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PUNITIVE DAMAGES AND INSURANCE: ARE PUNITIVE
DAMAGES INSURABLE? THE NORTH DAKOTA SUPREME
COURT SAYS YES, DESPITE NORTH DAKOTA'S PUBLIC
POLICY TO THE CONTRARY*

Continental Casualty Co. v. Kinsey, 499 N.W.2d 574 (N.D. 1993)

I. INTRODUCTION

Robert Kinsey (Kinsey), an attorney, paid a premium to Continental Casualty Company (Continental), a professional liability insurer, for legal malpractice coverage.¹ Anita Bjorgen (Bjorgen) retained Kinsey to represent her in a divorce proceeding.² Bjorgen's husband was substantially indebted to First National Bank of Crosby (Bank), and the Bank had security interests in a considerable amount of the Bjorgens' property.³ Kinsey had a conflict of interest in his representation of Bjorgen because he was on the Bank's Board of Directors and owned stock in the Bank and its holding company.⁴ Kinsey's fraudulent representation of Bjorgen resulted in the assessment of compensatory and punitive damages against Kinsey and in favor of Bjorgen.⁵ Continental, alleging that its insurance policy provided no coverage for punitive damages, initiated a declaratory judgment action to determine the extent of its coverage.⁶

* This case comment is dedicated to Michael Alan DeMent whose walk in life was short but enjoyable to all who knew him. May he rest in peace. The author would like to thank William P. Harrie, Esq., for his assistance and guidance in preparing this Case Comment.

1. *Continental Casualty Co. v. Kinsey*, 499 N.W.2d 574, 576 (N.D. 1993) [hereinafter *Kinsey III*].

2. *Bjorgen v. Kinsey*, 466 N.W.2d 553, 555 (N.D. 1991) [hereinafter *Kinsey I*]. This case is the first in a series of four involving Kinsey. The second case, *Bjorgen v. Kinsey*, 491 N.W.2d 389 (N.D. 1992) [hereinafter *Kinsey II*], is beyond the scope of this Comment as it exclusively addresses the appointment of a receiver. See *infra* note 6 (discussing the history of *Kinsey III* and *Kinsey IV*).

3. *Kinsey I*, 466 N.W.2d at 555.

4. *Id.* at 554-55. Furthermore, Kinsey had previously provided legal services to the Bank and had performed a title opinion on the real property that Bjorgen's husband mortgaged to the Bank. *Id.*

5. *Id.* at 557. See *infra* notes 21-24 and accompanying text (addressing the amount of damages assessed against Kinsey).

6. *Kinsey III*, 499 N.W.2d at 576. Continental provided Kinsey with legal representation in Bjorgen's malpractice action with a reservation that the insurance policy would not provide coverage for any damages awarded to Bjorgen for fraudulent conduct. *Id.* Kinsey's professional insurance policy with Continental excluded coverage for any fraudulent conduct by the insured. *Id.* at 577. When Bjorgen was awarded damages for Kinsey's fraudulent conduct, Continental filed a declaratory judgment action. *Kinsey III*, 499 N.W.2d at 576. Kinsey counterclaimed, alleging that Continental failed to act fairly or in good faith in representing him. *Id.* The counterclaim was dismissed by the district court for failure to raise genuine issues of material fact. *Id.* The North Dakota Supreme Court remanded that decision for reconsideration, as the trial court's decision was based on its finding that Kinsey's insurance policy did not provide coverage for Bjorgen's judgment. *Id.* at 582. The North Dakota Supreme Court held that the policy did provide such coverage. *Id.* On remand, the trial court determined that Kinsey's counterclaim had no "genuine issue of material fact" and affirmed its earlier order of summary judgment. *Continental Casualty Co. v. Kinsey*, 513 N.W.2d 66, 68 (N.D. 1994) [hereinafter *Kinsey IV*]. The North Dakota Supreme Court affirmed the trial court's decision, concluding that "Kinsey ha[d] failed to raise a genuine issue of material fact that Continental breached a duty to Kinsey of good faith and fair dealing in defending Kinsey in the Bjorgen litigation." *Id.* at 70.

Kinsey's professional liability insurance with Continental had several exclusions. Specifically, one exclusion denied insurance coverage for "any dishonest, fraudulent, criminal or malicious act or omission of the insured or any partner, employee, officer or stockholder of the insured."⁷ Another exclusion denied insurance coverage for "punitive or exemplary damages or any fine, penalty or claim for return of fees."⁸ The policy also contained a special endorsement form which provided: "The Company agrees with the insured that the exclusion referring 'to any award of punitive damages' does not apply to this policy."⁹ The trial court focused on the policy exclusions and determined that Kinsey's insurance policy did not provide coverage for Bjorgen's judgment.¹⁰ However, the North Dakota Supreme Court focused on the special policy endorsement and held that the policy did provide coverage for the punitive damages awarded to Bjorgen.¹¹

The purpose of this Comment is to examine the approach the North Dakota Supreme Court utilized to approve insurance coverage of punitive damages and the significance of this decision on North Dakota public policy.

II. FACTUAL BACKGROUND

Kinsey's fraudulent representation of Bjorgen originated on June 17, 1983, when Kinsey prepared a proposed divorce settlement agreement for Bjorgen.¹² The day before Kinsey sent Bjorgen the proposed settlement agreement, he contacted the Bank's legal counsel suggesting that the Bank take legal action against Bjorgen's husband to collect on his promissory notes.¹³ On August 15, 1983, Bjorgen instructed Kinsey to discontinue the divorce action and to prepare a deed transferring all of the property to her.¹⁴ Bjorgen determined that if the divorce action was dismissed, the property could be transferred "without adverse tax conse-

7. *Kinsey III*, 499 N.W.2d at 577. This exclusion did not apply to any acts resulting in a malicious prosecution claim. *Id.*

8. *Id.*

9. *Id.* This exclusion was required by North Dakota Insurance Commissioner Byron Knutson; however, this special endorsement is no longer required. Telephone interview with employee of North Dakota Insurance Commission (Feb. 1994). The office of the North Dakota Insurance Commissioner does not maintain records regarding the policy endorsements it requires. *Id.*

10. *Id.* at 582.

11. *Id.*

12. *Kinsey I*, 466 N.W.2d at 555. The proposed property settlement agreement for Bjorgen designated certain real property which Bjorgen's husband was to convey to Bjorgen. *Id.* Under this agreement, Bjorgen was to receive the real property for which Kinsey previously had done the title opinion. *Id.* Bjorgen was also to receive 10,000 shares of the Bank's holding company stock which were owned by her husband. *Id.*

13. *Id.* These promissory notes were not due until December 15, 1983. *Id.* Kinsey did not inform Bjorgen of the Bank's pending action against her husband and continued to periodically contact the Bank's legal counsel to check the status of its claim against Bjorgen's husband. *Id.*

14. *Id.* at 555-56.

quences."¹⁵ Bjorgen then would obtain a divorce once the property was conveyed.¹⁶ Kinsey agreed to prepare the deed but did not advise Bjorgen that dismissal of the divorce action would also dismiss her *lis pendens* claim on the property and thereby leave her with no priority ownership protection on her and her husband's real property.¹⁷

On September 14, 1983, Kinsey sent a letter to Bjorgen informing her that he could not transfer the property from her husband because it had been attached by the Bank.¹⁸ Concerned that Bjorgen's *lis pendens* claim was still of record and would take precedence over the Bank's attachment, Kinsey dismissed Bjorgen's divorce case in November, 1983.¹⁹

On November 5, 1986, Bjorgen brought a legal malpractice action against Kinsey founded upon Kinsey's conflict of interest and demanded treble damages for attorney deceit.²⁰ The jury found that Kinsey breached his professional duty to Bjorgen and awarded her \$172,000 in compensatory damages.²¹ Furthermore, the jury found Kinsey guilty of fraud or malice and awarded Bjorgen \$100,000 in punitive damages.²² The trial court trebled the compensatory damages pursuant to the relevant statute regarding the misconduct of an attorney,²³ but disallowed the

15. *Id.* at 556.

