

# PLAIN MEANING, EXTRINSIC EVIDENCE, AND AMBIGUITY: MYTH AND REALITY IN INSURANCE POLICY INTERPRETATION

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*Insurance coverage disputes are mostly about the correct interpretation of an insurance policy provision. But three myths confuse and confound thinking about the interpretation of insurance policies. The first myth is that an unambiguous insurance policy provision – a provision with a “plain” meaning – carries that meaning on its face. The second myth is that, if a policy provision has a plain meaning, then under the plain-meaning “rule,” sources of meaning outside the four corners of the insurance policy – sources “extrinsic” to the policy -- are not admissible to aid in interpreting the provision. The third myth is that ambiguous policy provisions are necessarily construed against the drafter, which in insurance is almost always the insurer. In reality, all three myths seriously oversimplify how interpretation takes place. The problem, however, is not that, in acting in ways that are inconsistent with the simplifying myths, the courts are undermining desirable rules by quietly following other, undesirable rules. On the contrary, we do not need to change the rules or practices that govern insurance policy interpretation; Rather, we need more clarity and a deeper understanding of the sophisticated, complex rules and practices that are actually in force and are actually applied in practice. This Article aims to provide both.*

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## INTRODUCTION

Insurance coverage disputes are mostly about the correct interpretation of an insurance policy provision.<sup>1</sup> The heated controversy that took place over a period of years at the American Law Institute (“ALI”) regarding the interpretation provisions of the Restatement of the Law of Liability Insurance (“RLLI”)<sup>2</sup> reflects the crucial role that the rules governing interpretation play in coverage disputes. In 2017, the ALI membership approved a rule that for several years had been included in drafts of the RLLI, permitting the introduction of extrinsic evidence, without limit, in order to determine whether a policy provision is ambiguous.<sup>3</sup> But the following year there was an about face. The Reporters recommended and the ALI adopted an amendment embodying the plain-meaning rule, which precludes the introduction of extrinsic evidence if the meaning of a policy provision is plain on its face.<sup>4</sup> This rule, and the entire RLLI, are now final.<sup>5</sup>

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<sup>1</sup> A quick glance at any of the principal insurance law casebooks confirms that this is the case. *See generally*, KENNETH S. ABRAHAM & DANIEL SCHWARCZ, *INSURANCE LAW & REGULATION* (6th ed. 2015); TOM BAKER & KYLE D. LOGUE, *INSURANCE LAW AND POLICY: CASES AND MATERIALS* (3d ed. 2013); LEO P. MARTINEZ & DOUGLAS R. RICHMOND, *CASES AND MATERIALS ON INSURANCE LAW* (8th ed. 2018); JEFFREY W. STEMPEL ET AL., *PRINCIPLES OF INSURANCE LAW* (4th ed. 2011).

<sup>2</sup> RESTATEMENT OF THE LAW OF LIABILITY INSURANCE (AM. L. INST., Proposed Final Draft No. 2, 2018) [hereinafter RLLI].

<sup>3</sup> *Id.* at § 3(2). This Section also provided for a presumption in favor of the plain meaning (if any) of the provision. This presumption had no explicit support in the case law. Rather, the minority, contextual rule, is that extrinsic evidence is admissible, but with no presumption in favor of plain meaning, to demonstrate that a provision that is unambiguous on its face contains a “latent” ambiguity. *Id.* at § 3 cmt. a; *see also* *City of Gross Pointe Park v. Michigan Mun. Liab. Pool*, 702 N.W. 2d 106, 113 (Mich. 2005); *Brown Mech. Contractors, Inc. v. Centennial Ins. Co.*, 431 So. 2d 932, 942 (Ala. 1983).

<sup>4</sup> RLLI § 3.

<sup>5</sup> *See, e.g., Eyeblander, Inc. v. Fed. Ins. Co.*, 613 F.3d 797, 802 (8th Cir. 2010) (stating that “[t]he plain meaning of tangible property includes computers....”).

This extended controversy, and the limitations of the restatement form, however, obscured and oversimplified both the rules governing interpretation and the process of interpretation that the rules govern.<sup>6</sup> In fact, the whole controversy was emblematic of three simplifying myths that confuse and confound thinking about the interpretation of insurance policies. The first myth is that an unambiguous insurance policy provision – a provision with a “plain meaning” – carries that meaning on its face. In reality, many policy provisions are accorded a plain meaning through an active process of interpretation. Courts often do not simply *receive* a plain meaning by reading an insurance policy. Rather, they actively *construct* that single, “plain” meaning.

The second myth is that, if a policy provision has a plain meaning, then under the plain-meaning rule, sources of meaning outside the four corners of the insurance policy – sources “extrinsic” to the policy -- are not admissible to aid in interpreting the provision.<sup>7</sup> In reality, important sources of meaning outside of an insurance policy may be considered, and often are considered, in interpreting policy provisions that courts then hold have an unambiguous, plain meaning.<sup>8</sup>

The third myth concerns ambiguous policy provisions – those that are reasonably susceptible to two different interpretations. Under the doctrine *contra proferentem* (“against the offeror” or drafter),<sup>9</sup> ambiguous policy provisions are supposedly construed against the drafter, which in insurance is almost always the insurer.<sup>10</sup> In reality, a finding of ambiguity merely authorizes the introduction of otherwise-inadmissible extrinsic evidence to aid in interpreting the ambiguous provision.<sup>11</sup> In addition, in

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<sup>6</sup> The RLLI did not fall prey to these myths, but the necessary requirements of both brevity and format (black-letter rules followed by concise “comments”) limited its capacity to dispel them, and foreclosed the kind of extended analysis undertaken here.

<sup>7</sup> See ROBERT H. JERRY II & DOUGLAS R. RICHMOND, UNDERSTANDING INSURANCE LAW 121 (6th ed. 2018) (describing this view without endorsing it).

<sup>8</sup> RLLI § 3 cmt. b.

<sup>9</sup> See ABRAHAM & SCHWARCZ, *supra* note 1, at 41; RESTATEMENT (SECOND) OF CONTRACTS §206 (1981) (providing for interpretation “against the Draftsman”).

<sup>10</sup> JERRY & RICHMOND, *supra* note 7 at 127, and at n.305 (identifying this view and citing courts adopting it).

<sup>11</sup> See RLLI § 4 cmt. b.

reality, even when the provision remains ambiguous after such extrinsic evidence is considered, the courts do not necessarily construe the provision in favor of coverage.<sup>12</sup>

In my view, what occurs in reality in all three respects is perfectly acceptable. The problem is not that, in acting in ways that are inconsistent with the simplifying myths, the courts are undermining desirable rules by quietly following other, undesirable rules. On the contrary, the problem is that statements the courts and commentators make often oversimplify the rules that are actually being applied, and thereby perpetuate misconceptions about the realities of insurance policy interpretation. We do not need to change the rules or practices that govern insurance policy interpretation; we need more clarity and a deeper understanding of the sophisticated, complex rules and practices that are actually in force and are actually applied in practice.<sup>13</sup>

This Article aims to provide both greater clarity and a deeper understanding of these rules and practices. Part I sets the stage for the analysis by distinguishing interpretation of insurance policies from both application of the policy to a claim, and construction of the policy in order to determine its legal effect. Because the plain-meaning rule applies only to interpretation, these distinctions are crucial. Part II explores the nature of insurance policy interpretation and the process of determining that policy provisions have a plain meaning by consulting the “whole” policy. The underlying insight that emerges is how active the process of arriving at a “plain” meaning can be, even when nothing “extrinsic” to an insurance policy is expressly taken into consideration.

Part III then considers the seemingly contradictory practice of expressly and openly considering certain matters that are extrinsic to the policy, even on the part of courts that follow a “strict” plain-meaning rule.

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<sup>12</sup> See discussion *infra* Section IV.B.

<sup>13</sup> The insurance law with which this Article is concerned is, in effect, insurance *contract* law. Many of the rules and concepts of insurance law are drawn straightforwardly from the law of contract interpretation. Others, however, are distinctive to insurance law, or find their most detailed elaboration and application in insurance law. In most instances there is little to be gained here from identifying in detail which rules replicate conventional contract law and which rules are distinctive to insurance law, although I will indicate important differences where appropriate, and will cite general principles of contract law when they are applicable.

Here I argue that this practice is not at all contradictory, because the matters these courts routinely consider are extrinsic to the policy but are not “evidence.” The plain-meaning rule, it turns out, is not really about plain meaning, but about which sources may be considered in determining whether a policy provision has a single reasonable meaning.

Finally, Part IV examines interpretation and construction when a policy provision is ambiguous. I show that the strong *stare decisis* effect accorded to the interpretation and construction of ambiguous policy provisions, as well as the notion that policy provisions that remain ambiguous even in the face of extrinsic evidence are automatically construed in favor of coverage, are both open to question. In short, this ambiguity about ambiguity needs examination.<sup>14</sup>

## I. INTERPRETATION, APPLICATION, AND CONSTRUCTION

Courts perform three functions relating to the meaning of insurance policies. *Interpretation* is the process of determining meaning.<sup>15</sup> *Application* is the process of determining whether, given the meaning of the relevant policy provision or provisions, a claim for coverage involving particular facts and circumstances is or is not covered. *Construction* is the process of determining the legal effect of an insurance policy,<sup>16</sup> which may or may not

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<sup>14</sup> Over twenty years ago, I developed a conceptual framework for analyzing the factors that could influence courts’ determinations that policy provisions are ambiguous, and of the consequences of these determinations. See Kenneth S. Abraham, *A Theory of Insurance Policy Interpretation*, 95 MICH. L. REV. 531 (1996). In a sense, this Article is an extension of that framework to the particular issue of the *evidence* that is relevant to the plain-meaning/ambiguity issue, identifying factors bearing on this issue at a level of detail that my general theory did not encompass. I note at several points below where there is resonance with the earlier Article. In addition, Part IV (C) adds a factor relevant to ambiguity (ambiguity as a “trap”) that I had not recognized at that time.

