

**PATCHWORK CONTEXTUALISM IN THE ANGLO-CANADIAN
LAW OF INSURANCE POLICY INTERPRETATION:
IMPLICATIONS FOR THE PRINCIPLES OF THE LAW OF
LIABILITY INSURANCE**

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The law of Canadian insurance policy interpretation can be seen as an apt natural experiment for some of the proposed principles in the American Law Institute's draft Principles of the Law of Liability Insurance ("Principles").¹ The Principles attempts to provide some unification of the American law of insurance policy interpretation. In the past, this area of law has been divided by two distinct traditions—a textualist tradition where insurance policy meaning is derived solely from the text of an insurance policy and a contextualist tradition where insurance policy meaning is derived from both the text of the policy and, to varying degrees, broader contextual factors existing outside the policy. The Canadian law of insurance policy interpretation is a unique amalgam of American contextual and English textual insurance policy interpretation principles. It is, at its best, a patchwork, peripatetic contextual approach—it can vacillate from contextualism to extreme textualism in case results. At its purest form, it attempts to strike very close to the alleged middle ground that the proposed Principles purport to itself strike.² The Principles attempts to straddle the bipolar textualist and contextualist camps of American insurance jurisprudence by providing a set of interpretive principles that draw on the best of both legal traditions. By understanding how the law of Canadian insurance policy interpretation operates—and fails—those charged with the task of drafting the Principles may be able to draw some comparative assistance in achieving this delicate balance that Canadian law has, for decades,

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1. PRINCIPLES OF THE LAW OF LIAB. INS. (AM. LAW INST., Tentative Draft No. 1, 2013).

2. *Id.* § 3 reporters' note b.

sought to achieve. At the very least, the Canadian experience may operate as a useful foil for how many of the issues tackled in the proposed Principles may actually play out in American insurance law disputes.

This Article proceeds in four parts. Part I explains the Canadian insurance litigation context. In evaluating the comparative usefulness of Canada's approach to insurance policy interpretation as a foil for the Principles' unification goals, certain systemic differences between Canadian and American insurance cases need to be understood. Part II of the Article details the two models of insurance policy interpretation prevalent in Canadian insurance law. It explains the genesis of those models as being an amalgam of both American and British insurance law traditions. This Part also exposes the patchwork contextualism and powerful textualist magnetism, which renders the Canadian approach problematic in many cases. Part III of the Article deconstructs some of the key elements to consider when designing insurance policy interpretation doctrine and attempts to demonstrate the inefficient problems encountered if those elements are misaligned, ignored, or forgotten altogether. It does so by referring to the benefits and detriments of the Canadian approach and uses the Principles' proposals and the British approach to insurance policy interpretation as reflective referential examples of what does and does not work. Part IV of the Article concludes by suggesting a model framework for insurance policy interpretation that draws on the best traditions in the American, Canadian, and British law of insurance policy interpretation. The framework, like the Principles, is mindful of the desire to straddle textualist concerns about the importance of text with the more contextualist concerns about how insurance operates in modern society. The end result is a structured approach that hopes to avoid some of the problems embedded in each country's current process for insurance policy interpretation.

A NOTE ON TEXTUALISM VERSUS CONTEXTUALISM

By "textualism," this Article means to reference that strain of jurisprudential thinking whereby meaning in the interpretive process is conducted primarily and preferably exclusively from the text of an instrument.³ Textualism is borne of formalist legal traditions. The goal is

3. See, e.g., P. S. ATIYAH & ROBERT S. SUMMERS, FORM AND SUBSTANCE IN ANGLO-AMERICAN LAW: A COMPARATIVE STUDY OF LEGAL REASONING, LEGAL THEORY, AND LEGAL INSTITUTIONS 96–100 (1987); JEFFREY W. STEMPEL, PETER N. SWISHER & ERIK S. KNUTSEN, PRINCIPLES OF INSURANCE LAW 110–13 (4th ed. 2011) (explaining "formalism" and "functionalism"); Avery Wiener Katz, *The Economics of Form and Substance in Contract*

one of predictability in interpretive result as derived from the objective meaning of a text. By “contextualism,” this Article means to reference that strain of jurisprudential thinking whereby meaning in the interpretive process is derived not only with deference to the text of an instrument but with reference other contextual factors as well: purpose, intent, expectations, and sociology. Contextualism is borne of functionalist legal traditions. The goal is one of ensuring the given meaning of a text is achieving desirable consequences in a just society.

I. THE CONTEXT OF CANADIAN INSURANCE LAW AND LITIGATION

The Canadian civil justice system, as it relates to insurance disputes, strongly mirrors the American system, with a few notable exceptions. These exceptions likely explain why the Canadian experience with insurance coverage litigation is far more muted in terms of litigation frequency, amounts at stake, and tolerated degrees of judicial and governmental control of insurance. Regardless of the differences between the two systems, comparisons between the two are helpful in that Canadian insurance policy interpretation principles attempt to balance textualist and contextualist approaches. Whether it does so successfully is challenged in subsequent parts below. Comparative thinking is therefore best informed by highlighting a few of the distinctions between American and Canadian insurance law and litigation.