16. *Id.*

17. *Kinsey I*, 466 N.W.2d at 556. Bjorgen would not be a priority creditor because the Bank's attachment of the Bjorgens' property would take precedence over any right Bjorgen had to the property through the divorce judgment. *Id.* Bjorgen requested the deed from Kinsey again on September 9, 1983. *Id.* On September 14th, the Bank notified Kinsey that it had obtained a writ of attachment on Bjorgens' real property. *Id.*

18. *Id.*

19. *Id.* In October, 1984, Bjorgen, not yet aware of Kinsey's fraudulent conduct, requested Kinsey to reinstate her divorce action. *Id.* Immediately following Bjorgen's divorce hearing on December 18, 1984, Kinsey informed Bjorgen that he owned a substantial interest in the Bank and requested that Bjorgen sign a quitclaim deed to the Bank. *Id.* The Bank's legal counsel had previously requested that Kinsey ask Bjorgen for a waiver of her right of redemption. *Id.*

20. *Id.* at 557. The North Dakota Century Code defines deceit as:

1. The suggestion as a fact of that which is not true by one who does not believe it to be true;
2. The assertion as a fact of that which is not true by one who has no reasonable ground for believing it to be true;
3. The suppression of a fact by one who is bound to disclose it, or who gives information of other facts which are likely to mislead for want of communication of that fact; or
4. A promise made without any intention of performing.

N.D. CENT. CODE § 9-10-02 (1987).

21. *Kinsey I*, 466 N.W.2d at 557.

22. *Id.*

23. N.D. CENT. CODE § 27-13-08 (1991).

Every attorney who:

1. Is guilty of any deceit or collusion or consents to any deceit or collusion with intent to deceive the court or any party;
2. Willfully delays his client's suit with a view to his own gain; or
3. Willfully receives any money or other property for or on account of any money or debt which he has not laid out or become answerable for, is guilty of a class A misdemeanor and in addition forfeits to the party injured treble damages to be recovered in a civil action.

punitive damage award, holding that the allowance of both treble damages and punitive damages for the same acts would result in a duplicative recovery.²⁴

After Bjorgen's professional malpractice action against Kinsey, Continental initiated a declaratory judgment action to determine the extent of its coverage.²⁵ The lower court concluded that the insurance policy was unambiguous and therefore, Kinsey had no coverage under the policy because the policy excluded coverage for fraudulent conduct, even though the special endorsement allowed coverage of punitive damages.²⁶ In the alternative, the lower court stated that even if the insurance policy was ambiguous, "insurance coverage for punitive damages is contrary to the public policy of this state."²⁷

On appeal, the North Dakota Supreme Court addressed the issue of the insurability of Kinsey's fraudulent conduct which resulted in an award of punitive damages.²⁸ On April 27, 1993, the North Dakota Supreme Court *held* that Continental's insurance policy with Kinsey was ambiguous.²⁹ Applying the doctrine of contract of adhesion, the court found that the policy provided coverage for punitive damages, up to the \$250,000 policy limits.³⁰ However, the policy did not provide coverage for actual or compensatory damages which arose from Kinsey's fraudulent conduct because the policy endorsement allowing insurance coverage only applied to an award of punitive damages.³¹ The North Dakota Supreme Court found that Continental had a right of indemnification from Kinsey for the

Id.

24. *Kinsey I*, 466 N.W.2d at 561.

25. *Kinsey III*, 499 N.W.2d 576.

26. *Id.* Under Kinsey's professional liability policy, Continental agreed to pay "all sums which the insured shall become legally obligated to pay as damages: 1. arising from the performance of professional services for others in the insured's capacity as a lawyer . . . because of an act or omission of the insured or any other person or firm for whose act or omission the insured is legally responsible . . ." *Id.* at 577. Kinsey's insurance policy contained several exclusions from coverage. See *supra* notes 7-8 and accompanying text (identifying the language of the relevant exclusions). However, the policy contained a special endorsement which provided that the exclusion of punitive or exemplary damages from coverage did not apply to that specific policy. See *supra* note 9 and accompanying text (addressing the specific language of this special policy endorsement).

27. *Kinsey III*, 499 N.W.2d at 576. The lower court did not give an explanation as to why it disregarded the special policy endorsement, nor did it address how or why insurance coverage of punitive damages is contrary to public policy. *Id.*

28. *Id.* at 574.

29. *Id.* at 579. The policy's special endorsement purported to insure punitive damages. However, a finding of oppression, fraud, or malice is a prerequisite to an award of punitive damages. N.D. CENT. CODE § 32-03-07 (1976). As a result, the North Dakota Supreme Court concluded that the exclusion from insuring "dishonest or fraudulent" conduct created an ambiguity because it was inconsistent with the coverage for punitive damages. *Kinsey III*, 499 N.W.2d at 579.

30. *Id.* See *infra* notes 112-113 and accompanying text (analyzing the doctrine of contract of adhesion).

31. *Kinsey III*, 499 N.W.2d at 579.

punitive damages because Kinsey's liability was a consequence of his intentional fraud and deceit.³²

On May 21, 1993, Continental filed a Petition for Rehearing which requested that the North Dakota Supreme Court clarify its opinion as to whether punitive damages are insurable under North Dakota law.³³ On May 26, 1993, the North Dakota Supreme Court denied Continental's Petition for Rehearing. Consequently, *Kinsey III* appears to be the conception of insurance coverage for punitive damages in the state of North Dakota.

III. HISTORY OF PUNITIVE DAMAGES AND INSURANCE

A. NORTH DAKOTA PUNITIVE DAMAGE REQUIREMENTS

North Dakota is among the majority of states which allow an award of punitive damages in tort actions.³⁴ North Dakota also allows an award

32. *Id.* at 576-77.

33. Petition for Rehearing at 1, *Continental Casualty Co. v. Kinsey*, 499 N.W.2d 574 (N.D. 1993) (Nos. 920288 & 920252).

34. See N.D. CENT. CODE § 32-03.2-11 (Supp. 1993) (repealing and amending N.D. CENT. CODE § 32-03-07 (1987)). Punitive or exemplary damages may be awarded under the following circumstances:

[i]n any action for the breach of an obligation not arising from contract, when the defendant has been guilty by clear and convincing evidence of oppression, fraud, or malice, actual or presumed, the court or jury, in addition to the actual damages, may give damages for the sake of example and by way of punishing the defendant.