<sup>15</sup> RESTATEMENT (SECOND) OF CONTRACTS §200 (AM. L. INST. 1979); E. ALLAN FARNSWORTH, FARNSWORTH ON CONTRACTS §7.08 (Zachary Wolfe ed., 4th ed. 2019).

<sup>16</sup> Edwin W. Patterson, *The Interpretation and Construction of Contracts*, 64 COLUM. L. REV. 833, 835 (1964).

coincide with its meaning as determined by interpretation. The plain-meaning rule governs interpretation, not application or construction.

#### A. INTERPRETATION

The plain-meaning rule prohibits considering extrinsic evidence of a policy provision's meaning when the policy provision has a plain meaning on its face.<sup>17</sup> By its terms, then, the rule only governs interpretation – the determination of meaning. The dominance of the plain-meaning rule in insurance contrasts starkly with general contract law, where the dominant approach is to permit the introduction of extrinsic evidence to aid interpretation.<sup>18</sup> Interpretation is a matter for the court, unless it depends on factually-disputed issues.<sup>19</sup>

It is sometimes said that a policy provision may be ambiguous in a particular context but unambiguous in another context.<sup>20</sup> The logical implication of such statements is that the provision has a plain meaning in one context but not a plain meaning in another context.<sup>21</sup> For example, CGL insurance policies typically contain a provision that excludes coverage of liability for damage to property in the “care, custody or control” of the insured.<sup>22</sup> It may be indisputable that an insured holding an item of personal

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<sup>17</sup> See RLLI §3.

<sup>18</sup> There is a plain-meaning rule in the general law of contracts, but many jurisdictions have rejected it, even while adopting the plain-meaning rule for insurance contracts. *Id.* at cmt a; JOSEPH M. PERILLO, *CONTRACTS* §3.10 at 136 (7th ed. 2014). The “modern” view in general contract law expressly permits the introduction of many forms of extrinsic evidence regardless of ambiguity. *RESTATEMENT (SECOND) OF CONTRACTS* §202 (AM. LAW INST. 1979) (providing that contracts are to be interpreted “in light of all the circumstances”) and §202(4)-(5) (providing that interpretation is to take place as consistent with relevant course of performance or dealing and usage of trade). In addition, evidence of prior negotiations is admissible to establish the meaning of the contract under many conditions. *Id.* at §214(c) It would be only a slight exaggeration, therefore, to say that there is no plain-meaning rule under the *RESTATEMENT (SECOND) OF CONTRACTS*.

<sup>19</sup> See RLLI §2(2); *RESTATEMENT (SECOND) OF CONTRACTS*, *supra* note 9, at §212(2).

<sup>20</sup> See, e.g., ABRAHAM & SCHWARCZ, *supra* note 1, at 45.

<sup>21</sup> See RLLI §3 cmt. f.

<sup>22</sup> ABRAHAM & SCHWARCZ, *supra* note 1, at 443.

property in his arms has the property in his “care, custody or control.” The provision therefore has a plain meaning in this context. On the other hand, whether a parcel that has been delivered and left on the doorstep of the insured is in the insured’s “care, custody or control” may be debatable. The provision arguably does not have a plain meaning in this context.

A different way of making this point would be to say that the “care, custody or control” exclusion has a plain meaning “as applied” to the claim involving personal property held in the insured’s arms, but is ambiguous “as applied” to the parcel left on the insured’s doorstep. There is nothing wrong with this alternative formulation in itself, but it does risk confusing the process of interpretation with the process of application. Under the plain-meaning rule, extrinsic evidence would not be admissible to interpret – to determine the meaning of – the “care, custody or control” exclusion, whether in the abstract or “as applied” to either of these claims for coverage. However, as indicated next, extrinsic evidence about either claim would be admissible to aid in the application of an interpretation made under the plain-meaning rule to a particular claim.

#### B. APPLICATION

The plain-meaning rule does not preclude the introduction of all extrinsic evidence. There is no prohibition on the admission of extrinsic evidence in order to apply a policy provision to a claim for coverage. For example, without evidence of the facts associated with a claim, the policy could not be applied to a claim. In my earlier hypothetical, evidence of the number of steps from the walkway up to the door of the insured’s home would be admissible, because this evidence would not bear on the meaning of the “care, custody or control” exclusion. Thus, extrinsic evidence is not admissible regarding the major premise of the interpretive syllogism (i.e., “custody means...”), whereas extrinsic evidence regarding the minor premise (“a parcel was left on the insured’s doorstep under the following conditions...”) is admissible. And this kind of evidence – that the insured suffered a loss, the conditions under which the loss occurred, the amount of the loss, and so forth – is necessarily extrinsic to the policy.<sup>23</sup>

It is undoubtedly true that, in the course of applying a policy provision to the facts of a claim, interpretation sometimes must occur. But this is not inconsistent with the distinction between interpretation and application. Interpretation does not have to be completed before application begins, in order still to constitute interpretation. Policy provisions may seem

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<sup>23</sup> See RLLI § 2 cmt. f.



to have a meaning in the abstract or in general that must be adjusted in the course of application, or provisions may have a meaning that is too abstract or too general to determine whether a claim is covered, until the particular facts and details of a claim are known. The interpreting court can take these claim-related facts into account in determining the meaning of the policy provision to be applied to these facts, or in sharpening that meaning in light of these particular facts. This does not violate the plain-meaning rule. What matters is that the facts of the claim, and any other extrinsic evidence that is admitted, be only a *predicate* to determining meaning, not a *source* of meaning.

Thus, the process of applying the meaning of a policy provision to the facts of a claim cannot always be altogether divorced from the *act* of interpretation, but it can be divorced from the *concept and function* of interpretation. An interpretation, standing alone, is like a rule – its meaning has a level of generality that is not necessarily self-applying, any more than legal rules are always self-applying. And just as applying a legal rule to a set of facts sheds light on the meaning of the rule, so the effort to apply the interpretation of a policy provision to a claim may sometimes shed additional light on the meaning of the provision.

Applying an interpretation to a claim may involve an implicit act of mini-, or concrete, interpretation. For example, if an auto liability insurance policy covers liability for injury “arising out of the use” of an auto, determination that “use” means to drive or otherwise employ would not automatically resolve the questions whether “use” includes throwing a firecracker out the window of a parked car.<sup>24</sup> Application of the term “use” to this set of facts requires what amounts to further interpretation in this concrete circumstance. The interpretation may be only implicit in the result, or the court may explain why these facts do or do not constitute a “use,” thus expressly interpreting that term in this particular context. The combination of a series of applications to similar claims involving slightly different facts may produce what amounts to a more detailed interpretation of the term “use.” But the facts of the claim in these situations serve only as a predicate to, not a source of, the interpretation.

Similarly, in *Stone Container Corp. v. Hartford Steam Boiler Inspection and Ins. Co.*,<sup>25</sup> a boiler and machinery insurance policy excluded coverage of losses caused by explosion, with an exception for losses caused

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<sup>24</sup> See *Farm Bureau Mut. Ins. Co. v. Evans*, 637 P.2d 491, 494 (Kan. Ct. App. 1981).

<sup>25</sup> 165 F.3d 1157 (7th Cir. 1999).

by explosion of an “object of a kind described below.” Included in the list objects described below were “(1) Steam boiler” and “(2) Electric steam generator.” The policyholder made a claim for coverage of a loss resulting from the explosion of a pulp digester. The court held that these policy provisions were unambiguous, and that a pulp digester did not satisfy the requirement that it be “of a kind” with the listed objects, because (although a pulp digester was “closest to a steam boiler”), a steam boiler creates steam by boiling water, whereas the steam in a pulp digester is generated outside and then fed into the digester.<sup>26</sup>

Although the court’s opinion (by Posner, J.) did not recount the court’s thought process, it seems highly likely that the court did not first determine in the abstract what kinds of objects were “of a kind” with those listed, and only after determining what characteristics these objects had in common, then turn to the facts of the claim to identify the characteristics of pulp digesters. Rather, in all probability the court attributed a provisional meaning to the policy provision, looked at the record evidence and thought about the characteristics of pulp digesters, reflected again about the meaning of the policy provision, and through this process of provisional interpretation and provisional application, arrived at a conclusion that applied the now better-understood meaning of the provision to the claim for coverage of losses caused by the pulp digester’s explosion. Interpretation of the provision and application of the meaning arrived at through interpretation to the pulp digester involved an iterative, or reflexive, process.

When both interpretation and application are matters for the court, then all this is mainly a matter of nomenclature, for both are then subject to appellate review. In contrast, when interpretation is for the court but application, even in the absence of a dispute about the empirical facts, is a question of fact (as it is in a minority of jurisdictions<sup>27</sup>), then applications, including the concrete interpretations that follow from application, may vary from case to case, even when the relevant facts are identical. If application is a question of fact, then some explosions of pulp digesters will be covered, and some will not be covered, by the same insurance policy that was at issue in *Stone Container*, depending on the application of the policy language by the trier of fact in each individual case.

This seems undesirable, in light of the fact that standard-form insurance policies should provide the same coverage to identically-situated insureds. The dominant, and I think preferable, approach, is therefore for

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<sup>26</sup> *Id.* at 1160.

<sup>27</sup> *See* RLLI § 2 cmt. f.

both interpretation and application to be matters for the court. When application depends on the resolution of a purely empirical dispute (*e.g.*, whether this pulp digester generated its own steam), the need for a finding of fact can be satisfied by asking the jury to bring in a special verdict, to be followed by the court's applying its interpretation to the factual findings contained in the that verdict.

The central point, however, is that the facts of a claim are not, and may not be permitted to be, a source of meaning. Rather, these facts may stimulate and focus the court's thinking about the meaning of the relevant policy provision on its face, and about the proper application of this meaning to the claim. The two functions, interpretation and application, are logically and conceptually distinct, even when they occur in an iterative sequence and the facts of the claim help to inform the court's thinking. Interpretation is logically prior to application, even when the two are temporally mixed.