A. *Countrywide Unification of Common Law of Insurance*

One difference about the Canadian legal system as compared to its American counterpart is the fact that, in Canada, the entire country enjoys predominantly de facto unification of common law insurance law principles across the individual provinces. Canadian provinces do not exhibit the same level of autonomy in lawmaking that American states do. In large part, this is due to the facts that provincial insurance statutes are nearly identically worded, in the main, from province to province, and, most importantly, the Supreme Court of Canada acts as a grand leveler of the common law. The Supreme Court is a court of general jurisdiction and hears appeals from provincial appellate courts on

Interpretation, 104 COLUM. L. REV. 496, 497-98 (2004); Peter Nash Swisher, *Judicial Interpretations of Insurance Contract Disputes: Toward a Realistic Middle Ground Approach*, 57 OHIO ST. L.J. 543, 546-47 (1996) [hereinafter Swisher, *Judicial Interpretations*]; Peter Nash Swisher, *Judicial Rationales in Insurance Law: Dusting Off the Formal for the Function*, 52 OHIO ST. L.J. 1037, 1040-58 (1991) [hereinafter Swisher, *Judicial Rationales*].

private law matters, including insurance.⁴ One of the Court's goals is to avoid conflicting results among the case law in the various provinces.⁵ There is no separate federal arm of insurance law, as insurance is generally the purview of the provinces. Thus, American-style state-federal diversity issues are avoided.⁶ This means that insurance policy interpretation principles are largely uniform common law developments built up from predominantly Supreme Court of Canada decisions that are binding on the entire country.

B. Regulatory Environment and Government Engineering of Automobile Insurance

The regulatory environment for insurance in Canada is also highly uniform among provinces. Provincial governments control insurance regulation. Nationwide uniform insurance law regulations are achieved via the Canadian Council of Insurance Regulators, the association of provincial insurance regulators.⁷ With the exception of automobile insurance, insurance policy forms are written by the insurance industry itself and marketed with little to no hands-on government regulation as to wording and content. Regulation of policy terms is thus left to the common law.⁸ However, insurance industry trade organizations like the Insurance Bureau of Canada and the Canadian Life and Health Insurance Association provide common sample wording of policies to their members which act as templates for policy wording among insurers. There is, as a result, little variance in insurance policy wording among various companies (though some slight variance can exist). In addition, there are often inter-company agreements about standard insurance practices that provide further incentives to standardize policy wording.⁹ Therefore, unlike American insurance regulation, which often has a regulatory arm at the state level for policy form approval,¹⁰ such a result is roughly achieved through soft industry coercive incentives.

As mentioned above, automobile insurance is the exception.

4. Although, the frequency is about zero to one insurance cases per year. *See, e.g.*, SUPREME COURT OF CANADA: STATISTICS 2004 TO 2014 (2015).

5. Erik S. Knutsen, *Seeking Leave to Appeal to the Supreme Court of Canada for Personal Injury Cases*, LITIGATOR: J. ONT. TRIAL LAW. ASS'N, July 2009, at 5–6.

6. *See, e.g.*, *Erie R.R. Co. v. Tompkins*, 304 U.S. 64, 71–76 (1938).

7. BARBARA BILLINGSLEY, *GENERAL PRINCIPLES OF CANADIAN INSURANCE LAW* 3 (2008).

8. Although, there is very basic regulation of fundamental insurance policy content in provincial insurance statutes. *See, e.g.*, Insurance Act, R.S.O. 1990, c. I.8 (Can. Ont.).

9. BILLINGSLEY, *supra* note 7, at 4.

10. STEMPEL, SWISHER & KNUTSEN, *supra* note 3, at 213–29.

Automobile insurance is highly regulated by the provinces, right down to the wording of the insurance policy.

1. Fault, Hybrid, and No-Fault Auto Systems

All drivers in Canada must have automobile liability insurance.¹¹ Québec and Manitoba operate a government-controlled, “purely no-fault automobile insurance” regime.¹² Saskatchewan operates a choice no-fault/tort auto insurance regime where drivers can ex ante elect which system they prefer at the time they purchase their automobile insurance.¹³ Ontario operates a hybrid tort/no-fault regime where only severely injured automobile accident victims are entitled to access the tort system—otherwise, the victim can only access no-fault first party accident benefits.¹⁴ All other provinces provide a minimum level of no-fault first party accident benefits but retain the tort system for resolving automobile accident compensatory disputes.¹⁵

2. The Government–Controlled Auto Insurance Market

Canadian automobile insurance is available to the public via two models: government-as-insurer and a market co-opt model.¹⁶ A few provinces¹⁷ run their own government-controlled insurance for their residents: the government-as-insurer model.¹⁸ These provinces create a regulatory arm of the provincial government to administer the insurance program, pay claims, and draft and revise the available insurance coverage.¹⁹ In such provinces, the insurance regulatory arm maintains “a monopoly on the provision of automobile insurance products.”²⁰ Consumers can only purchase the automobile insurance products provided for, priced by, and administered by the government insurer.²¹ In some cases, these products are sold only by a specific government agency

11. Erik S. Knutsen, *Auto Insurance as Social Contract: Solving Automobile Insurance Coverage Disputes Through a Public Regulatory Framework*, 48 ALTA. L. REV. 715, 717 (2011).

12. *Id.* at 719.

13. *Id.* at 720.

14. *Id.*

15. *Id.*

16. *Id.* at 718.

17. British Columbia, Manitoba, Québec, and Saskatchewan. *Id.*

18. *Id.*

19. *Id.*

20. *Id.*

21. *Id.*

directed to do so.²² In other instances, private market insurers may market and sell the government insurance products.²³ However, consumers are only offered the government-run insurance products.²⁴

Most provinces run a market co-opt system for automobile insurance.²⁵ In this system, a government agency (with insurance industry input) drafts and controls the scope of the automobile insurance products, but such products are priced and sold on the private market by for-profit insurers who administer and pay any eventual claims.²⁶ In this model, the government agency completely controls the wording of any available insurance products.²⁷ In fact, the policies are often enshrined in provincial legislation.²⁸

Regardless as to which auto insurance model a Canadian province employs, the private insurance industry has significant input through trade and lobby groups into how the policies are actually worded by the government.²⁹ This influence has resulted in near-standardization of automobile insurance policy wording across the country.³⁰ Interestingly, the wording of Canadian automobile insurance policies tracks standard American automobile insurance policy wording.