Id. Other states which allow an award of punitive damages in tort actions include: Alabama (*See, e.g.*, ALA. CODE § 6-11-1 and § 6-11-20 to 30 (1993)); Alaska (*See, e.g.*, ALASKA STAT. § 09.17.020 (1993)); Arizona (*See, e.g.*, ARIZ. REV. STAT. ANN. §§ 12-653.01 (1992); 46-455 (1993)); Arkansas (*See, e.g.*, ARK. CODE ANN. §§ 16-64-130, 23-89-209 (Michie Supp. 1993)); California (*See, e.g.*, CAL. CIVIL CODE § 3294 (West 1994)); Colorado (*See, e.g.*, COLO. REV. STAT. ANN. § 13-21-102 (West 1987)); Connecticut (*See, e.g.*, CONN. GEN. STAT. ANN. § 52-240b (West 1991)); Delaware (*See, e.g.*, DEL. CODE ANN. tit. 18, § 6855 (1989)); Florida (*See, e.g.*, FLA. STAT. ANN. § 768.72-73 (West 1994) and § 768.21 (West 1986 and Supp. 1994)); Georgia (*See, e.g.*, GA. CODE ANN. § 51-12-5.1 (Supp. 1993)); Hawaii (*See, e.g.*, HAW. REV. STAT. § 431:10-240 (1988)); Idaho (*See, e.g.*, IDAHO CODE § 6-1604 (1987)); Illinois (*See, e.g.*, ILL. STAT. ANN. ch. 735, 5/2-604.1 (Smith-Hurd 1993)); Indiana (*See, e.g.*, *Bud Wolf Chevrolet, Inc. v. Robertson*, 519 N.E.2d 135 (1988)); Iowa (*See, e.g.*, IOWA CODE ANN. § 668A.1 (West Supp. 1993)); Kansas (*See, e.g.*, KAN. STAT. ANN. § 60-3703 (1992)); Kentucky (*See, e.g.*, KY. REV. STAT. ANN. § 411.184 and § 411.186 (1993)); Maine (*See, e.g.*, *Tuttle v. Raymond*, 494 A.2d 1353 (1985)); Maryland (*See, e.g.*, MD. CODE ANN., CTS. & JUD. PROC. § 10-913 (1993)); Minnesota (*See, e.g.*, MINN. STAT. ANN. § 549.20 (West Supp. 1994)); Mississippi (*See, e.g.*, *Fowler Butane Gas Co. v. Varner*, 141 So.2d 226 (1962)); Missouri (*See, e.g.*, *McClellan v. Highland Sales & Ins. Co.*, 484 S.W.2d 239 (1972)); Montana (*See, e.g.*, MONT. CODE ANN. § 27-1-220 (1993)); Nevada (*See, e.g.*, NEV. REV. STAT. § 42.010 (1993)); New Jersey (*See, e.g.*, N.J. STAT. ANN. § 2A:58c-5 (West 1994)); New Mexico (*See, e.g.*, *Samedan Oil Corp. v. Neeld*, 577 P.2d 1245 (1978)); New York (*See, e.g.*, N.Y. CIV. PRAC. L. & R. § 8701 (McKinney 1994)); North Carolina (*See, e.g.*, *Newton v. Standard Fire Ins. Co.*, 229 S.E.2d 297 (1976)); Ohio (*See, e.g.*, OHIO REV. CODE ANN. § 2307.80 (1991)); Oklahoma (*See, e.g.*, OKLA. STAT. ANN. tit. 23, § 9 (West 1994)); Oregon (*See, e.g.*, OR. REV. STAT. § 41.315 (1992)); Pennsylvania (*See, e.g.*, *Martin v. Johns-Manville Corp.*, 494 A.2d 1088 (1985)); Rhode Island (*See, e.g.*, *Greater Providence Deposit Corp. v. Jenison*, 485 A.2d 1242 (1984)); South Carolina (*See, e.g.*, S.C. CODE ANN. § 15-69-210 (Law Co-op 1991)); South Dakota (*See, e.g.*, S.D. CODIFIED LAWS ANN. § 21-1-4.1 (1987)); Tennessee (*See, e.g.*, TENN. CODE ANN. § 29-34-201 (1993)); Texas (*See, e.g.*, TEX. CIV. PRAC. & REM. CODE ANN. § 41.004-.008 (West 1990)); Utah (*See, e.g.*, UTAH CODE ANN. § 78-18-1 (1993)); Vermont (*See, e.g.*, *Furno v. Pignona*, 522 A.2d 746 (1986)); Virginia (*See, e.g.*, VA. CODE ANN. §§ 8.01-38.1 (Michie 1987)); West Virginia (*See, e.g.*, Smith v.

of punitive damages in wrongful death actions.³⁵ However, punitive damages generally are not recoverable in breach of contract actions,³⁶ nor in actions against governmental entities.³⁷ The conduct required for an award of punitive damages in North Dakota is oppression, fraud, or malice, actual or presumed.³⁸ The North Dakota Supreme Court has stated that intentional or willful conduct alone does not satisfy the conduct required for an award of punitive damages.³⁹ There must also be clear evidence of oppressive, fraudulent, or malicious conduct to satisfy such an award.⁴⁰

B. NORTH DAKOTA INSURANCE COVERAGE OF PUNITIVE DAMAGES

The North Dakota Constitution is silent on the issue of insurance coverage for punitive damages.⁴¹ Furthermore, the North Dakota Legislature has never specifically addressed the issue of insurability of punitive damages; however, it has identified general types of interests and events which are insurable.⁴²

In 1943, the North Dakota Legislature enacted a statute which exonerated insurance companies from liability for the willful acts of their insured.⁴³ In *Hins v. Heer*,⁴⁴ the North Dakota Supreme Court interpreted this statute as an express statement of public policy that "an insured cannot be indemnified for losses caused by his own willful acts."⁴⁵

Perry 359 S.E.2d 624 (1987)); Wisconsin (*See, e.g.,* *Jeffers v. Nysse*, 297 N.W.2d 495 (1980)); Wyoming (*See, e.g.,* *Mayflower Restaurant Co. v. Griego*, 741 P.2d 1106 (1987)).

35. *See* *Puppe v. A.C. and S., Inc.*, 733 F. Supp. 1355 (D.N.D. 1990) (finding that punitive damages are recoverable in wrongful death actions).

36. N.D. CENT. CODE § 32-03.2-11. *See also* *Campbell v. Wishek Pub. Sch. Dist.*, 150 N.W.2d 840, 842 (N.D. 1967) (prohibiting punitive damage awards in cases involving claims for breach of contract). Punitive damages may be awarded only if the breach of contract action is permeated with other wrongs and if the insured party elects to waive the contract issues and recover in tort. *Id.*

37. N.D. CENT. CODE § 32-12.1-03 (Supp. 1993) (limiting the liability of political subdivisions).

38. *See supra* note 34 (quoting the punitive damages statute).

39. *Bismarck Realty Co. v. Folden*, 354 N.W.2d 636, 643 (N.D. 1984).

40. *Id.* North Dakota's conduct requirement for punitive damages is representative of the states with the strictest conduct requirements. RICHARD L. BLATT, ET AL., PUNITIVE DAMAGES: A STATE-BY-STATE GUIDE TO LAW AND PRACTICE § 8.44 at 265 (1991). For additional state-by-state analysis of punitive damages, *see id.* at ch. 8.

41. *Kinsey III*, 499 N.W.2d at 580.

42. *See* N.D. CENT. CODE § 26.1-29-11 (1989) (stating that any contingent or unknown event which creates a liability against a person who has an insurable interest may be insured against, with the exception of insuring the drawing of a lottery).

43. N.D. CENT. CODE § 26-06-04 (1943) (repealed and reenacted as § 26.1-32-04 (1989)) (exonerating insurer from liability for losses caused by insured's willful acts, but charging insurer for losses caused by insured's negligence).

44. 259 N.W.2d 38 (N.D. 1977).

45. *Hins v. Heer*, 259 N.W.2d 38, 40 (N.D. 1977). In *Heer*, the trial court held that Heer had "wantonly, willfully, and maliciously committed a physical assault upon Hins" and awarded \$20,000 compensatory damages and \$5,000 punitive damages. *Id.* The trial court concluded that Heer's insurance policy did not provide coverage for his acts as a matter of law because the insurance policy excluded coverage for injury or damage which the insured expected or intended. *Id.* at 39. The North Dakota Supreme Court stated that the insurance exclusion of bodily injury or property damage

Furthermore, the North Dakota Supreme Court has stated that insuring against liability arising directly from one's own willful act(s) is contrary to public policy.⁴⁶ The court has also explained that "[t]he reason for awarding punitive damages is to punish the wrongdoer in order to deter him, and others, from repetition of the wrongful conduct."⁴⁷ In addition, the North Dakota Century Code provides that contracts which exempt a person from responsibility for fraudulent or willful injuries to others are against "the policy of the law."⁴⁸

It is important to note, however, that North Dakota does not have a statute which specifically addresses contracts which insure against an award of punitive damages. Furthermore, very little North Dakota case law has addressed this issue.

One case which did address insurance and punitive damages is *Yesel v. Watson*⁴⁹ in which the North Dakota Supreme Court stated that a surety is not liable for a punitive damages award against its principal.⁵⁰ In making its decision, the North Dakota Supreme Court emphasized that the purpose of punitive damages is to punish the wrongdoer.⁵¹ Therefore, the court held that the state bonding fund was not required to pay the punitive damages award.⁵² Although *Yesel v. Watson* seems to strongly disfavor another party's payment of a punitive damage award for the wrongdoer, *Yesel* is limited in its applicability because it involved a state bonding fund and not a private insurance contract.⁵³

North Dakota has no other state appellate decision addressing the issue of insurability of punitive damages. Therefore, it is helpful to examine case law addressing insurance contracts in general. The North Dakota Supreme Court has given substantial weight to the reasonable expectations and intentions of the parties in interpreting the terms of coverage of an insurance policy.⁵⁴ In interpreting the terms of an insurance

which the insured expected or intended was applicable and therefore, Heer's conduct was not insured. *Id.* at 40.

46. See, e.g., *Haser v. Maryland Casualty Co.*, 53 N.W.2d 508, 512 (N.D. 1952) (stating that insurance which indemnifies a perpetrator for his criminal acts is void and against public policy).

47. *Dahlen v. Landis*, 314 N.W.2d 63, 68 (N.D. 1981).