### C. CONSTRUCTION

Interpretation must also be distinguished from construction, which is the process of determining the legal effect of a policy provision, or any other contract.<sup>28</sup> A policy provision can have one meaning (or more than one) but a different legal effect. *Contra proferentem* is a rule of construction, addressing the legal effect of ambiguous policy language. Similarly, the rule that policy language that affirmatively provides coverage should be construed broadly, and language (such as an exclusion) restricting coverage should be construed narrowly is, as it states, a rule of construction.<sup>29</sup> Whether this rule is anything other than an application of *contra proferentem* is not entirely clear, since some courts appear not to treat it this way, but that question is not pertinent here. And the invalidation of a policy provision on the ground that it violates public policy—for example, by covering liability for punitive damages<sup>30</sup>—is likewise an act of construction rather than interpretation.

Construction is sometimes camouflaged as interpretation, either unintentionally or deliberately, in order to obscure the extent of a court's

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<sup>28</sup> *Id.* §2 cmt. (g); FARNSWORTH, *supra* note 15, § 7.08.

<sup>29</sup> See JERRY & RICHMOND, *supra* note 7, at 127.

<sup>30</sup> See generally *Hartford Cas. Ins. Co. v. Powell*, 19 F. Supp. 2d 678 (N.D. Tex. 1998).

lawmaking.<sup>31</sup> This kind of conflation of the two functions can lead to uncertainty about what rules govern interpretation. A prominent example involves the letter sent to insurance commissioners in the early 1970s by insurance industry rating bureaus seeking state regulatory approval of the incorporation of a qualified “pollution exclusion” into the standard-form Comprehensive General Liability (CGL) insurance policy of the period. The proposed provision excluded coverage of liability for bodily injury or property damage caused by the discharge of pollutants, but contained an exception for discharges that were “sudden and accidental.” Some years after the exclusion was approved, policyholders contended in coverage disputes that, among other things, this letter’s assertions about the meaning and effect of the exception to the exclusion were misleading, and that insurers should therefore be estopped to assert that the term “sudden” had a temporal component.<sup>32</sup>

This is best understood as an argument about the proper construction of the term “sudden,” not about the interpretation of that term. The argument was, in effect, that even if the plain meaning of “sudden” within the four corners of the policy included a temporal component, the policy should not be enforced to give the provision its plain, temporal meaning. Because construction in such instances is a judicial intervention upsetting the meaning of a policy provision, courts may sometimes understandably be reluctant to acknowledge that they are engaged in construction rather than interpretation. Extrinsic evidence, such as the letter to insurance commissioners, should be admissible as relevant to construction, even when it is not admissible for purposes of interpretation. Confusing or conflating the two processes risks obfuscating the rule regarding the evidence that may be considered when interpretation, and not construction, occurs.

## II. PLAIN MEANING AND THE “WHOLE” POLICY

Courts following the plain-meaning rule do not merely stare at the words of a policy provision in order to determine whether the provision is ambiguous, or to determine what the provision means once they conclude that it is not ambiguous. Thus, plain meaning is not a self-evident fact. The

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<sup>31</sup> *See, e.g.*, FARNSWORTH, *supra* note 15, §7.08, at 7-75 (stating that courts “have more often ignored [this distinction] by characterizing the process of ‘construction’ as that of ‘interpretation’ in order to obscure the extent of their control over private agreement”).

<sup>32</sup> For discussion of this multi-year episode, *see* American States Ins. v. Koloms, 687 N.E. 2d 72, 79-82 (Ill. 1997).

conclusion that a policy provision has a plain meaning is itself the result of an interpretive process that is not always simple or one-dimensional. Typically, a plain meaning does not find the court. Rather, the court finds a plain meaning. It turns out that there is a lot more to plain meaning, and to the plain-meaning rule, than meets the eye.

A frequent formulation of the prohibition on the admission of extrinsic evidence is that the court must stay within the “four corners” of the policy in determining the meaning of the disputed provision.<sup>33</sup> Of course, if in doing so the court determines that the provision is not ambiguous, it has simultaneously determined the plain meaning of the provision, because an unambiguous policy provision is one that has only a single reasonable meaning.

The four-corners limitation reveals little, however, about how active the process of interpretation that is confined in this way actually is permitted to be, and often is. The material within the four corners of the policy is, obviously, the whole policy. The plain-meaning rule therefore not only permits consulting the whole policy to determine the meaning of a particular provision; it would be imprudent not to consult the whole policy in doing so.

Just as courts do not stare at a policy provision in order to determine if it has a plain meaning, they do not merely read the whole policy to help determine the meaning of a particular provision. First, a set of normative presumptions about how the “whole” insurance policy has been constructed and functions serve to guide interpretation of policy provisions whose meaning might otherwise be in doubt. Second, the canons of interpretation – which surprisingly have not been recognized to be directly about the relevance of the “whole” policy or contract – often provide strong direction about the significance of other provisions or terms in the policy for a disputed provision’s meaning.

#### A. THREE NORMATIVE PRESUMPTIONS ABOUT THE “WHOLE” POLICY

Both the general injunction to read the policy as a whole<sup>34</sup> and the canons of interpretation do more than confirm that the meaning of one policy

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<sup>33</sup> See, e.g., JERRY & RICHMOND, *supra* note 7, at 121.

<sup>34</sup> The notion that the whole contract is to be considered is a principle of both general contract law and insurance law. See RLLI § 3 cmt. g; RESTATEMENT (SECOND) OF CONTRACTS §202(2); National Union Fire Ins.

provision can shed light on the meaning of another provision. These principles of interpretation also reflect the notion that an insurance policy is a functioning mechanism, containing different parts that work together. Recognizing the functional quality of insurance policies reveals three features of the “whole” policy that are reflected in the courts’ approach to the interpretation of insurance policies.

These are the soft presumptions of consistency, coherence, and non-redundancy. The courts often do not state that they are following or invoking these presumptions, in part because the presumptions are so fundamental as to be almost transparent. But the courts follow them, nonetheless. This is because an insurance policy is not only a contract, but a communication of the terms of the contract to the parties and to the courts. The courts assume that, other things being equal, the parties have attempted not to contradict or unnecessarily repeat themselves, because these are features of effective and rational communication.

Nonetheless, because language is an imperfect instrument of communication, and the drafters of insurance policies sometimes imperfectly employ this imperfect instrument, the provisions contained in insurance policies are not always consistent, coherent, and non-redundant. For this reason, in practice the presumption that insurance policies have these characteristics are soft presumptions only, working propositions with an “other things being equal” quality to them.

### 1. Consistency

The strongest presumption is that policy provisions do not contradict each other. There is obviously something of a continuum running from complete consistency among policy provisions, to mere coherence, to lack of coherence, and finally to outright contradiction. There is at least a qualitative difference between an interpretation that avoids outright contradiction and one that goes further, by ensuring coherence among policy provisions. A policy provision may be out of keeping with the remainder of an insurance policy without directly contradicting another provision. In this situation a provision that does not cohere with the remainder of the policy could nonetheless be interpreted without the other provisions failing to function. But outright contradiction would render at least one of two inconsistent provisions inoperative. Insurers that draft standard-form

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Co. v. Fed. Ins. Co., 213 F. Supp. 3d 1333, 1340 (D. Colo. 2016); Progressive Cas. Ins. Co. v. Fed. Deposit Ins. Co., 80 F. Supp. 3d 923, 946 (N.D. Iowa 2015).

policies do not intend to include contradictory provisions in their policies, nor would policyholders intend to purchase a policy containing contradictory provisions.

It is for this reason, I think, that cases involving outright contradiction are rare.<sup>35</sup> When there is a real contradiction, the courts tend to hold that the conflict between two unambiguous, contradictory provisions creates an ambiguity. For example, in *Rusthoven v. Commercial Standard Ins. Co.*,<sup>36</sup> a policy contained two contradictory Endorsements. The court held that the contradiction created ambiguity, and interpreted the policy against its drafter, the insurer.<sup>37</sup> I have not found any case in which a party argued in favor of an interpretation that would blatantly contradict the plain meaning of another provision without asserting that the result was ambiguous policy language. Rather, the argument made in such situations is that the policy is ambiguous.

The virtually complete absence of cases in which the plain meaning of one policy provision is given precedence over the plain meaning of another provision that contradicts it, without a holding of ambiguity, is evidence of how powerful the presumption of consistency is. No one argues for an interpretation that would contradict the plain meaning of another policy provision, both because insurers try mightily not to draft contradictory language, and because the presumption of consistency is so strong. Reconciling apparent inconsistency is the name of the game.

## 2. Coherence

A second principle that follows from the notion that an insurance policy is a functional vehicle of communication that should be read as a whole is that a policy is likely to be coherent.<sup>38</sup> This means that, when a provision can be read to cohere with the other provisions in the policy, it

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<sup>35</sup> See, e.g., *PBM Nutritionals, LLC v. Lexington Ins. Co.*, 724 S.E.2d 707, 712-13 (Va. 2012) (rejecting contention that two policy provisions were in conflict).

<sup>36</sup> 387 N.W.2d 642 (Minn. 1986).

<sup>37</sup> *Id.* at 644-45.

<sup>38</sup> *But see In re SRC Holding Corp.*, 545 F.3d 661, 668 (8th Cir. 2008) (stating that “whether policy coverage ‘makes sense’ as a business matter is largely irrelevant....”).

should be read to cohere.<sup>39</sup> Presuming coherence is not the same as interpreting to avoid direct contradiction. There may be no literal or actual contradiction or inconsistency between one provision and the entire remainder of the policy, but one interpretation of a provision might nonetheless be out of keeping with the remainder.<sup>40</sup>

For example, in *Liristis v. American Family Ins. Co.*,<sup>41</sup> the insureds' home was contaminated by mold, apparently as a result of water used to extinguish a fire at the property. Their homeowners insurer denied coverage, relying on an exclusion providing that the policy did not cover "loss to the property...resulting directly or indirectly or *caused* by any one or more of the following...c. smog, rust, corrosion, frost condensation, mold wet or dry rot..."<sup>42</sup> The court held that the loss was not excluded, because the mold contamination was not a cause of loss, but the loss itself. It would not have contradicted this language to hold that the mold contamination was excluded. It would have been plausible to hold that mold contamination resulted from mold. But the policy language did distinguish between the cause of a loss and the loss itself. The court's holding in effect took the position that the exclusion in question should be interpreted so as to be coherent with the policy's distinction between causes of loss, on the one hand, and loss itself, on the other hand.