C. *Lack of Jury Input in Insurance Coverage Matters*

While Canadian provinces provide for the right to a jury trial in civil cases, issues of insurance coverage are nearly always decided by a judge without a jury.³¹ A jury trial in Canada is a procedural option, which is invoked by party choice in a civil dispute.³² In practice, this option is nearly always elected only in some personal injury cases. The process by which most insurance coverage and thus interpretation disputes are resolved—even in the context of an elected jury trial—is in a judge-alone motion that often takes place well before trial occurs. Insurance matters may often proceed by summary judgment motion or by a motion testing the substantive adequacy of the pleadings as to whether or not coverage

22. *See id.*

23. *Id.*

24. *Id.*

25. *Id.*

26. *Id.* at 718–19.

27. *Id.* at 718.

28. *Id.* at 718 n.9, 721–22.

29. *Id.* at 718–19.

30. *Id.* at 722.

31. Erik S. Knutsen, *Five Problems with Personal Injury Legislation (and What to Do About It!)*, 40 *ADVOCS.* Q. 492, 515 (2013).

32. *See id.*

even exists. The fact that insurance matters are reserved for a judge alone is significant because it means that questions of both insurance policy interpretation and factual findings rest with the same legally trained, experienced fact-finder. The jobs are often not separated and can get blurred, particularly in the interpretation context. Additionally, the judge-alone nature of insurance decisions has impacted the development of the applicable standards of appellate review for insurance-related issues.

D. Impact of Loser-Pays Fee Shifting Regime

The Canadian legal costs regime has an impactful dynamic on the insurance litigation scene in Canada, as non-institutional litigants must seriously consider the financial consequences at risk in having to potentially pay a portion of a successful adverse party's legal costs. The Canadian provinces follow a fee-shifting regime for legal costs in which the loser in a civil dispute pays a proportion of the winner's legal fees.³³ Most insurance and personal injury work is done on a contingency fee for plaintiff's counsel and on a per-hour basis for insurance defense work.³⁴ Nevertheless, a case lost at trial could mean the loss of a plaintiff's house because most everyday non-institutional litigants cannot afford to defray the costs of a successful adverse party's legal fees (even though the plaintiff's lawyer's time may not be charged to them). The costs regime therefore has a significant muting effect on private insurance litigation, as compared to a system like the United States where parties bear their own legal costs.

E. Modest Damage Awards

Canadian personal injury cases exhibit a far lower dollar value range of damage awards compared to American cases. With less at stake, the incentive for pursuing insurance claims related to injury is concomitantly less as well. The primary goal in Canadian personal injury damages is to provide for future care in a functional, replacement cost fashion.³⁵ Non-pecuniary damages for pain and suffering are judicially capped at

33. See, e.g., Erik S. Knutsen, *The Cost of Costs: The Unfortunate Deterrence of Everyday Civil Litigation in Canada*, 36 QUEEN'S L.J. 113, 114 (2010).

34. See *id.* at 119–20.

35. See, e.g., *Andrews v. Grand & Toy Alta. Ltd.*, [1978] 2 S.C.R. 229, 230 (Can.). That case set a judicially created cap at \$100,000 in 1978 dollars for the worst injury imaginable: a young person rendered quadriplegic and completely reliant on others. *Id.* at 265. That amount today, adjusted for inflation is approximately \$342,000 in 2015 Canadian dollars.

\$100,000 in 1978 Canadian dollars (about \$342,000 in 2015 Canadian dollars).³⁶ In addition, a number of provinces operate a no-fault automobile insurance system where the right to sue in tort for non-pecuniary damages is eliminated altogether.³⁷ In Ontario, the most populous province, the hybrid tort/no-fault automobile insurance system only allows injured automobile accident victims the right to sue for non-pecuniary damages if their injuries pass a verbal and quantitative threshold.³⁸ Punitive damages in Canada are comparatively far lower than their American counterparts, whether in the insurance bad faith context or otherwise. The test for punitive damages is exceedingly difficult for litigants to meet: wrongdoer conduct must be “malicious” and “high-handed.”³⁹ The high watermark in Canada was one million dollars in *Whiten v. Pilot Insurance Co.* in 2002 for an independent tort of bad faith against an insurance company that refused to pay a fire loss claim and accused the elderly insured couple of being arsonists who burned down their own home.⁴⁰ There was no evidence of arson, the couples’ cats died in the fire, and the husband froze his feet while standing in the snow in front of his blazing house.⁴¹ However, since *Whiten*, appellate courts have kept punitive damage awards far lower than the million-dollar mark for all kinds of cases. They generally hover around the \$20,000 mark, if awarded at all.⁴²

36. *Id.*

37. Knutsen, *supra* note 11, at 719-20.

38. *See id.* at 720 & n.15. The regulated verbal threshold for determining an accident victim’s entitlement to sue in tort includes death or the victim’s injury must be a “permanent serious disfigurement” or a “permanent serious impairment of an important physical, mental, or psychological function.” Insurance Act, R.S.O. 1990, c. I.8, s. 267.5(3) (Can.); *see also* Court Proceedings for Automobile Accidents that Occur on or After November 1, 1996, O. Reg. 461/96 (Can. Ont.). There is also a sliding statutory deductible for non-pecuniary damages claims of \$30,000 unless the non-pecuniary damages are found to be greater than \$100,000, in which case the deductible disappears. For family members of accident victims, the deductible is \$15,000 unless the non-pecuniary damages are found to be greater than \$50,000, in which case the deductible disappears. *See* Statutory Accidents Benefits Schedule, O. Reg. 34/10, ss. 32–46 (Can.).