48. See N.D. CENT. CODE § 9-08-02 (1987) (stating that any contract for the exemption of responsibility for one's own fraud or willful injury, or for a willful or negligent violation of the law, is against "the policy of the law"). Sections 9-08-02 and 26.1-32-04 of the North Dakota Century Code both prohibit contracts which insure the willful acts of someone who causes injury to others. *Kinsey III*, 499 N.W.2d at 581.

49. 226 N.W. 624 (N.D. 1929).

50. *Yesel v. Watson*, 226 N.W. 624, 625 (N.D. 1929) (finding that the state bonding fund was not liable for a punitive damages award when a police officer falsely arrested and assaulted the plaintiff).

51. *Id.* at 626. "The very purpose said to underlie the recovery of exemplary damages is to punish the wrongdoer, and, were its recovery not attended by this supposed virtue, punitive damages would long since have fallen into the discard with other forms of punitive remedies." *Id.*

52. *Id.*

53. *Id.*

54. *Lovas v. St. Paul Ins. Cos.*, 240 N.W.2d 53 (N.D. 1976).

contract, the court is "guided by the familiar rule that, as an adhesion contract drawn by the company, it must be construed most strongly against the insurance company."⁵⁵ The court's focus on the parties' intentions and the court's decision to construe adhesion contracts against an insurance company planted the seed for insurability of punitive damages.⁵⁶

C. MINORITY VIEW—NO INSURANCE COVERAGE OF PUNITIVE DAMAGES

Jurisdictions throughout the United States are divided on the question of insurability of punitive damages.⁵⁷ Most jurisdictions which have confronted this issue have permitted insurance against certain forms of punitive damages, such as when the insurance contract includes specific language allowing coverage for punitive damages.⁵⁸ Absent specific language in the policy, jurisdictions look to public policy for assistance in determining the insurability of punitive damages.⁵⁹ Public policy considerations include economic impact, loss prevention and deterrence, and punishment.⁶⁰ As of 1992, twenty-eight states allowed insurance coverage of punitive damages and thirteen states did not.⁶¹

55. *Hughes v. State Farm Mut. Auto. Ins. Co.*, 236 N.W.2d 870, 885 (N.D. 1975).

56. See William P. Zuger, *Insurance Coverage of Punitive Damages*, 53 N.D. L. Rev. 239, 259 (1976). The trend toward broadening the coverage of insurance was evident almost 20 years ago in North Dakota. *Id.* at 259-60.

57. Michael A. Rosenhouse, *Liability Insurance Coverage as Extending to Liability for Punitive or Exemplary Damages*, 16 A.L.R. 4th 11 (1982).

58. BLATT ET AL., *supra* note 40, at 76.

59. MARK S. RHODES, *COUCH ON INSURANCE* § 56:9 (2nd ed. 1983).

60. BLATT ET AL., *supra* note 40, at 74. The risk distribution of punitive damage awards is greatly increasing because of the widespread purchase of insurance. *Id.* Insurance companies are increasing premiums for policies covering punitive damages and are denying such coverage to policyholders who may have a particular risk of incurring an assessment of punitive damages. *Id.* Higher insurance premiums may punish the insured wrongdoer; however, where punitive damages are not borne by the wrongdoer, the insurer and probably the insurer's policyholders are also punished. *Id.*

61. The following states' courts have held that insurance coverage of punitive damages is void as contrary to public policy: California (*See, e.g., Lloyd's of London v. Pac. Southwest Airlines*, 786 F. Supp. 867 (C.D. Cal. 1992)); Colorado (*See, e.g., Universal Indem. Ins. Co. v. Tenery*, 39 P.2d 776 (1934)); Connecticut (*See, e.g., Bodner v. United Serv. Auto Ass'n.*, 610 A.2d 1212 (1992)); Florida (*See, e.g., Holton v. McCutcheon*, 584 So.2d 50 (Fla. Dist. Ct. App. 1991)); Minnesota (*See, e.g., United States Fire Ins. Co. v. Goodyear Tire & Rubber Co.*, 726 F. Supp. 740 (D. Minn. 1989)); Missouri (*See, e.g., Crull v. Cleb*, 382 S.W.2d 17 (Mo. App. 1964)); New Jersey (*See, e.g., Variety Farms, Inc. v. New Jersey Mfrs. Ins. Co.*, 410 A.2d 696 (N.J. Super. Ct. App. Div. 1980)); New York (*See, e.g., Hartford Accident and Indem. Co. v. Village of Hempstead*, 397 N.E.2d 737 (1979)); Ohio (*See, e.g., Casey v. Calhoun*, 531 N.E.2d 1348 (Ohio Ct. App. 1987)); Oklahoma (*See, e.g., Dayton Hudson Corp. v. Am. Mut. Liab. Ins. Co.*, 621 P.2d 1155 (1980)); Pennsylvania (*See, e.g., Nationwide Mut. Ins. Co. v. Hassinger*, 473 A.2d 171 (Pa. Super Ct. 1984)); Rhode Island (*See, e.g., Allen v. Simmons*, 533 A.2d 541 (1987)); and South Dakota (*See, e.g., Pierre v. United Fire & Casualty Co.*, 463 N.W.2d 845 (S.D. 1990)).

The courts which hold that public policy permits insurance coverage of punitive damages are: Alabama (*See, e.g., Capital Motor Lines v. Loring*, 189 So. 897 (1939)); Alaska (*See, e.g., Providence Washington Ins. Co. of Alaska v. City of Valdez*, 684 P.2d 861 (1984)); Arizona (*See, e.g., Price v. Hartford Accident & Indem. Co.*, 502 P.2d 522 (1972)); Arkansas (*See, e.g., S. Farm Bureau Casualty Ins. Co. v. Daniel*, 440 S.W.2d 582 (1969)); Delaware (*See, e.g., Valley Forge Ins. Co. v. Jefferson*, 628

The overwhelming public policy concern against insurance coverage of punitive damages is that the wrongdoer will not be punished for what he or she has done.⁶² By shifting the punishment to the insurance company, punitive damages fail in their purpose to punish the actor and to deter others from committing similar conduct in the future.⁶³

The most significant case in support of the minority rule that disallows insurance for punitive damages is *Northwestern National Casualty Co. v. McNulty*.⁶⁴ In *McNulty*, punitive damages were assessed against an intoxicated driver, which the driver's automobile insurance company refused to pay.⁶⁵ The Fifth Circuit applied Virginia law and held that punitive damages were not insurable because the purposes of punitive damages are to punish and deter the wrongdoer, and because the punishment should rest ultimately on the party who committed the wrong.⁶⁶ Judge Gewin, in a concurring opinion, expressed the concern that prohibiting insurance of punitive damages would not deter or punish wrongdoers because "[i]f the criminal penalties provided by such statutes failed to deter the wrongdoers, I seriously doubt that closing the market to insurance coverage will do so."⁶⁷

F. Supp. 502 (D. Del. 1986)); District of Columbia (*See, e.g., Hartford Life Ins. Co. v. Title Guar. Co.*, 520 F.2d 1170 (D.C. Cir. 1975)); Georgia (*See, e.g., Greenwood Cemetery, Inc. v. Travelers Indem. Co.*, 232 S.E.2d 910 (1977)); Idaho (*See, e.g., Abbie Uriguen Oldsmobile Buick, Inc. v. U.S. Fire Ins. Co.*, 511 P.2d 783 (1973)); Iowa (*See, e.g., Skyline Harvestore Sys., Inc. v. Centennial Ins. Co.*, 331 N.W.2d 106 (1983)); Kentucky (*See, e.g., Continental Ins. Co. v. Hancock*, 507 S.W.2d 146 (1973)); Louisiana (*See, e.g., Morvant v. United States Fidelity & Guar. Co.*, 538 So.2d 1107 (La. Ct. App. 1989)); Maryland (*See, e.g., First Nat'l Bank of St. Mary's v. Fidelity & Deposit Co.*, 389 A.2d 359 (1978)); Mississippi (*See, e.g., Anthony v. Frith*, 394 So.2d 867 (1981)); Montana (*See, e.g., MONT. CODE ANN. § 33-15-317* (1987)); First Bank v. Transamerica Ins. Co., 679 P.2d 1217 (1984); Nevada (*See, e.g., NEV. REV. STAT. § 42.010* (1981)); New Hampshire (*See, e.g., Am. Home Assurance Co. v. Fish*, 451 A.2d 358 (1982)); New Mexico (*See, e.g., Baker v. A.J. Armstrong*, 744 P.2d 170 (1987)); North Carolina (*See, e.g., N.C. GEN. STAT. § 58-72* (1986)); North Dakota (*See, e.g., Kinsey III*, 499 N.W.2d 574 (1993)); Oregon (*See, e.g., Harrell v. Travelers Indem. Co.*, 567 P.2d 1013 (1977)); South Carolina (*See, e.g., S.C. CODE ANN. § 38-77-30* (Law. Co-op 1987)); Carroway v. Johnson, 139 S.E.2d 908 (1965)); Tennessee (*See, e.g., Lazenby v. Universal Underwriters Ins. Co.*, 383 S.W.2d 1 (1964)); Texas (*See, e.g., Dairyland County Mut. Ins. Co. v. Wallgren*, 477 S.W.2d 341 (Tx. Civ. App. 1972)); Vermont (*See, e.g., Whitney v. Nationwide Mut. Ins. Co.*, 562 A.2d 467 (1989)); Virginia (*See, e.g., VA. CODE ANN. § 38.2-227* (Michie 1986)); West Virginia (*See, e.g., Hensley v. Erie Ins. Co.*, 283 S.E.2d 227 (1981)); Wisconsin (*See, e.g., Brown v. Macey*, 369 N.W.2d 677 (1985)); and Wyoming (*See, e.g., Sinclair Oil Corp. v. Columbia Casualty Co.*, 682 P.2d 975 (1984)).

