Goodbye to *Camelot*

Rory v Continental Ins Co Negates a Judicial Inquiry into the Reasonableness of a Contract Term

By Joel C. Tuoriniemi, Michael P. Petroskey, and Brandon M. Schwartz

The Michigan legislature has established a general period of limitations of six years for a breach of contract claim, while a third-party claim for injury to a person or property under an insurance contract has a three-year period. An issue arises, however, if a party claims there is an agreement creating a shortened period of limitations. In *Rory v Continental Ins Co,*[1] decided July 28, 2005, the Michigan Supreme Court addressed whether a court can undertake a judicial inquiry into the reasonableness of a contract provision setting forth a one-year period of limitations. In a sharply divided 4 to 3 decision, the *Rory* Court rejected use of the three-pronged reasonableness doctrine set forth in *Camelot Excavating Co, Inc v St Paul Fire & Marine Ins Co.*[2] This article (1) outlines past Michigan Supreme Court cases that formulated the "rule of *Camelot*," (2) summarizes the majority and dissenting opinions in *Rory*, (3) examines orders by the Commissioner of the Office of Financial and Insurance Services (Commissioner) and court of appeals cases released after *Rory,* and (4) discusses the future of the reasonableness doctrine in Michigan.

The Rule of *Camelot*

Camelot

In *Camelot,* a contractual provision set forth a one-year limitation for bringing suit on a private performance bond. The *Camelot* Court noted the general rule, set forth in *Tom Thomas Org, Inc v Reliance Ins Co,*[3] that such a provision was valid if reasonable, even though the period was less than that prescribed by the legislature.[4] The *Camelot* Court also stated that an analysis of the "reasonableness" of such a provision should address whether (1) the claimant has sufficient opportunity to investigate and file an action, (2) the time is so short as to work a practical abrogation of the right of action, and (3) the action is barred before the loss or damage can be ascertained.[5] In applying this "rule of *Camelot,*" the Court held that the provision was enforceable.

Justice Levin, author of the majority opinion in *Tom Thomas,* concurred with the *Camelot* majority. He wrote "separately to emphasize the narrowness of the holding and to express [his] concern about the development of a rule authorizing contractually shortened periods of limitation."[6] Justice Levin stated:

> The rationale of the rule allowing parties to contractually shorten statutory periods of limitation is that the shortened period is a bargained-for term for the contract. Allowing such bargained-for terms may in some cases be a useful and proper means of allowing parties to structure their business dealings.
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> In the case of an adhesion contract, however, where the party ostensibly agreeing to the shortened period has no real alternative, this rationale is inapplicable.[7]

Herweyer

Herweyer v Clark Hwy Services, Inc[8] involved a contract that limited the time to bring an employment-related cause of action to six months after termination of an employee. The contract also stated that if any provision was deemed unenforceable, the contract should be enforced "as far as legally possible."[9] This saving clause was the focus of the Supreme Court's opinion. The Michigan Court of Appeals had found that the saving clause created a requirement that the employee bring an action within a "minimally reasonable time."[10] Given that the plaintiff waited 31 months after termination to bring suit, the court of appeals had concluded the judicially imposed "minimally reasonable time" requirement had not been met.

The Supreme Court reversed, holding that the courts had no authority to impose such a requirement.[11] The *Herweyer* Court stated, however, that the scope of its review was limited to appropriate interpretation of the saving clause, and reversed the court of appeals on that basis only. No opinion was expressed "regarding the reasonableness of any shortened period agreed to by the parties."[12]

Citing Justice Levin's concurring opinion in *Camelot,* the *Herweyer* Court also distinguished employment contracts from other "private" contracts.[13] Acknowledging the disparate bargaining power often prevalent in negotiating an employment contract, the Court stated that such contracts deserve close judicial scrutiny. Following the *Herweyer* decision, scholars noted that whether a contractual term

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reducing the period of limitations was reasonable under the "rule of *Camelot*" remained unclear and would be subject to further review.[14]