39. *Whiten v. Pilot Ins. Co.*, [2002] 1 S.C.R. 595, 617 (Can.) (quoting *Hill v. Church of Scientology of Toronto*, [1995] 2 S.C.R. 1130 (Can.)).

40. *Id.* at 604–05.

41. *See id.* at 604.

42. *See, e.g.*, *Sagman v. Bell Tel. Co. of Can.*, 2014 ONSC 4183, para. 35 (Can. Ont.) (awarding punitive damages of \$50,000 in a case where \$300,000 general damages was awarded); *Ironside v. Delazzari*, 2014 ONSC 999, para. 72 (Can. Ont.) (awarding punitive damages of \$10,000 in a case where \$50,000 general damages was awarded); *Trout Point Lodge Ltd. v. Handshoe*, 2014 NSSC 62, para. 8 (Can. N.S.) (awarding punitive damages of \$25,000 each to two plaintiffs in a case where \$410,000 in total general damages was awarded); 122164 Can. Ltd. v. C.M. Takacs Holdings Corp., 2012 ONSC 6338, paras. 25, 29 (Can. Ont.) (awarding punitive damages of \$75,000 in a case where \$425,000 of general

The amounts at stake in Canadian insurance litigation are frequently far lower than the American counterpart. Canadian litigants risk an adverse costs award if they lose a case. Both of these factors mediate the frequency of Canadian insurance litigation. Having judges, not juries, deciding nearly all coverage-related issues also mediates predictability of coverage decisions to a significant degree.

II. THE CANADIAN APPROACH TO INSURANCE POLICY INTERPRETATION

The current approach to insurance policy interpretation in Canada can be seen as an amalgam of some traditions of an American contextualist approach and the traditional English strict textualist approach. This makes sense, considering the incredible influence of both countries on the common law of Canada. Canada began as an English colony and owes much of its common law genesis to English traditions. Yet it enjoys strong influence from its nearest neighbor—the United States. Because both America and Britain can be seen to take a different approach to insurance policy interpretation, it is not surprising that Canada has attempted to pick the best of both traditions in crafting its own jurisprudence in this area. The Canadian results are often patchwork and do not always hang together, as will be seen. Much of that is a result of the haphazard growth of legal precedent in the area, and a continuing lack of awareness as to the traditions and currency from which comparative principles and legal thinking is borrowed. All of this can be avoided with a few doctrinal tweaks, but historically equilibrium has yet to be achieved.

To demonstrate how the Canadian approach to insurance policy interpretation has arisen from American and British traditions, it is first helpful to explain those two countries' respective approaches. For the American tradition, the proposed Principles will be discussed as representing a middle ground position among the states.

A. *The American Approach in the Proposed Principles*

The proposed Principles of the Law of Liability Insurance attempts to chart some middle ground between a textualist and contextualist approach to insurance policy interpretation. Such a tactic appears to be chosen because there exists that same split within American insurance law jurisprudence.⁴³

damages was awarded).

43. STEMPEL, SWISHER & KNUTSEN, *supra* note 3, at 110–13; Swisher, *Judicial*

1. Presumption of Plain Meaning

The interpretive guidelines in the Principles employ a presumption favoring the plain meaning of insurance policy language while, at the same time, using the interpretive perspective of the reasonable policyholder as lens for keeping that plain meaning in perspective.⁴⁴ So “[t]he plain meaning of an insurance policy term is . . . that [which] a reasonable policyholder [in the policyholder’s circumstances] would give to that term[,] in relation to the claim at issue, in the context of the insurance policy as a whole, [and] without reference to [any] extrinsic evidence.”⁴⁵

2. Rebutting the Plain Meaning: Context and Purpose

This plain meaning can only be displaced if, after considering extrinsic evidence, a court finds that a reasonable policyholder would ascribe a different meaning to the term in the context of the case—some different meaning than that which a “text only” exercise can provide.⁴⁶ Extrinsic evidence is thus always admissible to displace the plain meaning initially arrived at by the court when the court uses only the text of the insurance policy as its interpretive source. Extrinsic evidence here includes pre-contractual dealings, course of performance evidence including past performance, drafting history of the policy, regulatory filings, other versions of similar policies, expert testimony of custom and practice of the insurance industry, and finally the history and purpose of the policy term.⁴⁷

This exercise introduces a bit of contextualist potential into the textualist plain meaning analysis by stressing context. The goal appears to be to show that the reasonable policyholder’s understanding of the term, in context, is superior to the plain meaning arrived at using the text of the policy alone.

Additionally, the interpretive analysis also appears to accommodate a consideration of purposive factors. Comment b to section 2 of the Principles details the “[o]bjectives of liability insurance policy interpretation”:

Interpretations, *supra* note 3, at 546–55; Swisher, *Judicial Rationales*, *supra* note 3, at 1038.

44. PRINCIPLES OF THE LAW OF LIAB. INS. § 3 (AM. LAW INST., Tentative Draft No. 1, 2013).

45. *Id.* § 3(3).

46. *Id.* § 3(2).