62. *See supra* note 60 and accompanying text.

63. *Id.*

64. 307 F.2d 432 (5th Cir. 1962). For further discussion of *McNulty*, see JOHN W. MORRISON, *THE INSURABILITY OF PUNITIVE DAMAGES* 4-5 (1985).

65. *Northwestern Nat'l Casualty Co. v. McNulty*, 307 F.2d 432, 433 (5th Cir. 1962).

66. *Id.* at 440. Judge Wisdom, writing for the majority, noted that the allowance of insurance coverage for punitive damages serves no useful purpose because insurance companies shift the burden to the public through premiums, and this ultimately punishes society for the insured's wrongdoings. *Id.* at 440-41.

67. *McNulty*, 307 F.2d at 444 (Gewin, J., concurring). Judge Gewin emphasized that a prohibition of insuring punitive damages may result in some injured parties receiving no recovery. *Id.* at 444-45.

In 1983, the Virginia Legislature enacted a statute allowing insurance coverage for punitive damages, and thereby overruled *McNulty*.⁶⁸ Nevertheless, *McNulty* commanded the minority rule for twenty-one years and is still influential today in several jurisdictions.⁶⁹

D. MAJORITY VIEW—INSURANCE COVERAGE OF PUNITIVE DAMAGES

The trend in the law is toward the insurability of punitive damages, especially when punitive damages are vicariously assessed, as in principal-agent situations.⁷⁰ The approach of vicariously-assessed punitive damages is referred to as the "hybrid approach."⁷¹ The hybrid approach prohibits insurance coverage of directly-assessed punitive damages, but permits insurance coverage of vicariously-assessed punitive damages.⁷² The hybrid approach has been utilized to support the majority rule that insurance coverage of punitive damages does not violate public policy. Even the majority opinion in *McNulty*, the seminal minority rule case prohibiting insurance coverage of punitive damages, noted that if punitive damages are permitted for vicarious conduct, the employer should be given the protection of insurance.⁷³

The most significant case in support of the majority rule that directly-assessed punitive damages are insurable is *Lazenby v. Universal Underwriters Insurance Co.*⁷⁴ In *Lazenby*, the Tennessee Supreme

68. VA. CODE ANN. § 38.2-227 (Michie 1986). See also *United Servs. Auto. Ass'n. v. Webb*, 369 S.E.2d 196, 197 (Va. 1988) (concluding that an insurance company was liable for "all sums" which the insured was legally entitled to, including punitive damages).

69. See *City Prods. Corp. v. Globe Indem. Co.*, 151 Cal. Rptr. 494 (Cal. Ct. App. 1979) (holding that public policy requires the burden of punitive damages to be borne by the party against whom they are assessed, not the insurer); *Crull v. Gleb*, 382 S.W.2d 17 (Mo. App. 1964) (stating that allowing a person to insure against punitive damages is contrary to public policy and the burden of paying such damages ultimately should rest on the wrongdoer); *Casey v. Calhoun*, 531 N.E.2d 1348 (Ohio App. 1987) (stating that the legislature and the judiciary had clearly expressed a policy against the insuring of punitive damages and therefore, any contract provision which contravenes that policy is void); *Variety Farms, Inc. v. New Jersey Mfrs. Ins. Co.*, 410 A.2d 696 (N.J. Super. 1980) (pointing out that a person who is able to insure himself against punishment gains a freedom inconsistent with the establishment of sanctions against such misconduct); *Hartford Accidental & Indem. Co. v. Hampstead*, 397 N.E.2d 737 (N.Y. 1979) (stating that to allow insurance coverage would totally defeat the purpose of punitive damages); and *Pierre v. United Fire & Casualty Co.*, 463 N.W.2d 845 (S.D. 1990) (stating that as a general rule, it is against public policy to allow an insured wrongdoer to shift the burden of payment of punitive damages to its insurer).

70. See *Rosenhouse*, *supra* note 57, at 25.

71. BLATT ET AL., *supra* note 40, at 83-84.

72. See *Ohio Casualty Ins. Co. v. Welfare Fin. Co.*, 75 F.2d 58 (8th Cir. 1934) *cert. denied*, 295 U.S. 734 (1935) (stating that if masters have no knowledge nor reason to know of their servants' wrongful acts, masters should not be held liable for servants' punitive damages and may be protected by insurance coverage). The Eighth Circuit noted that public policy is not violated by protecting a master from the unauthorized and unnatural acts of his or her servant. *Id.*

73. *McNulty*, 307 F.2d at 439-40.

74. *Lazenby v. Universal Underwriters Ins. Co.*, 383 S.W.2d 1 (Tenn. 1964). Several jurisdictions have followed the holding of the *Lazenby* case. See *supra* note 61. *Lazenby* is similar to *McNulty* in that both cases involved the assessment of punitive damages against an intoxicated driver. See *Lazenby*, 383 S.W.2d at 1; *McNulty*, 307 F.2d at 436. However, the *Lazenby* court allowed

Court reasoned that public policy is a key factor in the question of insurability of punitive damages.⁷⁵ The *Lazenby* court examined three public policy considerations in its decision to allow insurance coverage of punitive damages. First, the court questioned the theory that disallowing insurance coverage for punitive damages deters wrongdoers.⁷⁶ Second, the court determined that the insurance policy's language covered punitive damages.⁷⁷ Finally, the court determined that there was a fine line distinguishing simple negligence from negligence upon which punitive damages will be awarded.⁷⁸

In further support of the majority rule addressed in *Lazenby*, the Wyoming Supreme Court has stated that the threat of punitive damages has never been proven to deter a person from willful and wanton misconduct.⁷⁹ Other state courts have concluded that insurance coverage of punitive damages is not contrary to public policy when an insurance policy clearly requires the insurer to cover punitive damages.⁸⁰ In *Price v. Hartford Accidental & Indemnity Co.*,⁸¹ the Arizona Supreme Court reasoned that the defendant, whose insurance company paid the punitive damages assessed against him, would still be subject to criminal penalties and substantially higher insurance rates.⁸² Furthermore, the *Price* court emphasized that Arizona has more than one public policy and "[o]ne such public policy is that an insurance company which admittedly took a premium for covering all liability for damages, should honor its obligation."⁸³ The Arizona court concluded that the insurance company must honor its obligation and pay the punitive damages.⁸⁴

insurance coverage of punitive damages under the policy-owner's automobile liability insurance policy. 383 S.W.2d at 5. The Tennessee Supreme Court looked to the insurance policy's language and concluded that as a matter of interpretation, the policy insured both compensatory and punitive damages. *Id.* The type of insurance language used in *Lazenby* has been interpreted by most courts to cover both compensatory and punitive damages. *Id.* Therefore, policyholders with similar insurance policies would expect to be protected against all unintentional claims. *Id.*

75. *Lazenby*, 383 S.W.2d at 5.