The *Rory* Decision

In *Rory,* an insurance policy required that a claim or suit for uninsured motorist coverage be brought within one year after the date of accident. Citing *Camelot,* the Michigan Court of Appeals had held that the contact term creating a one-year period of limitations was unreasonable.[15]

In a 4 to 3 decision, the Michigan Supreme Court reversed. Justice Young, author of the majority opinion, wrote that the decision in *Camelot* was "premised upon the adoption of a 'reasonableness' test found in the dicta of *Tom Thomas.* In failing to employ the plain language of the contract, the *Camelot* court erred."[16] The majority opinion further noted:

> A fundamental tenet of our jurisprudence is that unambiguous contracts are not open to judicial construction and must be *enforced as written*. . . .
>
> When a court abrogates unambiguous contractual provisions based on its own independent assessment of "reasonableness," the court undermines the parties' freedom of contract. . . .
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>
> . . . A mere judicial assessment of "reasonableness" is an invalid defense upon which to refuse to enforce contractual provisions. Only recognized traditional contract defenses may be used to avoid the enforcement of the contract provision.[17]

The *Rory* Court then overruled *Tom Thomas, Camelot,* and subsequent decisions to the extent that such cases invalidated unambiguous contractual terms on the basis of a judicial reasonableness determination.[18]

"An 'adhesion contract' is simply that: *a contract.* It must be enforced according to its plain terms unless one of the traditional contract defenses applies. Regardless of whether a contract is adhesive, a court may not revise or void the unambiguous language of the agreement to achieve a result that it views as fairer or more reasonable."

The *Rory* majority further held that enforcing shortened periods of limitations was not contrary to public policy, stating that, with the exception of life insurance policies (under MCL 500.4046), Michigan has "'no general policy or statutory enactment . . . which would prohibit private parties from contracting for shorter limitations periods than those specified by general statutes.'"[19] The majority noted that the legislature had provided a mechanism to ensure the reasonableness of insurance policies issued in Michigan. Under MCL 500.2236, the Commissioner "may consider the reasonableness of the conditions and exceptions" when determining whether to grant approval to use a policy form.[20]

Opining that the *Herweyer* holding was a "summary conclusion" reached solely on the basis of Justice Levin's concurring opinion in *Camelot,* the *Rory* majority also rejected the argument that the policy was an unenforceable adhesion contract, stating: "An 'adhesion contract' is simply that: *a contract.* It must be enforced according to its plain terms unless one of the traditional contract defenses applies."[21] "Regardless of whether a contract is adhesive, a court may not revise or void the unambiguous language of the agreement to achieve a result that it views as fairer or more reasonable."[22]

In one of three separate dissents, Justice Kelly wrote that the reasonableness test set forth in *Camelot* was well founded and that "[t]he essential reasoning behind this rule is that an unreasonable limitations period offers an aggrieved party no recourse to the courts."[23] Justice Kelly emphasized that a party may not learn that he or she has a serious impairment, or that the party causing the injury was uninsured, until after one year has passed; as such, all prongs of the test outlined in *Camelot* and *Herweyer* "weigh against allowing a shortened limitations period . . . ."[24]

Concerning adhesion contracts, Justice Kelly wrote: "[T]he idea of balancing the inequities of form contracts (or what are now more commonly known as 'adhesion contracts') has been long recognized. And there is good reason for this longstanding recognition. Namely, the bargained-for exchange fundamental to traditional contracts simply does not exist in adhesion contracts."[25]

Justices Cavanagh and Weaver concurred with the result reached in Justice Kelly's dissent. Justice Cavanagh wrote that the general principle regarding enforcement of unambiguous contract terms is subject to "numerous caveats that are deeply rooted in our jurisprudence, including the following: where a contractual limitations provision shortens the otherwise applicable period of limitations, the provision must be reasonable to be enforceable."[26] Justice Weaver emphasized that the longstanding rule regarding enforcement of unambiguous contractual terms must be balanced with "specialized rules of interpretation and enforcement for insurance contracts" that foster consumer protection.[27]