47. *Id.* § 3 cmt. e.

[1] effecting the dominant protective purpose of insurance; [2] facilitating the resolution of insurance-coverage disputes and the payment of covered claims; [3] encouraging the accurate marketing of insurance policies; [4] providing clear guidance on the meaning of insurance policy terms in order to promote, among other benefits, fair and efficient insurance pricing, underwriting, and claims management; and [5] promoting the financial responsibility of insured parties for the benefit of injured third parties.⁴⁸

These objectives are to provide guidance for the interpretation of insurance policies, again providing potential for a contextualist interpretation.

3. Ambiguity, Purpose, and Consumer Protectionism

If it is impossible to determine a plain meaning for a policy term, the term is ambiguous.⁴⁹ In this instance, a court can use all permissible sources of extrinsic evidence to attempt to construe a meaning.⁵⁰ If the court is still unable to determine the meaning of the term that a reasonable policyholder would ascribe to it, then the term is interpreted *contra proferentem*, against the insurer that drafted it.⁵¹ The reasonable expectations doctrine⁵² itself is not explicitly referenced in the Principles but rather its milder form as an interpretive guide only is imbedded in

48. *Id.* § 2 cmt. b.

49. *Id.* § 4(1).

50. *See id.* §§ 3 cmt. e, 4 cmt. d.

51. *Id.* § 4(3).

52. That doctrine has at least three permutations in American law, but basically holds that the reasonable expectations of the policyholder be given some credence in the interpretive analysis. *See* Robert E. Keeton, *Insurance Law Rights at Variance with Policy Provisions*, 83 HARV. L. REV. 961, 966–74 (1970) (noting the original proposal to validate the policyholder’s reasonable expectations when interpreting insurance policies—even if the text of the policy is counter to the policyholder’s expectations); *see also* Kenneth S. Abraham, *Judge-Made Law and Judge-Made Insurance: Honoring the Reasonable Expectations of the Insured*, 67 VA. L. REV. 1151, 1152–53 (1981). In the first version, a policyholder’s reasonable expectation is only considered in the event of ambiguity in a policy term. *See* Keeton, *supra*, at 967–73. In the second, the policyholder is entitled to all coverage reasonably expected from the wording in the policy, save and except where the policy language clearly excludes such coverage. *See id.* at 968–73. In the third version, the policyholder’s reasonable expectations can demand coverage even though the language of the policy may say otherwise. *See id.* at 967–68. The various versions of the reasonable expectations doctrine differ in the degree of credence: from ambiguity tiebreaker as it is used in most states that adopt the reasonable expectations doctrine to, in a very few states, permitting coverage despite actual policy wording to the contrary. *Id.* at 967-74.

the analytic structure of the Principles themselves, because the interpretive perspective of the reasonable policyholder in the policyholder's position is the lens through which the plain meaning can be challenged.⁵³

In construing a policy term, it is permissible to inquire into the purpose of the term. Such an inquiry is an objective one and can be determined from "learned 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."⁵⁴ Finally, courts can consider whether the ambiguity could have been reasonably avoided by the drafter of the policy, and can take such into account when attempting to determine the meaning of an ambiguous term.⁵⁵ "Insurance policy interpretation is a question of law."⁵⁶

B. *The English Approach*

England takes a decidedly textualist contractual approach to interpreting insurance policies.⁵⁷ In England, freedom of contract reigns supreme as the driving force behind insurance policy interpretation principles and practices.⁵⁸ Insurance policies are afforded no special status in the law and are considered to be just like any other commercial or consumer contract. The same rules of interpretation that apply to commercial contracts also apply to insurance policies.⁵⁹ In English law, there is no acknowledgement that standard form insurance policies are contracts of adhesion nor are there any doctrinal adjustments to interpretive principles to redress the power imbalance between insurer and policyholder.⁶⁰ There is also no examination of the function of an insurance policy as part of a wider compensatory system. English courts do not employ any consumer protectionist tenets like reasonable

53. PRINCIPLES OF THE LAW OF LIAB. INS. § 4 cmt. b (AM. LAW INST., Tentative Draft No. 1, 2013).

54. *Id.* § 4 cmt. m.

55. *Id.* § 4 cmt. n.

56. *Id.* § 2(2).

57. JOHN LOWRY & PHILIP RAWLINGS, *INSURANCE LAW: DOCTRINES AND PRINCIPLES* 223 (2d ed. 2005).

58. John Lowry & Philip Rawlings, *Proximate Causation in Insurance Law*, 68 MOD. L. REV. 310, 315–16 (2005).

59. See JOHN BIRDS, BEN LYNCH & SIMON MILNES, *MACGILLIVRAY ON INSURANCE LAW* 301–02 (12th ed. 2012) [hereinafter MACGILLIVRAY].

60. See Lowry & Rawlings, *supra* note 58, at 318.

expectations nor do they construe coverage clauses broadly and exclusion clauses narrowly.⁶¹ The same interpretive principles apply equally to coverage and exclusion clauses.⁶² In short, the fiction of a bargain between the insurer and policyholder is maintained in English law.⁶³

The main objective of the English approach to insurance policy interpretation is to ascertain the intention of the parties—*both* insurer and policyholder.⁶⁴ The inquiry becomes: what would a reasonable person in the position of the parties have thought? The basic tenets of insurance policy interpretation are the same as for all commercial contracts: the search is for the ordinary, objective meaning.⁶⁵ Meaning ascribed to words is that meaning that a reasonable person would ascribe.⁶⁶ Words are to be given their ordinary meaning, taking into account the context in which the term appears and the policy as a whole. The purpose of the policy itself can be taken into account (although this is a decidedly limited inquiry about just the policy at issue in the dispute). Because the interpretive exercise is decidedly contractual in nature, English courts also regularly employ traditional interpretive maxims like *ejusdem generis*,⁶⁷ *expressio unius*⁶⁸ or *noscitur a sociis*.⁶⁹

The interpretive inquiry typically starts with the consideration of other English jurisprudence interpreting the insurance policy term at issue, if any such court decisions exists.⁷⁰ English courts pay particular deference to other English judicial decisions that may have construed the same or similar policy language.⁷¹

If a policy term is ambiguous, English courts construe that term *contra proferentem*. However, *contra proferentem* cannot be used to manufacture an ambiguity that did not exist prior to the inquiry itself.