76. *Id.* The court determined that since the state's criminal sanctions did not appear to deter the "slaughter on our highways and streets," neither would disallowing insurance for punitive damages for such conduct. *Id.*

77. *Id.*

78. *Id.*

79. *Sinclair Oil Corp. v. Columbia Casualty Co.*, 682 P.2d 975, 980 (Wyo. 1984). Emphasizing the right to freely contract, the court concluded, "[w]e will not invalidate a contract entered into freely by competent parties on the basis of public policy unless that policy is well settled, unambiguous and not in conflict with another public policy equally or more compelling." *Id.* at 979.

80. *See, e.g., Price v. Hartford Accidental & Indem. Co.*, 502 P.2d 522 (Ariz. 1972); *Providence Washington Ins. Co. of Alaska v. City of Valdez*, 684 P.2d 861 (Ala. 1984).

81. 502 P.2d 522 (Ariz. 1972).

82. *Price v. Hartford Accidental & Indem. Co.*, 502 P.2d 522, 524 (Ariz. 1972). The defendant injured another while drag racing. *Id.* at 523.

83. *Id.* at 524.

84. *Id.*

Other courts have held that the "all sums" language in a policy includes liability for both compensatory and punitive damages.⁸⁵ The Iowa Supreme Court in *Skyline Harvestore Systems, Inc. v. Centennial Insurance Co.*⁸⁶ considered two competing public policies in interpreting "all sums" language: the freedom to contract versus the deterrent purpose of punitive damages.⁸⁷ In holding that the "all sums" language covered punitive damages, the *Skyline* court elevated freedom to contract above public policy reasons for punitive damages, and explained that a wrongdoer does not weigh the benefits of a wrong act against potential costs.⁸⁸ Furthermore, the court explained that persons considered to be poor risks may be punished with the substantial difficulty and high costs in obtaining insurance coverage.⁸⁹

The Montana Supreme Court has specifically addressed the issue of insurability of punitive damages and has concluded that insurance coverage of punitive damages does not violate public policy.⁹⁰ In focusing on the requirements for an exemplary damages award, the Montana Supreme Court noted that concepts such as "recklessness" and "oppression" have not yet been defined.⁹¹ Consequently, a defendant may be unable to know whether his or her conduct would result in an award of punitive damages until after the trial.⁹² The Montana Supreme Court concluded that the decision of whether to insure punitive damages should remain with insurance carriers and their customers until the law of punitive damages is more certain and predictable.⁹³ Taking an even stronger approach, the Texas court of appeals has stated that the Texas financial

85. See *Skyline Harvestore Sys., Inc. v. Centennial Ins. Co.*, 331 N.W.2d 106 (Iowa 1983). The "all sums" language in *Skyline* stated, "[t]he company will pay on behalf of the insured *all sums* that the insured shall become legally obligated to pay as damages . . ." *Id.* at 107 (emphasis added).

86. 331 N.W.2d 106 (Iowa 1983).

87. *Skyline Harvestore Sys., Inc. v. Centennial Ins. Co.*, 331 N.W.2d 106, 107 (Iowa 1983). The court emphasized the dangers of invalidating private contracts on the basis of public policy and stated that "for a court to undertake to invalidate private contracts upon the ground of 'public policy' is to mount 'a very unruly horse, and when you once get astride it you never know where it will carry you.'" *Id.* at 109 (quoting *Harrell v. Travelers Indem. Co.*, 567 P.2d 1013, 1016 (Or. 1978)).

88. *Skyline*, 331 N.W.2d at 109. The court explained that "we doubt that ordinary potential tortfeasors make calculations to determine if the expected benefits of a harmful act are outweighed by the potential costs of punitive damages, insured or uninsured." *Id.*

89. *Id.* A Maryland court pointed out that denying insurance coverage of punitive damages could jeopardize small businesses whose owners suffered punitive damages awards in malicious prosecution actions wherein the business owners acted in good faith. *First Nat'l Bank v. Fidelity & Deposit Co.*, 389 A.2d 359 (Md. 1978). See *infra* notes 106-107 and accompanying text (addressing Continental's malicious prosecution policy language).

90. *First Bank v. Transamerica Ins. Co.*, 679 P.2d 1217, 1218 (Mont. 1984).

91. *Id.* at 1222.

92. *Id.* This is because the judge or jury must first determine if the defendant's conduct was reckless or oppressive. *Id.*

93. *Id.* at 1223. Oregon courts have speculated that disallowance of coverage might lead to the financial ruin of a professional person, wage earner, housewife, or retired person. *Harrell v. Travelers Indem. Co.*, 567 P.2d 1013 (Or. 1977).

responsibility statute *requires* insurance companies to provide coverage for all liability imposed by law, which includes punitive damages.⁹⁴

IV. LEGAL ANALYSIS

Kinsey III, which followed the majority rule and allowed insurance coverage of punitive damages, marked a major departure from North Dakota statutory law which forbids the insuring or exonerating of fraudulent conduct.⁹⁵ The majority in *Kinsey III* found that there were at least two different interpretations⁹⁶ to Continental's insurance policy with Kinsey, making the policy ambiguous.⁹⁷ The court applied the doctrine of contract of adhesion and determined that the policy should be construed in the light most favorable to the insured.⁹⁸

According to the majority, the ambiguities in the insurance policy arose from the fraudulent conduct exclusion and the express policy endorsement waiving the punitive damages exclusion.⁹⁹ The first possible interpretation identified by the majority was that the policy excluded coverage for any damages arising from Kinsey's fraudulent conduct.¹⁰⁰ This interpretation would relieve Continental from any obligation to pay because Kinsey's conduct was found to be fraudulent.¹⁰¹ The other possible interpretation was that the policy endorsement expressly waived the punitive damages exclusion and therefore, would obligate Continental to pay Kinsey's punitive damages.¹⁰² Under the doctrine of contract of adhesion, the majority chose the latter interpretation because it was most favorable to the insured, given the policy's ambiguity.¹⁰³

Contrary to the majority's determination that the policy was ambiguous, Justice Levine found Continental's insurance policy with Kinsey to

94. Dairyland County Mut. Ins. Co. v. Wallgren, 477 S.W.2d 341, 342 (Tex. Civ. App. 1972) (interpreting TEX. INS. CODE ANN., arts. 5.06, 5.35 (allowing insurance coverage for punitive damages)).

95. N.D. CENT. CODE § 26.1-32-04 (1989) (exonerating insurer for losses caused by insured's willful acts, but charging insurer for losses caused by insured's negligence).

96. The court applied State Farm Mut. Auto. Ins. Co. v. LaRoque, 486 N.W.2d 235 (N.D. 1992), and found two alternative interpretations to Kinsey's insurance contract. *Kinsey III*, 499 N.W.2d at 579. The *LaRoque* court defined an ambiguous contract as one where reasonable arguments as to a contract's meaning can be made in support of contrary positions. *LaRoque*, 486 N.W.2d at 238.

97. *Kinsey III*, 499 N.W.2d at 577. See *supra* notes 7-9 and accompanying text (identifying the ambiguous policy language).

98. *Kinsey III*, 499 N.W.2d at 577-78.

99. *Id.* at 579. For the language of this exclusion and waiver, see *supra* notes 7-9 and accompanying text.

100. *Kinsey III*, 499 N.W.2d at 579. The court based this interpretation on a clause in the insurance contract which specifically excluded coverage of fraudulent conduct. See *supra* note 7 and accompanying text for contract language.

101. *Kinsey III*, 499 N.W.2d at 577.

102. *Id.* See *supra* notes 7-9 and accompanying text for policy language.

103. *Id.* at 579.

be, in its entirety, unambiguous.¹⁰⁴ Justice Levine explained that the majority "omits a key part of the exclusion to come up with an ambiguity."¹⁰⁵ According to Justice Levine, the policy endorsement allowing coverage of punitive damages clearly applied only to a malicious prosecution claim.¹⁰⁶ However, the majority did not mention this malicious prosecution exception to the exclusion of punitive damages. In fact, the only reference to this malicious prosecution exception is by Justice Levine.¹⁰⁷ In her dissent, Justice Levine stated that the contract was not ambiguous "because of its plain language."¹⁰⁸ However, even if there were two different interpretations to the insurance policy, Justice Levine reasoned that excluding coverage for any punitive damages arising from fraudulent conduct was the only reasonable interpretation because Continental's payment of the punitive damages assessed against its insured would violate North Dakota public policy and was therefore void.¹⁰⁹ Justice Levine stated, "[a] contract should be construed, if possible, to follow the law and public policy, not to contravene it."¹¹⁰ North Dakota does not have a well-established public policy regarding punitive damages and insurance; however, Justice Levine suggested that sections 26.1-32-04 and 9-08-02 of the North Dakota Century Code enunciate a public policy against the insuring of punitive damages.¹¹¹

Justice Levine seemed to infer that the majority created an ambiguity in order to reach a result-oriented decision. In its finding that Continental's insurance policy with Kinsey was ambiguous, the majority utilized the "doctrine of contract of adhesion"¹¹² as a tool to construe the ambiguous policy strongly against Continental and in favor of providing insurance

104. *Kinsey III*, 499 N.W.2d at 582 (Levine, J., dissenting).