Post-*Rory* Applications

Insurance Contracts

In response to *Rory,* the Commissioner has issued orders that prohibit periods of limitations of less than three years on new and revised policy forms for uninsured/underinsured motorist coverage.[28] The orders state that a limitations period of less than three years is misleading and unreasonably affects risks expected to be assumed by consumers.[29] In reaching this conclusion, each order noted that the court of appeals in *Rory* had trouble reconciling a one-year limitations period with the requirement that a plaintiff suffer a serious impairment of body function before liability arises, given that whether such an impairment exists may not be able to be determined one year after an injury.[30]

While the orders address the use of new and revised policy forms for uninsured/underinsured motorist coverage, neither applies to policy forms currently in use as long as those forms are not modified

in any respect. The Commissioner is "currently considering what action is appropriate with regard to those policies or riders in use" before the effective date of the orders and "may withdraw approval of those forms . . . at a future time."[31]

Employer/Employee Relationships

Pre-*Rory* cases in the employer/employee context dealt with contractually shortened periods of limitation by applying the "rule of *Camelot.*"[32] The court of appeals case of *Clark v DaimlerChrysler Corp*[33] addressed whether a six-month period of limitations set forth and agreed to by prospective employees in an employment *application* was enforceable.[34] The *Clark* majority applied the holding in *Rory,* finding that "[b]ecause there are no statutes explicitly prohibiting the contractual modification of limitations periods in the employment context, the contract provision is not contrary to law."[35] The *Clark* majority also addressed whether the traditional contract defense of unconscionability could be used to invalidate the shortened period of limitations. With regard to substantive unconscionability, "a contract or contract provision is not invariably substantively unconscionable simply because it is foolish for one party and very advantageous to the other. Instead, a term is substantively unreasonable where the inequity of the term is so extreme as to shock the conscience."[36] The *Clark* majority concluded that the six-month limitations period was not so extreme that it shocked the conscience and enforced the provision as written.

The dissenting judge in *Clark* concluded that the provision was substantively unconscionable. Judge Neff noted that, unlike the case in *Rory,* no statutory safeguards, such as the review for reasonableness by the Commissioner, exist to evaluate shortened periods of limitation contained in an employment application. Judge Neff also stated, when calling into question the fact that the shortened period of limitations was obtained through an employment application: "There is nothing in the courts' reasoning to prevent all employers in Michigan from now simply inserting the judicially approved six-month limitations period in preprinted employment application forms, effectively 'legislating by imposition' a new severely shortened limitations period for employment-related claims."[37]

The Future of the Reasonableness Doctrine in Michigan

While the prohibition orders of the Commissioner address the application of *Rory* to insurance policies for uninsured/underinsured motorist benefits, abrogation of the "rule of *Camelot*" continues to apply to cases outside that context. The Michigan Court of Appeals recently concluded that *Rory* is a "complete break from solid, longstanding law in this state" and held that the decision is only to be applied prospectively.[38] Nonetheless, after *Rory,* absent statutory authority, a court may evaluate the "reasonableness" of shortened periods of limitations only if a traditional contract defense, such as substantive unconscionability, allows such an analysis. The decision in *Clark* highlights the marked difference in the "reasonableness" inquiry available under the three-pronged "rule of *Camelot*" versus a substantive unconscionability argument,

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which requires that the shortened period be so extreme as to shock the conscience.

Interestingly, the majority opinions in both the *Rory* and *Clark* cases indicated that possible restoration of a version of the "rule of *Camelot*" lies with the Michigan legislature. As noted in *Rory,* when determining the validity of a covenant not to compete in an employment setting, MCL 445.774a allows a court to determine if such agreement is "reasonable as to its duration, geographical area, and the type of employment or line of business."[39] The *Clark* decision expressed "sympathy for the dissent's argument that there ought to be limitations on an employer's ability to contractually modify periods of limitation, especially in the civil rights context," but reasoned that creating such a rule is within the ambit of the Michigan legislature, not the judiciary.[40]