61. *Id.* at 317.

62. *Id.*

63. LOWRY & RAWLINGS, *supra* note 57, at 223.

64. See JOHN BIRDS, BIRDS' MODERN INSURANCE LAW 239–40 (9th ed. 2013).

65. See *Inv'rs Comp. Scheme Ltd. v. W. Bromwich Bldg. Soc'y* [1997] HL 28 (Eng.).

66. BIRDS, *supra* note 64, 240–44; MALCOLM A. CLARKE, THE LAW OF INSURANCE CONTRACTS 397–409 (5th ed. 2006); MACGILLIVRAY, *supra* note 59, at 301–22; ROBERT MERKIN & RAOUL P. COLVINAUX, COLVINAUX'S LAW OF INSURANCE 117 (9th rev. ed. 2010).

67. MACGILLIVRAY, *supra* note 59, at 310. This rule holds that items in a specific list are limited only to those items, and courts cannot construe the list as being more expansive. BIRDS, *supra* note 64, at 240.

68. CLARKE, *supra* note 66, at 405. This rule holds that an express mention of one thing must exclude all others. *Id.*

69. MACGILLIVRAY, *supra* note 59, at 311. This rule holds that, in a list of words that display an uncertain scope, the character of the scope is to be taken from those words surrounding the term, if they have a recognizable feature.

70. *Id.* at 302.

71. BIRDS, *supra* note 64, at 239; CLARKE, *supra* note 66, at 399–400; MERKIN & COLVINAUX, *supra* note 66, at 115.

There is evidence that *contra proferentem* is often used as a tiebreaker in the interpretive exercise, as the ambiguity determination on the front end can often be in the eye of the beholder.⁷²

Finally, English courts aim to achieve a commercially sensible result.⁷³ If a literal meaning produces a ludicrous result, such should be avoided.⁷⁴

The rules of interpretation are not immutable and can be changed via contract.⁷⁵ The question of construction is a question of law,⁷⁶ and English courts do not use juries. Insurance policies are not required to go through a governmental approval or regulatory process.⁷⁷ The regulation of insurance policy language is thus left to the common law courts.⁷⁸

English courts do not consider extrinsic evidence in the interpretive exercise.⁷⁹ They employ a purist form of the *parol evidence rule*.⁸⁰ There is no inquiry into prior negotiations, subjective intent of the parties, nor underwriting or industry practices. The prospectus of an insurance company is not relevant to the interpretation of a policy term, for example.⁸¹

John Lowry and Philip Rawlings explain that one reason why England does not treat insurance policies any differently than any other bargained-for contract is because there is no perceived public policy flavor to insurance in England, as contrasted with the United States.⁸² In America, they argue, insurers (and especially liability insurers) are expected to provide a public interest good via insurance, so it is necessary that American law take a broader interpretive approach that favors consumer protection and compensation.⁸³ England is, by contrast, a welfare state with publicly funded healthcare. Most insurance disputes

72. John Birds notes that “even the judges cannot always agree as to whether or not sufficient ambiguity exists.” BIRDS, *supra* note 64, at 247.

73. *Id.* at 240–41; *see also* CLARKE, *supra* note 66, at 418; MACGILLIVRAY, *supra* note 59, at 304.

74. LOWRY & RAWLINGS, *supra* note 57, at 315; MACGILLIVRAY, *supra* note 59, at 305.

75. MERKIN & COLVINAUX, *supra* note 66, at 114.

76. BIRDS, *supra* note 64, at 239.

77. JOHN BIRDS, *INSURANCE LAW IN THE UNITED KINGDOM* 23 (2d ed. 2014).

78. *Id.*

79. *See* BIRDS, *supra* note 64, at 240; MERKIN & COLVINAUX, *supra* note 66, at 117.

80. CLARKE, *supra* note 66, at 407; MALCOLM CLARKE, *POLICIES AND PERCEPTIONS OF INSURANCE LAW IN THE TWENTY-FIRST CENTURY* 381–83 (2005); LOWRY & RAWLINGS, *supra* note 57, at 223; MACGILLIVRAY, *supra* note 59, at 319. Indeed, Malcolm Clarke notes that English courts take a decidedly cautious approach to any background inquiry about anything other than the text of an insurance policy.

81. MACGILLIVRAY, *supra* note 59, at 313.

82. Lowry & Rawlings, *supra* note 58, at 317–18.

83. *See id.* at 318.

thus involve commercial insurance, so there is far less need to focus on individual consumer rights.⁸⁴

Another, perhaps, more likely explanation for England's strict textualist response to insurance law may simply be a greater deference to a common law tradition of textualism that is very difficult to shake, even in today's modern world. One only has to be reminded that the birthplace of insurance was in England with Lloyd's to understand the immense influence that that industry has on English commercial life and the law.⁸⁵ It is curious indeed how the birthplace of the common law system itself could continue to somehow still hold tight to the fiction of the bargain between insurer and policyholder in the face of today's standard form insurance policies where no bargaining is typically to be had.