105. *Id.*

106. *Id.* at 583. The policy endorsement in its entirety stated: "This insurance does not apply . . . [to] any dishonest, fraudulent, criminal or malicious act or omission of the insured or any partner, employee, officer or stockholder of the insured. This exclusion does not apply to any such act or omission which is the basis of a malicious prosecution claim." *Id.* (emphasis added).

107. *Kinsey III*, 499 N.W.2d at 583 (Levine, J., dissenting).

108. *Id.*

109. *Id.*

110. *Id.* (citing *Seher v. Woodlawn Sch. Dist. No. 26*, 59 N.W.2d 805 (N.D. 1953)).

111. *Kinsey III*, 499 N.W.2d at 583 (Levine, J., dissenting). Sections 26.1-32-04 and 9-08-02 of the North Dakota Century Code both prohibit the insuring of willful or fraudulent acts or the exonerating of such acts. See *supra* notes 43, 48. Justice Levine stated that "[a] statute controls a contrary [insurance] policy provision and the conflicting provision in the insurance contract must give way to the statute." *Kinsey III*, 499 N.W.2d at 583.

112. This doctrine is explained in *Aid Ins. Servs., Inc. v. Geiger*, 294 N.W.2d 411, 414-15 (N.D. 1980). The *Geiger* court explained: "[I]t is well-established in North Dakota that, because an insurance policy is a contract of adhesion, any ambiguity or reasonable doubt as to the meaning of the policy is to be strictly construed against the insurer and in favor of the insured." *Id.* at 414. The *Geiger* court stated that insurance policies are written by insurance experts and "[i]nsurance policies should be written so that an ordinary layperson, untrained in the field of insurance, can clearly understand them and know whether or not coverage is afforded." *Id.* at 414-15. "If they are not so written, the insurance company must assume the consequences of the ambiguity and resulting confusion." *Id.* at 415.

coverage for Kinsey.¹¹³ The majority did not apply the rule of strict construction¹¹⁴ because it is a general rule for interpreting ambiguous contracts, whereas the doctrine of contract of adhesion is limited to ambiguous "adhesion" contracts.¹¹⁵ The majority, in applying the doctrine of contract of adhesion, held that the contract must be interpreted against Continental because Continental created the ambiguity and therefore, must assume its consequences.¹¹⁶

The *Kinsey III* majority next turned to the interplay between statutory law and public policy to ascertain any legislative intent or any public policy regarding the insurability of punitive damages.¹¹⁷ The majority examined the North Dakota statutes which identify contracts that are against "the policy of the law,"¹¹⁸ and which identify acts by an insured which will exonerate an insurer.¹¹⁹ The majority determined that these two statutes, construed together, "clearly manifest a public policy of discouraging persons from committing fraud or other willful acts that cause injury to others."¹²⁰ The court then compared section 26.1-32-04 of the

113. *Kinsey III*, 499 N.W.2d at 577-578, (citing *Mills v. Agrichemical Aviation, Inc.*, 250 N.W.2d 663, 671 (N.D. 1977)). However, if parol evidence is offered or if application of other relevant rules of contract indicate that the parties did not contemplate insurance coverage, the doctrine of contract of adhesion will not be applied. *Kinsey III*, 499 N.W.2d at 578.

114. N.D. CENT. CODE § 9-07-19 (1987). The rule of strict construction provides that ambiguous contract language should be interpreted against the party who caused the ambiguity or uncertainty. *Id.* Although the majority indicated that they applied the doctrine of contract of adhesion and not the rule of strict construction, there actually is little, if any, distinction between these rules in the insurance context. Both have the result of construing ambiguous contracts against the party who created the ambiguity, the insurance company.

115. *Kinsey III*, 499 N.W.2d at 579. The majority in *Kinsey III* contended that the doctrine of strict construction was not a rule of last resort for contract interpretation; rather it was a rule to be applied with other relevant rules to resolve ambiguities in adhesion contracts. *Id.* Furthermore, the majority noted that the parties did not assert any factual dispute as to the meaning of the ambiguous policy provisions, nor did they present any relevant parol evidence to exhibit the parties' mutual intent. *Id.* Justice Levine strongly disagreed with the majority's contention that the doctrine of strict construction was not a rule of last resort. *Id.* at 582. Justice Levine stated that the rule of strict construction should be applied last, "just as its language tells us to" rather than applied first, "like the majority does in fact." *Id.* Furthermore, Justice Levine stated, "[i]t is an oxymoron, an illogical assertion, to apply [the rule of strict construction] 'along with other rules of construction.'" *Id.*

116. *Id.* According to the majority, Continental's endorsement form allowing insurance coverage of punitive damages would be meaningless if the policy was construed to not cover punitive damages when fraudulent or malicious conduct was involved. *Id.* at 579. The majority concluded that to give the endorsement form waiving the punitive damages exclusion full effect, it must apply when fraudulent or malicious conduct was involved. *Id.*

117. *Kinsey III*, 499 N.W.2d at 581.

118. N. D. CENT. CODE § 9-08-02 (1987) (stating that any contract for the exemption of responsibility for one's own fraud or willful injury, or for a willful or negligent violation of the law, are against "the policy of the law").

119. N.D. CENT. CODE § 26.1-32-04 (1989) (exonerating insurer for losses caused by insured's willful acts, but charging insurer for losses caused by insured's negligence).

120. *Kinsey III*, 499 N.W.2d at 581. "These statutes foster that public policy by prohibiting contracts which would exempt a person from being held responsible for the consequences of his wrongful intentional conduct (Section 9-08-02, N.D.C.C.) and by precluding insurers from indemnifying insureds for losses caused by the insured's willful acts (Section 26.1-32-04, N.D.C.C.)." *Id.* Justice Levine, extending this line of reasoning, concluded that sections 26.1-32-04 and 9-08-02 of the North Dakota Century Code enunciate a public policy against the insurability of punitive damages. *Id.* at 583. See *supra* notes 109, 111 and accompanying text.

North Dakota Century Code with an identical California statute specifying acts of an insured that will exonerate an insurer.¹²¹ While the majority agreed with a California court's interpretation that the statute exempts insurers from liability for punitive damages incurred by an insured's intentional acts,¹²² it nevertheless held Continental responsible for the punitive damages assessed against Kinsey because of the ambiguities in the policy.¹²³

Finally, the majority addressed several public policy considerations: the public policy for enforcing contracts that do not contravene public policy; the public policy for supporting the intentions of the parties in a contract; the public policy for discouraging persons from committing fraudulent acts, and the public policy against insurance companies collecting premiums for coverage they do not intend to offer.¹²⁴ However, most of those public policies were given minimal, if any, consideration before the majority determined that punitive damages are insurable.¹²⁵ The court recognized that it has a significant function to "maintain and enforce contracts" which do not contravene public policy.¹²⁶ The majority also cited an insurance treatise which contends that it is against public policy to insure punitive damages without "specific language in the policy extending coverage for punitive damages"¹²⁷ Nevertheless, the majority found that although North Dakota statutory law has a public policy prohibiting contracts which exempt persons from their wrongful intentional conduct, the Legislature did not intend to "benefit insurance companies by allowing them to collect premiums for coverage they do not intend to provide."¹²⁸ The majority thus seemed to give considerably more weight to the freedom to contract and to the prevention of insurance companies from collecting premiums for coverage they do not

121. See CAL. INS. CODE § 533 (West 1993) (providing that "[a]n insurer is not liable for a loss caused by the willful act of the insured; but he is not exonerated by the negligence of the insured, or of the insured's agents or others."); N.D. CENT. CODE § 26.1-32-04.