### 3. Non-redundancy

The softest presumption arising out the injunction that an insurance policy should be read as a whole is that policy language is not redundant – that every provision in a policy has an independent meaning.<sup>43</sup> Every

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<sup>39</sup> The principle that every provision should be accorded some meaning is an aspect of this notion. *See, e.g.*, *Bedford Internet Office Space, LLC v. Travelers Ins. Co.*, 41 F. Supp. 3d 535, 547 (N.D. Tex. 2014) (interpreting a policy so as to avoid rendering a policy provision of no effect).

<sup>40</sup> *See, e.g.*, *S. Tr. Ins. Co. v. Phillips*, 474 S.W.3d 660, 669 (Tenn. Ct. App. 2015) (holding that policy's consistently drawing a distinction between fire, on the one hand, and vandalism and malicious mischief, on the other hand, was significant).

<sup>41</sup> 61 P.3d 22 (Ariz. 2002).

<sup>42</sup> *Id.* at 24 (emphasis added).

<sup>43</sup> This is a general principle of contract law interpretation. *See* RESTATEMENT (SECOND) OF CONTRACTS § 229 (AM. LAW INST. 1981); FARNSWORTH, *supra* note 15, §7.13.



provision, that is, is presumed to do work and to be a necessary part of the policy.<sup>44</sup>

The reason this presumption is so soft is that it is in tension with a counter-tendency that also is sometimes exhibited by the drafters of insurance policies. This is the practice of sometimes including duplicative provisions in order to ensure or emphasize the importance of a limitation on coverage. This is the familiar “belt and suspenders” approach that is employed in the drafting of many legal documents.<sup>45</sup> Because the drafters want to avoid uncertainty, as well as the disputes and litigation that uncertainty may yield, they sometimes include duplicative provisions out of an excess of caution.

For example, in *TMW Enterprises v. Federal Ins. Co.*, the policyholder argued that the insurer’s interpretation of an all-risk property insurance policy rendered the “ensuing loss” in the policy “superfluous, empty words with no independent function.”<sup>46</sup> The court responded with an interpretation that gave the clause an independent meaning, but then continued: “But even if we choose to label this type of drafting a form of redundancy, which we do not think it is, that label surely is not a fatal one when it comes to insurance contracts, where *redundancies abound*.”<sup>47</sup> That phrase seems to have resonated with subsequent courts. It has since been cited in a number of opinions addressing putative redundancies in insurance policies.<sup>48</sup>

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<sup>44</sup> See, e.g., *Phoenix Ins. Co. v. Infogroup, Inc.*, 147 F. Supp. 3d 815, 822 (S.D. Iowa 2015) (stating that “The Court interprets undefined words in the context of the policy as a whole, and avoids interpreting the policy in such a way as to render parts of a contract ‘surplusage’”); *Northrup Grumman Corp. v. Factory Mut. Ins. Co.*, 805 F. Supp. 2d 945, 951 (C.D. Cal. 2011) (applying the principle of non-redundancy).

<sup>45</sup> See, e.g., *Cactus Ave., LLC v. Fid. & Guar. Ins. Co.*, No. E051787, 2012 WL 649966, at \* 4 (Cal. Ct. App. Feb. 28, 2012) (indicating that “Here, similarly, an insurer could understandably want to take a ‘belt-and-suspenders’ approach and thus exclude losses under the seepage exclusion, the water exclusion, or both”); *In re SRC Holding Corp.*, 545 F.3d 661, 670 (8th Cir. 2008) (“nothing prevents the parties from using a belt and suspenders approach in drafting the exclusions, in order to be doubly sure”).

<sup>46</sup> *TMW Enters. v. Fed. Ins. Co.*, 619 F.3d 574, 577 (6th Cir. 2010).

<sup>47</sup> *Id.* (emphasis added).

<sup>48</sup> See, e.g., *Ardente v. Standard Fire Ins. Co.*, 744 F.3d 815, 819 (1st Cir.

## B. The Canons of Interpretation

The function of a series of “canons” of interpretation, well known in contract law generally, is to identify a number of commonly-occurring relationships between or among provisions, and to specify the significance of these relationships. A number of the canons of interpretation are in fact directed primarily at the implications of the provisions in the remainder of the policy for the meaning of a disputed provision.<sup>49</sup>

For example, *expressio unius est exclusio alterius* directs that the expression of one thing should be considered the exclusion of another thing that is not expressed.<sup>50</sup> If a liability insurance policy provides that it covers liability for “damages,” it is a fair inference that the absence of any mention of liability for “restitution” implies that the latter is not covered.<sup>51</sup>

Similarly, the canon *eiusdem generis* indicates that where general language is accompanied by a list of examples, the general language is to be interpreted as referring to things of the same kind as are listed.<sup>52</sup> Thus, an exclusion of coverage of liability for injury or damage caused by “war,” including “undeclared or civil war,” as well as “warlike action by a military force,” and “insurrection, rebellion, [and] revolution” implies that the term “war” does not include terrorism.<sup>53</sup>

Finally, under the canon *noscitur a sociis*, the meaning of a word is to be understood by reference to the meaning of the words around it.<sup>54</sup> According to this canon, an exclusion referring to the “release” of pollutants, as part of a list referring to the “discharge, dispersal, release or escape” of

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2014); U.S. Liab. Ins. Co. v. Benchmark Constitution Servs., 797 F.3d 116, 123 (1st Cir. 2015).

<sup>49</sup> For discussion of the canons, see JOHN EDWARD MURRAY, JR., MURRAY ON CONTRACTS 470-71 (5th ed. 2011); 2 E. ALLEN FARNSWORTH, FARNSWORTH ON CONTRACTS 293-95 (3d ed. 2004).

<sup>50</sup> See MURRAY, *supra* note 49, at 471; Farnsworth, *supra* note 49, §7.13.

<sup>51</sup> ABRAHAM & SCHWARCZ, *supra* note 1, at 466. See also Old Republic Ins. Co. v. Stratford Ins. Co., 777 F.3d 74, 81 (1st Cir. 2015) (applying, in effect, *expressio unius*, by noting that the policy made reference to one feature of the insured’s business and notably did not refer to another feature).

<sup>52</sup> See MURRAY, *supra* note 49, at 471; FARNSWORTH, *supra* note 49, §7.13.

<sup>53</sup> See ABRAHAM & SCHWARCZ, *supra* note 1, at 469.

<sup>54</sup> See MURRAY, *supra* note 49, at 470.

pollutants, for example, would be interpreted to be listing means by which pollutants may be freed *from* confinement, and not to the deposit of pollutants *into* a place of confinement.<sup>55</sup>

In each of these situations, the application of a canon about the significance of other policy language helped to render unambiguous a policy provision that might otherwise be regarded as reasonably susceptible to two different interpretations. The meaning of “damages” was clarified by virtue of the absence of any reference to “restitution” in liability insurance policy; the term “war” was interpreted not to include “terrorism” because of the examples of “war” included in the policy; and the meaning of “release” was interpreted by reference to the list of similar terms surrounding it. In all three situations the canons were, in effect, applications of the more general injunction that the interpretation of a disputed policy provision should not occur in isolation from the rest of the policy. Rather, the policy is to be read as a whole.<sup>56</sup>

The lesson of my examination of the injunction to read the policy as a whole is that identification of a policy provision’s plain meaning is often an active process. The conclusion that a policy provision has a plain meaning means only that, based on the sources of meaning that may be consulted, the provision has a single reasonable meaning that must be deemed “plain” by virtue of the process of interpreting it. The plain-meaning rule is not about “plain” meaning, but about the sources that may be consulted to determine whether a policy provision has only one reasonable meaning. These observations about the complexity of the process of determining plain meaning are rendered all the more forceful once the matter that lies outside the four corners of the policy, but still may be considered under the plain-rule, are brought into view.

### III. EXTRINSIC SOURCES OF MEANING UNDER THE PLAIN-MEANING RULE

Even under the plain-meaning rule, courts routinely and expressly consult certain sources of meaning that are outside the four corners of the insurance policy. These include facts that are so fundamental that they do not

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<sup>55</sup> See, e.g., *Bd. of Regents v. Royal Ins. Co. of Amer.*, 517 N.W. 2d 888, 891 (Minn. 1994).

<sup>56</sup> See MURRAY, *supra* note 49, at 470; FARNSWORTH, *supra* note 49, §7.13.

even need to be articulated as sources of meaning; the “purpose” of a form of insurance coverage or a particular policy provision; dictionary definitions; other judicial decisions, statutes and regulations; and secondary legal sources.<sup>57</sup>

The RLLI notes in a comment that, although the majority of courts follow the plain-meaning rule, these courts sometimes differ about which sources outside an insurance policy may be considered in interpreting an unambiguous policy provision. In this sense, the RLLI suggests, it might be said that there is not a “single” plain-meaning rule. The differences, however, are minimal. A few plain-meaning courts have taken the position that evidence of custom, practice, and usage may be considered even in interpreting an unambiguous policy provision.<sup>58</sup> These courts seem to treat such matters as “legislative facts” of the sort I discuss below in Section C. But for the most part, courts that subscribe to the plain-meaning rule do not consider custom, practice, and usage when interpreting unambiguous policy provisions.

How is it that certain sources of meaning outside of the policy can be considered, notwithstanding the prohibition against considering extrinsic evidence? The answer is that each of the above sources of meaning may be considered, despite the fact that they lie outside the four corners of the policy, because they are form of “implicit” knowledge without which judicial reasoning could not take place; because they are facts subject to judicial notice; or because they are “legislative” facts that are not subject to the rules of evidence.

#### A. IMPLICIT KNOWLEDGE

Insurance policy provisions are not self-defining. Modern contract theory has long recognized that a particular interpretation may be simple, straightforward, and incontestable, but that it is an interpretation nevertheless, even when it is the only reasonable interpretation.<sup>59</sup> This is because the reader of a contract, such as an insurance policy, including the

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<sup>57</sup> See RLLI § 3 cmt. b.

