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The Role of Extrinsic Evidence in Resolving Policy Ambiguity under the Restatement, Law of Liability Insurance

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My last post examined the Restatement, Law of Liability Insurance's treatment of the use of extrinsic evidence when a policy term has a plain meaning on its face. If on its face a policy term has more than one meaning to which it is reasonably susceptible, the term does not have plain meaning and it is interpreted under the Restatement's rules for resolving ambiguity.

Traditional Approaches to Resolving Ambiguity

Traditionally, courts have employed some version of the *contra proferentum* principle under which ambiguous contract terms are interpreted "against the offerer" to resolve ambiguity in insurance policies. Under the version *contra proferentum* doctrine that prevailed in the 1970s and 1980s and still prevails in some states, the process of interpreting insurance policies was largely mechanical and, more often than not, the policyholder won. Courts typically began their analysis of coverage questions with a familiar catechism: Is the policy term subject to more than one interpretation? Is the insured's interpretation of the term reasonable? If the answer to these questions was yes, courts routinely declared the policy term ambiguous and applied the insurance law axiom that ambiguities should be construed against the insurer without considering the full context of the term.

Over time, courts¹ and commentators² began to recognize that mechanical application of the *contra proferentum* rule makes the meaning of insurance policies less predictable and, in some instances, affords insureds rights that do not exist in the language of the policy. These concerns

¹ *Bank of the West v. Superior Court*, 2 Cal.4th 1254, 1264, 10 Cal.Rptr.2d 538, 544, 833 P.2d 545 (1992).

² Michelle E. Boardman, *Contra Proferentem: The Allure of Ambiguous Boilerplate*, 104 Mich. L. Rev. 1105, 1127 (2006).

led to attempts to put the law of insurance policy interpretation on a predictable footing— attempts that culminated during the 1990s in a shift away from reflexive pro-policyholder rules of interpretation.

The Contra Proferentum Rule under the Restatement, Law of Liability Insurance

The Restatement's approach to *contra proferentum* is consistent with the growing number of courts that have interpreted ambiguity against the insurer only as a last resort interpretative tie breaker. Under § 4 of the Restatement, an ambiguous term is interpreted in favor of the party that did not supply the term (usually the insured), *unless the other party persuades the court that this interpretation is unreasonable in light of extrinsic evidence*. Relevant extrinsic evidence includes the objective purpose of the term which can be found in treatises, insurance-industry trade literature, the drafting history of the policy, prior court decisions, statements made to regulatory agencies during the policy approval process, expert testimony, and comparison with other insurance policy forms available on the market.

Role of Insured's Objective Reasonable Expectations

In assessing the reasonableness of the coverage-promoting interpretation, the Restatement asks how a reasonable person in the policyholder's position would have understood the term in question. Although the subjective understanding of the policyholder plays no role in the analysis, the commercial sophistication of the policyholder does. An interpretation that may not be objectively reasonable from the perspective of a commercially sophisticated policyholder may be objectively reasonable from the perspective of a policyholder with little commercial experience.

Relevance of Drafting Difficulties

Another consideration is the ease with which the insurer could redraft the policy to more plainly express the meaning urged by the insurer. The easier it would be for the insurer to state the meaning more plainly, the more likely it is that the coverage-promoting interpretation is the meaning that a reasonable policyholder would give to the term.

My next post will explore further the role of policyholder sophistication in the interpretation of insurance policies.