Further evidence of the resistance toward ideals of consumer protection in the insurance sphere can be seen by reviewing how English courts and English authors of insurance treatises staunchly and consistently reject any notion about importing American insurance concepts into English law. It is fascinating that all standard English treatises say something about this issue. Apparently, in the eyes of some English commentators, the large volume of American case authority and the "consumer-friendly attitude" of certain American courts make American insurance jurisprudence an ill fit in English law.⁸⁶ Many English treatises and decisions specifically note that England does not follow the American-style doctrine of reasonable expectations and therefore anything "American" would not do in an English insurance law court (perhaps for fear of contamination?).⁸⁷ This is in complete contrast to the warm reception of American insurance law ideas in Canadian law.

84. *Id.*

85. See KENNETH S. ABRAHAM, *THE LIABILITY CENTURY: INSURANCE AND TORT LAW FROM THE PROGRESSIVE ERA TO 9/11*, at 14–22 (2008).

86. MERKIN & COLVINAUX, *supra* note 66, at 115; accord CLARKE, *supra* note 66, at 395–96; MACGILLIVRAY, *supra* note 59, at 303. Indeed, John Birds states that

[i]t could be argued that the principles from the American cases are somewhat vague so that it would be difficult, if not impossible, to predict the result on the facts of any particular case, and that, if further interference with policy terms is felt to be justified, it would be better to have a regime of prior approval of policy forms within guidelines laid down by statute.

BIRDS, *supra* note 64, at 236.

87. LOWRY & RAWLINGS, *supra* note 57, at 223; MACGILLIVRAY, *supra* note 59, at 303; see also *Yorkshire Water Servs. Ltd. v. Sun All. & London Ins. PLC* [1997] 2 Lloyd's Rep. (AC) 21, [28] (Eng.); *Smit Tak Offshore Servs. v. Youell* [1992] 1 Lloyd's Rep. (AC) 154, [159] (Eng.).

C. The Canadian Approach

1. Anglo-American Influences in Canadian Insurance Law

It is first important to understand that, unlike American or English courts, Canadian courts are widely receptive and indeed interested in jurisprudential developments in Anglo-American courts.⁸⁸ Comparative jurisprudence and foreign legal scholarship is regularly cited and relied upon as being persuasive in Canadian court cases at all levels. In fact, insurance law stands prime among Canadian jurisprudential subjects as probably exhibiting the heaviest use of American and English legal precedents.

This perhaps curious tradition makes sense when you think about the incredible influence both England and America have—and have had—on all aspects of life of the comparatively smaller Canada. Canada's legal tradition is borne out of its English colonial roots. Even today, English law has influence in Canadian courts as being highly persuasive. This is in part a nod to its historical influence as, in the past, it was common for many leading Canadian jurists to obtain legal training in Britain. However, Canada's locational and cultural proximity to the United States has also meant that Canadian courts frequently are faced with having to understand the directions of American jurisprudence and whether or not American courts have already solved a problem that Canadian courts have yet to encounter. In the insurance sphere, common wording of common insurance policy provisions makes the area ripe for comparative legal treatment.⁸⁹ Why reinvent the wheel if someone has

88. See, e.g., S.I. Bushnell, *The Use of American Cases*, 35 UNBLJ. 157, 158–60 (1986) (highlighting the Supreme Court of Canada's increasing trend from 1876 to 1983 of citing American case law). In insurance law, such has been a trend since at least 1914. See, e.g., *Cunningham v. St. Paul Fire & Marine Ins. Co.*, [1914] 16 D.L.R. 39, 42 (Can. B.C. S.C.C.); *McCoy v. Nat'l Benefit Life & Prop. Assurance Co.* [1918] 1 W.W.R. 466, 466 (Can. B.C. C.A.) (“In the absence of English and Canadian authorities it is well to have regard to American authorities in fire-insurance cases.”), *aff'd*, [1918] 57 S.C.R. 29 (Can.); see also *Bonser v. London & Midland Gen. Ins. Co.* (1969), 7 D.L.R. 3d 561, 568–69 (Can. Ont. H.C.), *aff'd*, [1973] S.C.R. 10 (Can.).

89. *Re Partners Invs. Ltd.* (1981), 124 D.L.R. 3d 125, 126 (Can. Ont. H.C.) (“The insurer carries on business in the United States of America as well as Canada. The same all-risk policy with precisely the same exclusion clauses has been interpreted by American Courts. It might then be assumed that the insurer, and perhaps also the insured, would expect the policy to be interpreted in a similar manner in Canada as in the United States. It would be in the best interests of both the insurer and its clients in the business community if the interpretation of the policy was the same on both sides of the border. With this in mind, it might be helpful if I indicate what I take to be the position set forth by the American cases and then determine whether the reasoning in those cases is contrary to Canadian authorities that are binding upon me.”); *Commerce Capital Tr. Co. v. Cont'l Ins. Co.* (1982),

attempted to solve a near-identical issue about an identical phrase and is closely related in terms of legal traditions and culture?