<sup>58</sup> See, e.g., *Sunbeam Corp. v. Liberty Mut. Ins. Co.*, 781 A.2d 1189, 1193 (Pa. 2001); *Auto-Owners Ins. Co. v. Anderson*, 756 So. 2d 29, 36 (Fl. 2000); *Beazley Ins. Co., Inc. v. Ace American Ins. Co.*, 880 F. 3d 64, 69 (2d Cir. 2018); RLLI § 3 cmt. c.

<sup>59</sup> See FARNSWORTH, *supra* note 15, at §7.11 (arguing that it is questionable whether a word has a meaning at all when divorced from the circumstances).

judicial reader, always encounters contract language in a context, and always brings to bear what he or she already knows or supposes to be the relevant context when understanding – and therefore when interpreting – the meaning of that language. For the legal reader, this includes background understandings of the legal and insurance market contexts in which an insurance policy operates.

Sometimes courts expressly articulate the context in which the interpretive task is situated. But often that context is so transparent to courts, and courts expect that context to be so transparent to the legal readers to whom the court's opinion is mainly addressed, that it does not occur to the court that making explicit what is implicit in the court's reasoning is necessary. But logically, this context – which lies outside the four corners of the insurance policy -- is a source that contributes to the meaning of the policy provision being interpreted. As James Bradley Thayer noted in the first modern treatise on evidence over a century ago, "In conducting a process of judicial reasoning, as of other reasoning, not a step can be taken without assuming something which has not been proved; and the capacity to do this with competent judgement and efficiency, is imputed to judges and juries as part of their necessary mental outfit."<sup>60</sup>

I call these assumptions and sources of meaning "implicit knowledge." For example, many liability insurance policies cover liability incurred "because of" bodily injury or property damage.<sup>61</sup> To the best of my knowledge, no court has ever held this phrase to be ambiguous. Nonetheless, to understand what the words mean, it is necessary to know that damages awarded in tort cases alleging bodily injury or property damage may include losses that are the consequence of the injury damage in question, such as medical expenses for treating bodily injury, or profits lost because of damage to property. Liability for these kinds of consequential losses is imposed "because of" bodily injury or property damage, even if it is not "for" such injury or damage.

Because all courts know this, the words "because of" in liability insurance policies seem in most cases to carry their meaning "on their face," without needing any interpretation. But that only appears to be the case. It is the legal and insurance context in which the words "because of" are used in

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<sup>60</sup> JAMES BRADLEY THAYER, PRELIMINARY TREATISE ON EVIDENCE 279-80 (1898).

<sup>61</sup> See, e.g., ABRAHAM & SCHWARCZ, *supra* note 1, at 439 (CGL insurance policy).

liability insurance policies that renders them subject to only one reasonable interpretation. However, when a claim for coverage of an unconventional form of liability arises – for example, when the party seeking to recover damages from the policyholder that are the consequence of bodily injury is not the same party who suffered bodily injury – then the courts must become more explicit what these words mean.<sup>62</sup>

Sometimes the legal and insurance context that informs the court’s interpretation is more complex, but still “goes without saying.” For example, in *Federal Ins. Co. v. Raytheon Co.*, the policyholder claimed coverage under its Directors & Officers (D&O) liability insurance policy for liability incurred in an ERISA action; It had earlier been a defendant in a different securities law suit. The D&O insurers contended that coverage of liability in the second suit was excluded under a “pending and prior litigation” exclusion in their policies. The exclusion applied to claims against the insured “based upon, arising from, or in consequence of any demand, suit or other proceeding” pending against the insured prior to a specified date. The court held that the exclusion applied if the “allegations in the second complaint find substantial support in the first complaint,” and concluded that they did.<sup>63</sup>

In order to arrive at this interpretation, however, the court had to have an understanding the complexity of ERISA and securities law suits generally, and the consequent detail that complaints typically contain, including the standard allegations regarding jurisdiction, identity of the parties, and remedies, that all such complaints make. These boilerplate allegations would have no bearing on whether the complaints substantially overlapped, since they are allegations that most complaints in complex civil suits would contain. If these sorts of allegations had been relevant to the application of the exclusion, however, then the overlap between the two complaints would have appeared to be far more substantial than it actually was – indeed, there probably would have been no issue even worth litigating. The court did not articulate any of this background context, and it did not need to do so. These facts about complex civil litigation were implicit knowledge that were one of the sources of the meaning of the unambiguous “prior and pending litigation” exclusion.

In short, it is inevitable and completely proper for courts to rely on facts outside the four corners of an insurance policy that are necessary to an

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<sup>62</sup> See, e.g., *Cincinnati Ins. Co. v. H.D. Smith*, 829 F.3d 771, 774-45 (7th Cir. 2017) (holding that state of West Virginia’s costs for addressing opiate addiction epidemic were incurred “because of” bodily injury, despite the fact that West Virginia itself suffered no bodily injury).

<sup>63</sup> See *Fed. Ins. Co. v. Raytheon Co.*, 426 F.3d 491 (1st Cir. 2005).

understanding of the meaning of policy provisions that the courts must interpret. Ordinarily such facts would not be in dispute if they were made explicit. But the meaning of the policy provision being interpreted might be different if the facts were otherwise. The facts may “go without saying,” in both senses of this phrase, but they are nonetheless sources of meaning extrinsic to the language of the insurance policy itself that are routinely sources relevant to the meaning of insurance policy provisions.

#### B. ADJUDICATIVE FACTS SUBJECT TO JUDICIAL NOTICE

More than fifty years ago, Kenneth Culp Davis distinguished between “adjudicative” and “legislative” facts. The former are facts that pertain specifically to the facts of a particular case, whereas the latter pertain to legal reasoning or the formation of legal principles.<sup>64</sup> Judicial notice is the process by which a court recognizes as true an adjudicative fact so well known and indisputable that it does not need to be formally introduced as evidence.<sup>65</sup>

A court may take judicial notice of adjudicative facts if the facts are “generally known” or “can be accurately and readily determined from sources whose accuracy cannot reasonably be questioned.”<sup>66</sup> Certainly dictionary definitions of terms used in an insurance policy fall into this category. The same is true of such matters as the fact that the most direct route of flight between New York and Miami is partly over water more than three miles outside the territorial limits of the United States, a fact that figured in a well-known case involving the interpretation of policy language requiring that crashes occur “within” the United States.<sup>67</sup> Adjudicative facts of this sort lie outside the four corners of an insurance policy. But courts may

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<sup>64</sup> Kenneth Culp Davis, *An Approach to Problems of Evidence in the Administrative Process*, 55 HARV. L. REV. 364, 404-07 (1942).

<sup>65</sup> Judge Posner also has observed that some “information tends to fall somewhere between facts that require adversary procedure to determine and facts of which a court can take judicial notice,” candidly acknowledging that “judges and their law clerks often conduct research on cases, and it is not always research confined to pure issues of law, without disclosure to the parties.” *Rowe v. Gibson*, 798 F.3d 622, 628 (7th Cir. 2015).

<sup>66</sup> FED. R. EVID. 201(b).

<sup>67</sup> See *Vargas v. Ins. Co. of N. Am.*, 651 F.2d 838 (1981).

take judicial notice of such facts and rely on them as sources of the meaning of policy provisions.

### C. LEGISLATIVE FACTS

In addition, the rules of evidence do not preclude courts from considering what have been called “legislative facts,” to distinguish them from adjudicative facts that pertain to the particular dispute.<sup>68</sup> A classic example of a legislative fact is the proposition that testimony by one spouse against another in a criminal proceeding would undermine most any marriage.<sup>69</sup> The purpose of a particular form of insurance, or of a particular standard-form policy provision, would generally fall into this category as well.

In contrast to adjudicative facts that are subject to judicial notice, which must effectively be indisputable, legislative facts need not satisfy this test:

[J]udge-made law would stop growing if judges, in thinking about law and policy, were forbidden to take into account facts they believe, as distinguished from facts which are “clearly...within the domain of the indisputable.” Facts most needed in thinking about difficult problems of law and policy have a way of being outside the domain of the clearly indisputable.<sup>70</sup>

Rather, a court’s authority to consider legislative facts “renders inappropriate any limitation in the form of indisputability, any formal requirements of notice other than those already inherent in affording opportunity to hear and be heard and exchanging briefs, and any requirement of formal findings at any level.”<sup>71</sup>

There are numerous cases in which the courts consider legislative facts outside the four corners of the insurance policy without ever holding

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<sup>68</sup> FED. R. EVID. 201 Advisory Committee’s note (a); Davis, *supra* note 64.

<sup>69</sup> FED. R. EVID. 201 Advisory Committee’s note (a) (citing *Hawkins v. United States*, 358 U.S. 74, 79 (1958)).

<sup>70</sup> *Id.* (quoting Kenneth Culp Davis, *A System of Judicial Notice Based on Fairness and Convenience*, in ROSCOE POUND *ET AL.*, PERSPECTIVES OF LAW 69, 82 (1964)).

<sup>71</sup> *Id.*



that a policy provision is ambiguous or admitting *evidence* regarding the meaning of the provision. For example, in *Port Authority of New York and New Jersey v. Affiliated FM Ins. Co.*, the court held that the presence of asbestos fibers in buildings operated by the policyholder did not constitute “physical loss or damage” under its property insurance policies, because the buildings were not uninhabitable or unusable. Interpreting the provision to provide coverage, the court said, “would not comport with the intent of a first-party ‘all-risks’ policy, but would transform it into a maintenance contract.”<sup>72</sup> There is nothing in the opinion indicating that evidence regarding the “intent of a first-party all risks policy” had been introduced, because there was no need for such evidence. That is a matter of legislative, not adjudicative fact. The court’s own knowledge of the function of property insurance, as distinguished from maintenance contracts, informed its interpretation of the policy provision and led it to the plain meaning of the policy.<sup>73</sup>

The court in *City of Johnstown v Bankers Standard Ins. Co.*<sup>74</sup> relied on the purpose of the insurance policy at issue in that case in a very similar manner. The insured in that case claimed coverage of environmental cleanup liability under its CGL insurance policies. Its insurers denied coverage on the basis of a provision that excluded coverage of liability for property damage that was “expected or intended” by the insured, arguing that the provision precluded coverage of “risks” that the insured expected or intended.<sup>75</sup> The court rejected this argument, holding that “to exclude all losses or damages which might in some way have been *expected* by the insured could expand the field of exclusion until virtually no recovery could be had on insurance. This is so since it is mishaps that are ‘expected’ – taken in its broadest sense – that are insured against.”<sup>76</sup> This conclusion was obviously premised on the court’s understanding of the principal risks of liability that CGL insurance policies are intended to cover. In effect the court held that because CGL insurance policies are designed to cover liability for

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<sup>72</sup> 311 F.3d 226, 236 (3d Cir. 2002).