Conclusion

While this article has addressed judicial application of the reasonableness doctrine in cases involving shortened periods of limitations, the *Rory* majority did not limit its holding to only cases of that type. Therefore, the current status of the law in Michigan is that unambiguous contractual terms must be enforced by the court as written, without an analysis of the reasonableness of such terms, unless (1) statutory authority to conduct such an analysis exists or (2) under a traditional contract defense, such as substantive unconscionability, reasonableness is a factor. *Rory* abolished the three-pronged test previously used to evaluate shortened periods of limitation—the "rule of *Camelot.*" It appears that any resurrection of this rule—a "return to *Camelot*"—depends on action by the Michigan legislature. ◆

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Footnotes

1. *Rory v Continental Ins Co,* 473 Mich 457; 703 NW2d 23 (2005).
2. *Camelot Excavating Co, Inc v St Paul Fire & Marine Ins Co,* 410 Mich 118; 301 NW2d 275 (1981).
3. *Tom Thomas Org, Inc v Reliance Ins Co,* 396 Mich 588; 242 NW2d 396 (1976).
4. *Camelot,* 440 Mich at 126, citing *Tom Thomas,* 396 Mich at 592, which in turn cited Anno: *Validity of contractual time period, shorter than statute of limitations, for bringing action,* 6 ALR3d 1197 (1966).
5. *Camelot,* 410 Mich at 127.
6. *Id.* at 140–141 (Levin, J., concurring).
7. *Id.* at 141.
8. *Herweyer v Clark Hwy Services, Inc,* 455 Mich 14; 564 NW2d 857 (1997).
9. *Id.* at 16.
10. *Id.* at 17.
11. *Id.* at 24.
12. *Id.* at 18.
13. *Id.* at 21.
14. See Mamat, *An overview of employment agreements—Covenants not to compete and arbitration agreements,* 76 Mich B J 1090 (1997).
15. *Rory,* 473 Mich at 462–463 and n 2, citing *Rory v Continental Ins Co,* 262 Mich App 679; 687 NW2d 304 (2004).
16. *Rory,* 473 Mich at 468.
17. *Id.* at 468–470.
18. *Id.* at 470.
19. *Id.* at 471, quoting *Camelot,* 410 Mich at 139.
20. *Rory,* 473 Mich at 474.
21. *Id.* at 477, 487–488 (emphasis in original).
22. *Id.* at 489.
23. *Id.* at 493 (Kelly, J., dissenting).
24. *Id.* at 498.
25. *Id.* at 507.
26. *Id.* at 513 (Cavanagh, J., dissenting).
27. *Id.* at 516–519 (Weaver, J., dissenting).
28. Michigan Department of Labor and Economic Growth, Office of Financial and Insurance Services (OFIS), Order No 05-060-M, entered December 16, 2005, available at <http://www.michigan.gov/documents/Prohibition_Order_121605_145496_7.pdf> and Order No 06-008-M, entered April 4, 2006, available at <http://www.michigan.gov/documents/prohibitiion_order_and_memo_156299_7.pdf> (each accessed November 2, 2006).
29. OFIS Order No 05-060-M, p 4, and OFIS Order No 06-008-M, p 4, both citing MCL 500.2236(5).
30. See *Rory,* 262 Mich App at 685–687.
31. OFIS Order No 05-060-M, p 5, and OFIS Order No 06-008-M, p 6.
32. See, e.g., *Myers v Western-Southern Life Ins Co,* 849 F2d 259 (CA 6, 1988), and *Timko v Oakwood Custom Coating, Inc,* 244 Mich App 234; 625 NW2d 101 (2001).
33. *Clark v DaimlerChrysler Corp,* 268 Mich App 138; 706 NW2d 471 (2005).
34. See also *Verdichizzi v Wright & Filippis, Inc,* unpublished opinion per curiam of the Court of Appeals, issued November 10, 2005 (Docket No 261680); 2005 LEXIS Mich App 2786 (2005).
35. *Clark,* 268 Mich App at 142.
36. *Id.* at 144 (citation omitted).
37. *Id.* at 156 (Neff, J., dissenting).
38. *West v Farm Bureau Gen Ins Co (On Remand),* 272 Mich App 58, 68; ___ NW2d ___ (2006).
39. MCL 445.774a, cited in *Rory,* 473 Mich at 475 n 32.
40. *Clark,* 268 Mich App at 142 n 2.