconscionable conduct on the part of the carrier."); *Botti v. CNA Ins. Co.*, 361 N.J. Super. 217, 225 (App. Div. 2003) ("an insured is charged with knowledge of the contents of its policy, in the absence of fraud or unconscionable conduct on the part of the insurer").

[10] *See, e.g.*, *N.J.A.C.* 11:1-20.2.

[11] *S.T. Hudson Eng'rs, Inc. v. Pa. Nat'l Mut. Cas. Co.*, 388 N.J. Super. 592, 604 (App. Div. 2006) ("as with any contract, construing insurance policies requires a broad search 'for the probable common intent of the parties in an effort to find a reasonable meaning in keeping with the express general purposes of the policies'") (citation omitted), *certif. denied*, 189 N.J. 647 (2007).

[12] *McNeilab, Inc. v. N. River Ins. Co.*, 645 F. Supp. 525, 544 (D.N.J. 1986) ("If the intent of the parties is unclear from the contract, extrinsic evidence can be brought in to elucidate their intent.").

[13] *See Zacarias v. Allstate Ins. Co.*, 168 N.J. 590, 594 (2001); *President v. Jenkins*, 180 N.J. 550 (2004); ("When interpreting an insurance policy courts should give the policy's words 'their plain, ordinary meaning.'") (citation omitted); *Benjamin Moore & Co. v. Aetna Cas. & Sur. Co.*, 179 N.J. 87, 102 (2004) ("we are mindful . . . that the words of an insurance policy should be given their plain meaning"); *Newport Assocs. Dev. Co. v. Travelers Indem. Co.*, 162 F.3d 789 (3d Cir. 1998) ("Under New Jersey law, the words of an insurance contract should be given their everyday and common meaning.").

than the one purchased."[14] In fact, the New Jersey Supreme Court has cautioned against writing a better policy of insurance than the one purchased even where ambiguities exist.[15] Moreover, if at all possible, an insurance policy should be read in such a way that each term and provision is given meaning; no term or provision should be treated as superfluous or without effect.[16]

In the first instance, therefore, it is necessary to determine whether the particular policy language at issue is ambiguous. In determining whether an ambiguity exists, "a court must not 'torture' the language of a contract to create ambiguity where none exists."[17] Indeed, "[c]ourts are not afforded the luxury to change the language of the insurance policy to create ambiguity."[18] Moreover, it is well established that "an ambiguity does not arise simply because the parties have offered two conflicting interpretations."[19] Similarly, a policy "exclusion is not rendered ambiguous merely because the definitions appear on one page and the exclusions appear on another."[20] The question as to whether the language of an insurance policy is ambiguous is a

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[14] *Zacarias*, 168 N.J. at 595; *President*, 180 N.J. at 562 ("If the policy terms are clear, courts should interpret the policy as written and avoid writing a better insurance policy than the one purchased.").

[15] *Flomerfelt v. Cardiello*, 202 N.J. 432, 441 (2010) (citing *Walker Rogge, Inc. v. Chelsea Tile & Guar. Co.*, 116 N.J. 517, 529 (1989), *appeal after remand*, 254 N.J. Super. 380 (App. Div. 1992)).

[16] *Gunther v. Metro. Cas. Ins. Co.*, 33 N.J. Super. 101, 112 (Law Div. 1954) ("No part of any contract, particularly a policy prepared with the care with which this one was prepared, should be treated as useless unless it is indeed useless."); *Zurich Am. Ins. Co. v. Keating Bldg. Corp.*, 513 F. Supp. 2d 55, 64 (D.N.J. 2007) (rejecting the insurance company's proffered interpretation of the meaning of a policy term on the basis that it would render another term "superfluous, a result that is contrary to New Jersey law regarding interpretation of insurance policies"); *Sebro Packaging Corp. v. Liberty Mut. Fire Ins. Co.*, 69 F. Supp. 2d 642, 644 (D.N.J. 1999) (court rejected the insured's interpretation of the insurance policy on the basis that it would render certain language meaningless); *Pine Belt Auto., Inc. v. Royal Indem. Co.*, 2009 WL 1025564, *5 (D.N.J. Apr. 16, 2009) ("The Court finds that adopting [the insured's] proposal would violate a cardinal rule of contract construction – specifically, that a court must give effect to all contract provisions."), *aff'd*, 400 F. App'x 621 (3d Cir. 2010).

[17] *Pittston Co. Ultramar Am. Ltd. v. Allianz Ins. Co.*, 124 F.3d 508, 520 (3d Cir. 1997); *Longobardi v. Chubb Ins. Co.*, 121 N.J. 530, 537 (1990) ("the words of an insurance policy should be given their ordinary meaning, and in the absence of an ambiguity, a court should not engage in a strained construction to support the imposition of liability").

[18] *Rothschild v. Foremost Ins. Co.*, 653 F. Supp. 2d 526, 531 (D.N.J. 2009).

[19] *Polarome Int'l, Inc. v. Greenwich Ins. Co.*, 404 N.J. Super. 241, 259 (App. Div. 2008), *certif. denied*, 199 N.J. 133 (2009); *see also Simonetti v. Selective Ins. Co.*, 372 N.J. Super. 421, 429 (App. Div. 2004) ("an insurance policy is not ambiguous merely because two conflicting interpretations have been offered by the litigants"); *Rosario ex rel. Rosario v. Haywood*, 351 N.J. Super. 521, 530-31 (App. Div. 2002) (same); *Powell v. Alemaz, Inc.*, 335 N.J. Super. 33, 44 (App. Div. 2000) ("An insurance policy is not ambiguous merely because two conflicting interpretations of it are suggested by the litigants. Rather, both interpretations must reflect a reasonable reading of the contractual language.").

[20] *Weitz v. Allstate Ins. Co.*, 273 N.J. Super. 548, 551 (App. Div. 1994).