<sup>73</sup> *Id.* There may of course be cases in which the purpose of a particular policy provision is not a legislative fact, because the purpose arises out of a feature of industry custom, or the needs of a particular policyholder. But the general purpose of a particular form of insurance will almost always be a legislative, not an adjudicative, fact.

<sup>74</sup> 877 F.2d 1146 (2d Cir. 1989).

<sup>75</sup> *Id.* at 1149.

<sup>76</sup> *Id.* at 1150 (*italics in original*).

negligence, the “expected or intended” provision could not properly be interpreted to exclude coverage of liability for most negligence.

#### D. TAKING STOCK

Courts subscribing to the plain-meaning rule routinely consider certain matter outside the four corners of the insurance policy when interpreting policy provisions: implicit knowledge, adjudicative facts subject to judicial notice, and legislative facts. I think that the best way to understand this practice is not to consider each source an exception to the rule that extrinsic evidence is not admissible if a policy provision has a plain meaning. Rather, although these sources of meaning are extrinsic to the insurance policy, they are not extrinsic evidence because, for all practical purposes, they are not *evidence*. By this I mean not only that they need not be formally admitted into evidence. More importantly, what renders them not *evidence* is that their existence or non-existence is not a question of fact that is subject only to the highly deferential review that is accorded to findings of fact at the appellate level.

On the contrary, whether to employ implicit knowledge, take judicial notice of an adjudicative fact, or rely on a legislative fact – and what these sources reveal to be true – are decisions for the court – in effect, decisions of law – and as such are subject to *de novo* review on appeal. This insight explains and justifies the vast majority of references to and reliance on sources outside the four corners of the insurance policy by plain-meaning courts.

This is especially important in view of the fact that the vast majority of insurance disputes concern standard-form policy provisions whose meaning, whatever it is, governs the rights of numerous policyholders. If standard-form policy provisions are to have a standard meaning, the resolution of insurance disputes must have the effect of precedent under *stare decisis*. If interpretations typically involved the resolution of questions of fact, then most interpretive decisions by the courts that relied on judicial notice and legislative facts could have little or no *stare decisis* effect. But of course they do have that effect. It follows that judicial interpretations of standard-form policy provisions relying on sources of meaning extrinsic to the policy are not resolutions of questions of fact based on conventional evidence, and therefore that the sources of meaning outside the four corners of the policy on which they rely are not really factual evidence at all. In short, there is nothing inconsistent or paradoxical about plain-meaning courts considering these sources of meaning.

IV. AMBIGUITY ABOUT AMBIGUITY: INTERPRETATION AND  
CONSTRUCTION OF AMBIGUOUS POLICY PROVISIONS

Once a plain-meaning court determines that a policy provision is ambiguous, then the plain-meaning rule no longer precludes the admission of extrinsic evidence to determine the more reasonable interpretation of the ambiguous provision.<sup>77</sup> Only the conventional rules of evidence limit what the court may consider when a policy provision is ambiguous. Common forms of extrinsic evidence include the negotiations, if any, between the parties, their course of dealing once the policy has been issued,<sup>78</sup> custom and usage,<sup>79</sup> and the drafting history of standard-form policy provisions.<sup>80</sup>

In most jurisdictions the courts first attempt to determine whether, in light of any extrinsic evidence that is admitted after a court holds that a policy provision is ambiguous, the ambiguous provision has a single meaning.<sup>81</sup> This is interpretation. Only if the extrinsic evidence does not resolve the ambiguity in this fashion does the court then apply *contra proferentem*. This is construction. An important but little-recognized issue regarding interpretation of ambiguous policy provisions is the *stare decisis* effect of an interpretation, for this concerns whether, and when,

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<sup>77</sup> RLLI § 4 cmt. b.

<sup>78</sup> See, e.g., *Motors Liquidation Co. v. Allianz Ins. Co.*, No: N11C-12-022 FSS CCLD, 2013 WL 7095859 at \*5 (Del. Super. Ct. Dec. 31, 2013).

<sup>79</sup> See, e.g., *Transp. Indem. Co. v. Dahlen Transp., Inc.*, 161 N.W. 2d 546, 550 (Minn. 1968) (considering evidence of insurance industry custom and usage).

<sup>80</sup> See, e.g., *Balandran v. Safeco Ins. Co. of Am.*, 972 S.W.2d 738, 741-42 (Tex. 1998).

<sup>81</sup> In a minority of jurisdictions, the courts apply *contra proferentem* immediately upon concluding that a policy provision is ambiguous, without considering extrinsic evidence of the provision's meaning. See, e.g., *Wash. Nat'l Ins. Corp v. Ruderman*, 117 So. 3d 943, 949 (Fl. 2013); Daniel Schwarcz, *Coverage Information in Insurance Law*, 101 MINN. L. REV. 1457, 1505-10 (arguing that this should be the rule generally). In addition, sometimes when a court immediately applies *contra proferentem*, it is not possible to determine which approach a court is applying, because it is unclear from the court's opinion whether any extrinsic evidence was introduced. See, e.g., *Vargas v. Ins. Co. of N. Am.*, 651 F.2d 838 (3d Cir. 1981); *N. Pac. Ins. Co. v. Hamilton*, 22 P.3d 739 (Or. 2001).

interpretations of unambiguous and ambiguous policy provisions have the same kind of precedential effect. Similarly, a little-recognized issue regarding the construction of ambiguous policy provisions is whether there is a role to be played by the very different reasons for a policy provision's ambiguity. I discuss both issues below.

#### A. INTERPRETING AMBIGUOUS POLICY PROVISIONS

Sometimes interpretation based in part on extrinsic evidence reaches the conclusion that the policy provision at issue has a single meaning. Interpretations of this sort typically are given the same strong *stare decisis* effect as interpretations under the plain-meaning rule. But whether this makes sense depends on what sources of meaning were called upon to interpret the provision. If the interpretation is a decision of law, then it should have that *stare decisis* effect. On the other hand, if truly evidentiary, factual sources have been considered – as is permitted once the provision has been determined to be ambiguous – then the interpretation arrived at may be based in whole or in part on findings of fact, and the *stare decisis* effect of the decision should be more limited.<sup>82</sup>

For example, if in order to interpret a provision a court based its interpretation on statements made by the parties in negotiating the policy or in custom-drafting it, or on the course of dealing between the parties subsequent to the issuance of the policy, then the decision would have only the *stare decisis* effect, if any, that a decision relying on findings of fact about such matters may have. A dispute between different parties over the meaning of the same ambiguous policy provision could therefore be resolved differently, depending on the extrinsic evidence relevant to their independent dispute.<sup>83</sup> An appellate court reviewing such interpretations would have only

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<sup>82</sup> Professor Farnsworth has made this point about the scope of review of contract decisions generally. See FARNSWORTH, *supra* note 15, §7.17. But he does not extend the point to *stare decisis*, and I have never seen the point made, in either respect, about interpretations of insurance policy language.

<sup>83</sup> For examples of such disputes in classic cases, see *Silberg v. Cal. Life Ins. Co.*, 521 P.2d 1103, 1109 (Cal. 1974) (involving dispute over insurance industry custom regarding payment of claims and subsequently seeking reimbursement from insured or another insurer); *Morton Int'l, Inc. v. Gen. Acc. Ins. Co.*, 629 A.2d 831, 855 (N.J. 1993) (involving dispute over inferences to be drawn from drafting history of the qualified pollution exclusion in CGL policies).

limited authority to reverse them, presumably for something like abuse of discretion.

On the other hand, suppose that a court rested its interpretation on findings of fact that were more generally relevant to the interpretation of the policy provision, such as custom and usage within an industry (including the insurance industry), or the drafting history of a standard-form provision. There is no question that appellate courts treat such interpretations as being reviewable *de novo*.<sup>84</sup> In my experience, subsequent courts asked to interpret the same policy provision treat the earlier decision as having *stare decisis* effect. This evidently precludes revisiting the factual predicates on which the earlier decision rested, including the nature and significance of custom and usage, and implications of the drafting history of the ambiguous policy provision at issue.

Why do interpretations resting on findings about generally-applicable facts such as industry custom and usage, and standard-form drafting history, have the broad *stare decisis* effect that they are usually accorded, even though the interpretations rest on factual premises that in other settings could be relitigated? For example, why are interpretations based on drafting history treated as if they are not subject to re-litigation in a claim by a different policyholder?

I think there are several possible explanations. First, this treatment may actually be unjustified or not even (strictly speaking) what actually happens. In fact, it may be that courts adhere to decisions based on findings of fact regarding industry custom or drafting history mainly because subsequent litigants do not attempt to introduce new evidence regarding these matters, and that the courts would actually consider substantial new evidence, and decide differently if the evidence warranted doing so, especially after the passage of a considerable amount of time. Perhaps decisions based on such matters of fact are potentially subject to re-litigation.

Second, however, if this is the case, re-litigation could be highly disruptive. Then, a particular trial court's findings of fact about custom or drafting history might in principle be subject to a different inference by a subsequent trial court, even if no new evidence were introduced. Standard policy language would then potentially be subject to different interpretations, depending on findings by different courts, case-by-case.

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<sup>84</sup> See, e.g., *PBM Nutritionals, LLC v. Lexington Ins. Co.*, 724 S.E.2d 707, 712 (Va. 2012) (holding that an appellate court reviews interpretations of insurance contracts *de novo*).