122. *Kinsey III*, 499 N.W.2d at 580 (citing *City Prods. Corp. v. Globe Indem. Co.*, 151 Cal. Rptr. 494 (1979)).

123. *Id.* at 579.

124. *Kinsey III*, 499 N.W.2d at 581.

125. *Id.* The court concluded that, "Continental is required to meet its contractual obligation to pay for punitive damages awarded against Kinsey, but it has recourse against Kinsey for these payments, because the losses stem from Kinsey's willful fraud and deceit." *Id.*

126. *Kinsey*, 499 N.W.2d at 580 (citing *Seher v. Woodlawn Sch. Dist.*, 59 N.W.2d 805, 810 (1953)). The majority in *Kinsey III* arguably contradicted this function, because it enforced insurance coverage of punitive damages even as it admitted that it is against public policy to exempt insureds for their intentional or willful acts. See *supra* note 120 and accompanying text.

127. *Kinsey III*, 499 N.W.2d at 580 (citing MARK S. RHODE, *COUCH ON INSURANCE* § 56:9, at 16. The policy language in Kinsey's policy was not specific; in fact, the majority found it to be ambiguous. However, the majority still allowed the policy to cover punitive damages. See *supra* notes 100-103 and accompanying text (discussing the majority's interpretation of the ambiguous policy terms).

128. *Id.* at 581. There is no mention of the amount of the premium paid by Kinsey in the court record of *Kinsey III*.

intend to offer, than to the public policy against contracts which exempt a person from liability for willful acts.

Justice Levine stressed that statutory law controls over a contrary public policy provision and that "the conflicting provision in the insurance contract must give way to the statute."¹²⁹ However, the majority appeared to disregard the statutory law prohibiting the insuring of willful or fraudulent acts, and instead allowed contrary public policy to prevail over statutory law. Anticipating the problems caused by allowing fraudulent and willful acts to be insured, the majority then backpedaled from its holding and allowed Continental to seek indemnity from Kinsey for the losses caused from Kinsey's "willful fraud and deceit."¹³⁰ The logic behind the majority's decision to grant indemnity was that the Legislature did not intend to "benefit insureds who cause intentional injury to others, by allowing them to shift to insurance carriers the monetary responsibility for their intentional torts."¹³¹ Justice Levine recognized the majority's assertion that it could not enforce the policy and contended that the majority, therefore, rewrote the insurance policy to "creat[e] an extra policy remedy."¹³² This "extra policy remedy" consisted of Continental paying the punitive damages and then obtaining reimbursement from Kinsey.¹³³

The majority did not assert that insurance coverage for punitive damages no longer violates public policy. Instead, the majority stated the issue in terms of whether public policy allows an insurer to break its express contractual promise to pay for punitive damages assessed against its insured.¹³⁴ The majority answered in the negative, giving full effect to the parties' mutual intentions to contract for insurance coverage of punitive damages.¹³⁵

In response, Justice Levine unequivocally stated her disbelief that insurance coverage for punitive damages was intended by the parties, especially because the insured was an attorney who presumably would

129. *Kinsey III*, 499 N.W.2d at 583 (Levine, J., dissenting). See also *Anderson v. Northwestern Fire & Marine Ins. Co.*, 201 N.W. 514 (1924) (stating that statutory law controls contrary stipulations in a contract).

130. *Kinsey III*, 499 N.W.2d at 581.

131. *Id.* The court looked to *Fastow v. Burleigh County Water Resource Dist.*, 415 N.W.2d 505 (N.D. 1987) for this decision. *Id.* at 580. The *Fastow* court held that "a political subdivision's liability exposure is limited as envisioned by the statute, but the full extent of purchased insurance coverage is available to satisfy judgments entered against a political subdivision." *Fastow*, 415 N.W.2d at 510.

132. *Kinsey III*, 499 N.W.2d at 583 (Levine, J., dissenting).

133. *Id.* Justice Levine pointed out that Continental did not contract to pay punitive damages, nor did it and Kinsey agree to subrogate Bjorgen's claim against Kinsey. *Id.* Justice Levine concluded, "I believe neither the majority's construction of the contract nor the argument upon which the construction is based, is reasonable. There being only one reasonable construction, there is no ambiguity." *Id.*

134. *Kinsey III*, 499 N.W.2d at 581.

135. *Id.*

know the law and avoid conduct warranting punitive damages.¹³⁶ Justice Levine contended that the majority first created an ambiguity and then construed it against Continental so that punitive damages were insured.¹³⁷ Justice Levine concluded that "as a grand finale, the majority fashions a solution for the problems of its own making: it converts a liability insurance policy that was purchased to and intended to provide indemnity, into a surety bond, not contracted for, and presumably not paid for."¹³⁸

V. IMPACT

The potential ramification of *Kinsey III* is that the North Dakota Supreme Court will allow insurance coverage for punitive damages, provided that such coverage is expressly written in the policy. The North Dakota Supreme Court recognized that insurance coverage for punitive damages is against public policy.¹³⁹ However, the majority weighed this public policy against the freedom to contract and concluded that the mutual intentions of the parties outweighed any public policy against insurance coverage of punitive damages.¹⁴⁰ In doing this, the North Dakota Supreme court sent a message to contracting parties that freedom to contract has been elevated over the reluctance to exonerate a party from liability for willful or fraudulent acts. Parties can now presumably contract for something that may be against public policy as long as it is expressly written in the contract and the parties intended to contract for it.

Furthermore, *Kinsey III* may close the book on future public policy considerations in relation to insurance policies. If the insurance policy is interpreted as not providing coverage for punitive damages, the issue of public policy will likely never be addressed. If the policy is interpreted as covering punitive damages, the insurer will probably not be able to escape its contractual obligations, despite the legislature's expressed public policy concerns.

Insurance companies doing business in North Dakota should be concerned about the precedent established by *Kinsey III*. *Kinsey III* cautions insurance companies to clearly express terms and coverage in their policies so that they are not held liable for coverage which they did not intend to provide.

136. *Kinsey III*, 499 N.W.2d at 582 (Levine, J., dissenting). Justice Levine expounded, "[a]fter all, the insured is a lawyer whose stock in trade is knowledge of the law or the skill to acquire that knowledge, and the law, specifically, sections 26.1-32-04 and 9-08-02, prohibits insuring for willful injury and the punitive damages arising from that injury." *Id.*

137. *Id.* at 584.

138. *Id.*

139. *Kinsey III*, 499 N.W.2d at 581.

140. *Id.*

Kinsey III may also alleviate an injured party's difficulty in collecting on his or her judgment. In *Kinsey III*, Bjorgen had more of a chance of collecting her judgment from Continental than from Kinsey. Perhaps the court recognized this in ordering Continental to compensate Bjorgen; Continental was then given the problem of trying to collect from Kinsey.¹⁴¹ In doing this, the North Dakota Supreme Court has sent out a "deep pocket" message that injured parties will be compensated when wrongfully injured. The burden of collecting judgments now rests with the insurance companies which are indemnified for the fraudulent conduct of their policy-holders.

The North Dakota Supreme Court does not necessarily impede the punishment factor of punitive damages by allowing insurance coverage of such damages. The wrongdoer is required to indemnify his or her insurance company for any punitive damages awards.¹⁴² Additionally, an insured may be liable for punitive damages which exceed the limits contained in the policy. Furthermore, the insured may be punished for wrongful or fraudulent conduct by other methods such as criminal charges, disciplinary actions,¹⁴³ and increased insurance premiums.

Ultimately, *Kinsey III* empowers the citizens of North Dakota with a significantly greater freedom to contract. Accordingly, the availability of insurance coverage for punitive damages will probably depend solely upon the language of the insurance policy. However, the echo of Justice Levine's last remarks leaves a chilling impact on the majority's allowance of insurance coverage for punitive damages: "A rose by any other name is still a rose. Payment of punitive damages by Continental is still against public policy."¹⁴⁴

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141. *Id.*

142. *Id.* Although wrongdoers must indemnify their insured, seldom are wrongdoers financially able to indemnify.

143. Disciplinary actions were brought against attorney Kinsey for his fraud and deceit. See Brief of Appellee at 4 & n.1, *Continental Casualty Co. v. Kinsey*, 499 N.W.2d 574 (N.D. 1993) (Nos. 920288 and 920252).

144. *Kinsey III*, 499 N.W.2d at 584 (Levine, J., dissenting).