Third, the courts may be treating findings about such matters as custom and usage and drafting history as involving legislative rather than adjudicative facts, and therefore subject to *de novo* appellate review that generates a strong *stare decisis* effect. That may be an accurate characterization of certain such facts – the general and undisputable explanation for the addition of an absolute pollution exclusion to CGL insurance policies beginning in 1986 is a good example.<sup>85</sup> But that cannot be the explanation for the strong *stare decisis* effect accorded other interpretations that involve disputable characterizations of custom and usage or drafting history.

Fourth, the justification for this treatment may resonate with the principle underlying non-mutual offensive collateral estoppel. If a policyholder has won a case involving facts generally relevant to the meaning of a standard-form policy provision, then a subsequent, different insurer is treated as being bound by the earlier decision that technically binds only the earlier insurer. The second insurer stands in the shoes of the earlier insurer as long as the earlier insurer had an incentive to fully litigate the issue in question, and lost. This whole analogy would work against insurers, but not against policyholders, since one policyholder cannot reasonably be understood to have been litigating on behalf of all policyholders.

Finally, it may be that the practice of according *stare decisis* effect to interpretations based on generally-applicable facts is a prudential exercise by the courts rather than one that, technically, is mandatory. The practice facilitates treating standard-form policy language as having a uniform meaning, and thereby enhances the advantages of having standard-form policies.<sup>86</sup> If an earlier factual finding about the significance of custom and usage or drafting history for the meaning of an ambiguous standard-form provision turns out later to have been flawed, later courts still can exercise their discretion to revisit it. Since *stare decisis* is itself an essentially prudential doctrine,<sup>87</sup> the seemingly anomalous precedential effect that the courts give to interpretations based on custom and usage and drafting history may be more apparent than real.

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<sup>85</sup> See *Am. States Ins. v. Koloms*, 687 N.E.2d 72, 79-82 (Ill. 1997).

<sup>86</sup> See RESTATEMENT (SECOND) OF CONTRACTS § 211(2) (indicating that interpreting standard form contracts so as to treat similarly-situated parties in the same manner is desirable).

<sup>87</sup> See FREDERICK SCHAUER, THINKING LIKE A LAWYER 36 (2009) (noting the practice of “ordinarily requiring that decisions follow precedent”).

B. CONTRA PROFERENTEM: THREE LEVELS OF CONSTRUCTION  
AGAINST THE DRAFTER

It is quite possible for a policy provision to remain ambiguous even after consideration of extrinsic evidence relevant to the meaning of the provision. In such cases, under the traditional application of *contra proferentem*, the provision is construed against the drafter, which in the case of standard-form provisions is the insurer. The one recognized limit in this situation is that a construction that affords policyholders coverage that they could not reasonably expect is not to be adopted.<sup>88</sup> This might be understood as an interpretive limit on *contra proferentem*, since in a sense an interpretation that would afford policyholders more coverage than they would reasonably expect is not a reasonable interpretation.

There also are hints in the case law, however, that the reason that a policy provision is ambiguous may have a bearing on the process of construction. These hints actually have a substantial normative basis that has not been recognized: the greater the amount of blame for the ambiguity that can be attributed to the drafter, the stronger the justification for construing the provision against the insurer and in favor of coverage. There are three levels of blameworthiness, corresponding to the reason that the provision came to be drafted as it was.

## 1. Ambiguity by Necessity

Some policy provisions are ambiguous out of necessity. The problem they address may be complex, the language that would be required to unambiguously resolve particular issues in advance of all disputes may be lengthier than is practical or desirable,<sup>89</sup> or all the situations to which the

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<sup>88</sup> See RLLI, at § 4 cmt. f; *Chute v. North River Ins. Co.*, 214 N.W. 473, 474 (Minn. 1927) (holding that construing an ambiguous policy provision in favor of coverage the policyholder could not reasonably expect would “ignore the purpose of the contract”). In my earlier Article about insurance policy interpretation, I called this the “majoritarian” approach, distinguishing it from a “penalty” approach that would construe an ambiguous provision in favor of coverage regardless of whether it was reasonable to expect that coverage. Abraham *supra* note 14, at 545-50.

<sup>89</sup> See Daniel Schwarcz, *Coverage Information in Insurance Law*, 101 MINN. L. REV. 1457, 1474 (2017) (arguing that longer policy provisions

provision may apply may be difficult to predict and unambiguously address. As one court astutely put this point:

Drafters cannot anticipate all possible interactions of fact and text, and if they could to attempt to cope with them in advance would leave behind a contract more like a federal procurement manual than like a traditional insurance policy. Insureds would not be made better off in the process. The resulting contract would not only be incomprehensible but also more expensive.<sup>90</sup>

For example, the standard-form homeowners policy defines an insured (among other things) as “residents of your [the policyholder’s] household who are...<sup>21</sup> and in your *care* or the *care* of a resident of your household who is your relative.”<sup>91</sup> Although I have found no cases on the issue, there is a pretty good argument that the word “care” in this context is ambiguous, in the sense that it has either pretty broad or quite narrow boundaries.<sup>92</sup> Being “in your care” might require that the policyholder serve as the complete support for a bedridden person who is unable to perform bodily functions without assistance, or it might require only serving a temporarily ill person meals and helping the person to get out of bed. But specifying the exact contours of “care,” especially given the different possible gradations of “care,” would require extended verbiage addressed to an issue that is likely to arise only rarely under homeowners’ policies. The result is that the term “care” is ambiguous, and would likely remain

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makes it more difficult for policies to be understood *ex ante*, by those selling them, regulating them, and deciding whether to buy them). In my earlier article, I referred to this kind of assessment as the application of a “linguistic standard of care.” Abraham, *supra* note 14, at 537-38. To ignore this factor would, I think, be to impose strict liability on the drafter for employing unavoidably ambiguous policy language. *Id.* at 538-40.

<sup>90</sup> See *Harnischfeger Corp. v. Harbor Ins. Co.*, 927 F.2d 974, 976 (7th Cir. 1991); FARNSWORTH, *supra* note 15, §7.09 (indicating that the difficulty of foreseeing all the circumstances that will arise sometimes accounts for lack of clarity).

<sup>91</sup> See ABRAHAM & SCHWARCZ, *supra* note 1, at 186-87 (emphasis added).

<sup>92</sup> Professor Farnsworth identifies haziness at the boundary of a concept as “vagueness,” and suggests that intentional vagueness may be more justified than intentional ambiguity. FARNSWORTH, *supra* note 15, at §7.09.



ambiguous even if extrinsic evidence addressing the meaning of the term were available and admitted.

Similarly, the standard-form CGL policy covers liability incurred because of bodily injury or property damage that occurs “during the policy period,” and further provides that such bodily injury or property damage “includes any continuation, change or resumption of *that* ‘bodily injury’ or ‘property damage’ after the end of the policy period.”<sup>93</sup> The term “that” (technically, a “demonstrative adjective”<sup>94</sup>) is almost certainly ambiguous in some contexts. Suppose that during policy year one, hazardous waste leaks from a site and contaminates groundwater (underground water) lying fifty feet beyond the boundary of the site where it was deposited. That is “property damage.” Suppose further, however, that in policy year two, the waste that was already in the groundwater migrates further, and contaminates previously-uncontaminated groundwater, lying between 50 and 500 feet beyond the boundary of the site. Under the above-quoted provision, is the contamination that occurred during policy year 2 a continuation of “that” original property damage (in which case it is not covered under the policy in force during year 2), or is it new “property damage” that is not counted as part of the original property damage (and therefore is covered under the policy in force in year 2)?

In this context, both are arguably reasonable interpretations on the face of this policy language. Extrinsic evidence would be admissible to determine which interpretation is more reasonable, but may well not resolve the ambiguity. Yet, whichever interpretation is adopted would have required extensive verbiage to address unambiguously in the policy, especially since my hypothetical is an example of only of a number of different factual scenarios that might have to be identified. In effect, the term “that” is a placeholder that, understandably, delegates the task of elaboration to the courts.

This necessity explanation for ambiguity of the sort reflected in the homeowners’ policy’s use of the term “care,” and the CGL policy’s use of the term “that,” justifies an evenhanded search for the more reasonable interpretation of the policy provision in the context of the claim at issue, because the insurer’s drafting does not reflect sloppiness or an effort to take advantage of policyholders. In this setting, *contra proferentem* should

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<sup>93</sup> *Id.* at 439 (emphasis added).

<sup>94</sup> See *What is a Demonstrative Adjective?*, YOUR DICTIONARY <https://grammar.yourdictionary.com/parts-of-speech/adjectives/demonstrative-adjectives.html> (last visited on May 20, 2019).

operate as a rule of last resort, a genuine tiebreaker to be used only when the evidence does not generate a single interpretation that is at least slightly more reasonable than a competing interpretation or interpretation.

The courts, however, tend not to resolve such situations in this way. Rather, often they avoid holding that a policy provision that is ambiguous out of necessity, and instead treat the situation as calling for the creation of a rule governing the problem rather than for an interpretation of the policy language. Perhaps the most prominent example of this approach is the courts' adoption of the pro-rata approach to the allocation of coverage responsibility among multiple triggered CGL insurance policies that were issued before the above-quoted provision addressing the continuation of injury or damage was included in the standard-form policy. The CGL policy covered liability "for those sums that the insured becomes legally obligated to pay as damages... because of bodily injury or property damage...which occurs during the policy period."<sup>95</sup> The policy did not unambiguously address the extent of each policy's coverage responsibility if bodily injury or property damage occurred during multiple policy periods. But the courts nonetheless developed a rule that allocated coverage responsibility on a pro-rata basis.<sup>96</sup>

Another example of this approach is the courts' treatment of exclusions from coverage of liability for bodily injury or property damage "expected or intended from the standpoint of the insured."<sup>97</sup> These exclusions are arguably ambiguous in a number of ways. For instance, they do not address whether coverage of one insured is excluded when another insured expected or intended harm; and they do not address whether coverage is excluded when one type of harm (*e.g.*, bodily injury) is expected but a different type of harm (*e.g.*, property damage) occurs. On one view, addressing all these possibilities would render the provision unduly complicated.<sup>98</sup> Instead of holding that the provision is ambiguous, therefore,

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<sup>95</sup> See KENNETH S. ABRAHAM, *INSURANCE LAW & REGULATION* 440 (1990).

<sup>96</sup> See, *e.g.*, *Boston Gas Co. v. Century Indem. Co.*, 910 NE. 2d 290 (Mass. 2009). Other courts adopted a rule of joint and several responsibility. See, *e.g.*, *Goodyear Tire & Rubber Co. v. Aetna Cas. & Sur. Co.*, 769 N.E. 2d 835 (Ohio 2002).

<sup>97</sup> ABRAHAM & SCHWARCZ, *supra* note 1, at 440.

<sup>98</sup> The reason I have qualified this statement is that the standard-form homeowners policy has addressed this issue with fairly straightforward language. See *id.* at 205 (setting out a provision indicating that liability for harm is excluded even if that harm is "of a different kind, quality or degree

the courts have developed rules (though they vary) addressing these permutations.<sup>99</sup>

In such cases, the courts do not appear to be engaging in either interpretation or construction. In fact, however, they are doing the latter. The best understanding of the courts' development of rules of this sort to see it as the construction of policy provisions that are necessarily ambiguous. Because the drafter of provisions that are ambiguous by necessity is arguably not to blame for such ambiguity, invoking *contra proferentem* is regarded as inappropriate. Instead, the courts substitute a rule for what would otherwise be an unduly complex policy provision.

## 2. Ambiguity Resulting from Faulty Drafting

A second, and more blameworthy, reason that a policy provision may ambiguous is that it has been poorly drafted. The courts have frequently held that, the more easily it would have been to draft a provision that would have rendered its meaning clear, the stronger the argument that the provision is ambiguous.<sup>100</sup> The classic statement of this notion is that of Judge Frankel in the *Pan American* case:

Where the risk is well known and there are terms reasonably apt and precise to describe it, the use of substantially less certain phraseology upon which dictionaries and common understanding may fairly differ, is likely to result in interpretations favoring coverage rather than exclusion.<sup>101</sup>

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than initially expected for intended”).

<sup>99</sup> See, e.g., *SL Indus., Inc. v. American Motorists Ins. Co.*, 607 A.2d 1266 (N.J. 1992) (preserving the possibility of coverage when a different type of harm than occurred was expected); *American Family Ins. Co. v. Walser*, 628 N.W. 2d 605 (Minn. 2001) (holding that the exclusion applies as long as some harm was expected).

<sup>100</sup> See *ABRAHAM & SCHWARCZ*, *supra* note 1, at 540-44 (referring to this as a “perfectibility standard”).

<sup>101</sup> *Pan American World Airways, Inc. v. Aetna Cas. & Sur. Co.*, 368 F. Supp. 1098, 1188 (S.D. N.Y. 1973), *aff'd*, 505 F.2d 989 (2d Cir. 1974). See also *Estrin Const. Co. v. Aetna Cas. & Sur. Co.*, 612 S.W. 2d 413 (noting that an inept drafter has the resources to do better).

For example, in *Vlastos v. Sumitomo Marine & Fire Ins. Co. (Europe)*, a policy provisions stated, “Warranted that the 3rd floor is occupied as [a] janitor’s residence.”<sup>102</sup> There was evidence that a janitor lived on the third floor, but that it had other uses as well. The insurer denied coverage on the ground that the provision required that the third floor be used *only* as a janitor’s residence. The court rejected this argument, holding that the provision was ambiguous its face, because “occupied” could reasonably have meant either “occupied exclusively” or “occupied in part.”<sup>103</sup> The fact that the addition of a single word – “exclusively” – would have rendered the provision unambiguous was central to the court’s reasoning.<sup>104</sup>

Because one of the strongest arguments for *contra proferentem* has always been that the doctrine gives insurers the incentive to draft unambiguous policy provisions, a strong version of *contra proferentem* tends to be applied to faulty drafting that results in ambiguity. If an insurer drafts a sloppy or imprecise provision that could have been made unambiguous with little additional effort and no corresponding disadvantage, then the insurer has, in effect, been negligent. If there is also no extrinsic evidence supporting the insurer’s interpretation, the principle underlying *contra proferentem* strongly supports construing the provision against the drafter.

Even if there is extrinsic evidence supporting the insurer, however, *contra proferentem* should have substantial gravitational pull. The argument for rescuing the insurer by heavily weighing sources of extrinsic evidence such as the negotiations between the parties or custom and usage, is weak in this setting. Only strong and highly persuasive evidence should be permitted to rescue the insurer from its own faulty drafting in such a situation.

### 3. Ambiguity as a Trap

The last reason for ambiguity resonates most strongly with the policy underlying *contra proferentem*: the use of ambiguous policy language as a trap. Ordinarily there will be no direct evidence that an insurer deliberately

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<sup>102</sup> *Vlastos v. Sumitomo Marine & Fire Ins. Co. (Europe)*, 707 F.2d 775 (3d Cir. 1983).

<sup>103</sup> *Id.* at 780.

<sup>104</sup> *See also* *Great American Fidelity Ins. Co. v. JWR Construction Services*, 882 F. Supp. 2d 1340, 1356 (S.D. Fl. 2012) (indicating that had the insurer “wished to exclude the faulty work of persons acting on [the insured’s] behalf, it could easily have done so by using clear policy language to that effect”).

designed an ambiguous policy provision with the aim of using it as a trap. Certainly standard-form language, drafted by committees of organizations such as ISO, rarely if ever has that aim. But individual insurers sometimes draft language that sets a trap, and even standard-form language is sometimes seized upon by individual insurers in a manner that functions like a trap.

For example, in *Vargas v. Ins. Co. of N. Amer.*, an aviation insurance policy covered occurrences, accidents, or losses that happened “within the United States of America, its territories or possessions, Canada or Mexico.”<sup>105</sup> The insured’s plane crashed in the sea, twenty-five miles west of Puerto Rico, on a flight that began in New York, with stops in Miami and Haiti.<sup>106</sup> The insurer denied coverage, on the ground that the loss did not occur “within” the required territory. Yet the insurer knew that the insured planned to fly the plane in the Caribbean. This was a blatant effort to use the literal meaning of the word “within” to avoid coverage. The court rejected that effort, holding that the word “within” was ambiguous – subject to more than one reasonable interpretation -- and construed the provision against the insurer, in part because the insured’s interpretation was consistent with the “realities of airplane travel,” which sometimes requires flights between two places within the continental United States (such as flights between New York and Miami) to “pass over waters beyond the territorial limits” of the United States.

The insurer’s attempt to set a trap was even more blatant in *Silberg v. California Life Ins. Co.*,<sup>107</sup> the seminal decision permitting the imposition of extracontractual liability on an insurer for bad-faith denial of a claim. There a provision in a health insurance policy excluded coverage of “any loss caused by or resulting from (1) injury or sickness for which compensation is payable under any Workmen’s Compensation...Law.”<sup>108</sup> The insurer asserted that this exclusion precluded coverage, not only of any loss paid by workers’ compensation but of all losses incurred by the insured for an injury or sickness for which workers’ compensation paid anything at all.

The insurer therefore refused to pay any of the insured’s losses until it was determined whether any workers’ compensation would be paid, and when the insured settled his workers’ compensation claim, the insurer denied

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<sup>105</sup> See *Vargas v. Ins. Co. of N. Am.*, 651 F.2d at 840.

<sup>106</sup> *Id.*

<sup>107</sup> 521 P. 2d 1103 (Cal. 1974) (emphasis added).

<sup>108</sup> *Id.* at 1111.

coverage entirely, including for the losses that workers' compensation did not pay. The insurer did this despite having advertised "ALL BENEFITS PAYABLE IN FULL REGARDLESS OF ANY OTHER INSURANCE YOU MAY HAVE."<sup>109</sup> This is about as clear an example as there can be of insurer's attempt at bait-and-switch. Clearly the insurer was using the ambiguity of the word "payable" as a trap.

Finally, the insurer in *Corban v. United Automobile Services Association*<sup>110</sup> took the position that the "anti-concurrent causation" clause in its homeowners policy, which precluded coverage if a loss was "caused" by an excluded cause, even if a covered cause contributed "in any sequence" to the loss, precluded coverage of loss caused by hurricane wind damage, if later-caused (and excluded) water damage contributed to that loss.<sup>111</sup> The court held that the phrase "in any sequence" was ambiguous and invoked *contra proferentem*, in part because the insurer's interpretation would have excluded coverage of loss that had already occurred, on the ground that an excluded cause subsequently contributed to the loss.<sup>112</sup> The insurer's position offered what in common parlance would be called a "gotcha" interpretation: "your loss occurred, and it was covered at the moment it occurred, but subsequent events out of your control deprived you of insurance for this already-covered loss." Few if any insureds would have expected that result, or understood the relevant language to provide for it. It reflected an effort by the insurer to use the language of the anti-concurrent causation clause as a trap that had been set for the insured and then sprung after a covered loss had occurred.

## CONCLUSION

The interpretation of insurance policies turns out to be a more sophisticated and more complex process than the myths about interpretation sometimes make it out to be. Interpretations yielding the conclusion that a policy provision has a single, plain meaning are often active searches for meaning, not passive receptions of a meaning that is evident on the face of a provision. In addition, the idea that extrinsic evidence is not admissible to aid in the interpretation of a provision with a plain meaning masks the fact that important sources of meaning that are outside the policy are commonly considered in the course of interpretation. Finally, both the *stare decisis*

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<sup>109</sup> *Id.*

<sup>110</sup> 20 So. 3d 601 (Miss. 601).

<sup>111</sup> *Id.* at 612.

<sup>112</sup> *Id.* at 615.

effect of interpretations of ambiguous policy language, and differences in the reasons that an ambiguous policy provision came to be included in a policy, pose issues that have gone largely unrecognized because of the tendency to oversimplify what occurs when ambiguous policy language is interpreted or construed. Greater clarity about all of these interpretive phenomena deepens our understanding of the role played by plain meaning, extrinsic evidence, and ambiguity in the interpretation of insurance policies.