Recently, interest in English insurance law precedents has waned in preference for American insurance law. This may be due to a combination of factors. Primary among them is the fact that Canadian courts place a high degree of importance on consistency in judicial interpretation of insurance policy terms.⁹⁰ The first place of reference for any insurance policy interpretation question is, therefore, to other court decisions construing the same or similar terms. Second, insurance policy wording is remarkably consistent between Canada and the United States, making comparisons of judicial decisions construing the same or similar wording helpful between jurisdictions. Many American insurers have Canadian divisions. Third, American insurance jurisprudence features some consumer protection principles that have been adopted in Canada, but not in Britain, and thus analogies to the two countries are more apt. The traditions are not that different. Fourth, the sheer number of available American insurance law decisions and treatises simply makes finding a case on point that much easier. It is often difficult to even locate wording for English insurance policies as the industry itself is very different and, in many instances, can feel foreign or arcane to a Canadian lawyer. Fifth, as a practical matter, Canadian lawyers seeking to do some foreign law

133 D.L.R. 3d 459, para. 19 (Can. Ont. H.C.) (“In my view this reasoning is particularly compelling when as in this case, there are well-reasoned U.S. authorities which construe insurance policies which are virtually identical to the one in dispute.”); *Zurich Ins. Co. v. 686234 Ont. Ltd.* (2002), 222 D.L.R. 4th 655, para. 34 (Can. Ont. C.A.) (“[W]here there is little or no Canadian authority on a point of insurance law, our courts have turned to American law for assistance. This is particularly so where the same provision, such as the absolute pollution liability exclusion in CGL policies, is in common use by the insurance industry in Canada and the United States and where the American authorities have applied rules of construction not materially different from our own.”); *Clarkson Co. v. Canadian Indem. Co.* (1979), 101 D.L.R. 3d 146, para. 18 (Can. Ont. H.C.) (“In my opinion, this is the approach of reason. In the absence of binding authority in one’s own jurisdiction, assistance should be sought where it can be found, whether from the Courts of other Provinces of Canada or from the Courts of other countries.”).

90. *See, e.g., Co-operators Life Ins. Co. v. Gibbens*, [2009] 3 S.C.R. 605, 619 (Can.). (“As Newbury J.A. pointed out in the court below, ‘courts will normally be reluctant to depart from [authoritative] judicial precedent interpreting the policy in a particular way’ where the issue arises subsequently in a similar context, and where the policies are similarly framed. Certainty and predictability are in the interest of both the insurance industry and their customers.” (alteration in original) (citation omitted)); *see also Algoma Steel Corp. v. Allendale Mut. Ins. Co.* (1990), 72 O.R. 2d 782, para. 14 (Can. Ont. C.A.) (“When words in a policy have once been judicially interpreted, they will be construed in the same way should their meaning be in issue in a subsequent case. Where the Court has already decided the meaning of words used in a policy of insurance, the doctrine of precedent will be applied, and the same interpretation will be given should the meaning of the same words be in issue in a later case.”).

research can more easily find American legal decisions in searchable electronic format or in a treatise than English legal decisions. Sixth, there are stronger insurance industry and insurance practicing bar ties between Canada and the United States, incentivizing information flow about litigation tactics and trends. There are frequent cross-border conferences, and Canadian lawyers regularly take part in American insurance continuing legal education opportunities. Finally, there is a general trend in Canadian law of increasing comfort and preference with utilizing American jurisprudence in Canadian courts. This may, in part, be due to the fact that many more jurists now seek graduate legal education in the United States as opposed to Britain. That has meant that generations of jurists with American legal education are now quite comfortable in doing American legal research, in all of its nuances. Whatever the reason, the recent fondness for utilizing American legal precedents in Canadian insurance policy coverage decisions shows no signs of decreasing. This influence has set Canada up to follow an American-influenced, sometimes peripatetic patchwork contextualist approach to insurance policy interpretation.

2. How Canadian Courts Interpret Insurance Policies

The Canadian approach to insurance policy interpretation—in doctrine and in practice—is a patchwork amalgam of both the English and American approaches. Depending on the type of insurance policy targeted in the analysis, Canadian courts utilize two different interpretive models: a legislative model for legislated automobile insurance policies and a contractual model for every other type of policy.⁹¹

a. The Contractual Model

The contractual model of interpretation is used for interpreting all insurance policies not enshrined in legislation. As will be discussed below, many Canadian courts also mistakenly fall into using this model to interpret legislated automobile policies as well. Unlike in English courts but similar to American courts, Canadian courts recognize that insurance policies are contracts of adhesion and therefore some consumer protection principles are important to employ in certain instances in the interpretive exercise.⁹² The myth of the bargain between insurer and

91. Knutsen, *supra* note 11, at 723–24.

92. *See, e.g.,* Brissette v. Westbury Life Ins. Co., [1992] 3 S.C.R. 87, para. 37 (Can.) (“The American courts have reasoned that insurance policies are contracts of ‘adhesion’ and therefore ambiguities contained in them should be resolved in favour of the insured.”); *see*

policyholder is, however, maintained to some degree.⁹³ Its practical effect is far more muted than in English law because the Canadian contractual approach attempts to balance this bargain myth against an acknowledgement that insurance policies are contracts of adhesion.⁹⁴ The end result is that courts try to correct for the fact that policyholders may have the choice to accept or reject the purchase of a policy (or additional coverage), but they typically have little ability to alter a specific term in a policy itself.⁹⁵

The Supreme Court of Canada has set a basic common law framework for the contractual model of insurance policy interpretation.⁹⁶ It is interesting to note that, over time, the Court itself never consistently repeats the framework in the same language or even orders the principles to be applied in the same sequence. Each time the principles of the contractual model are restated, they are done so with slight explanatory additions or the order of interpretive steps is different. This has created some palpable inconsistencies in applying the principles because courts cannot ascertain the primacy of various principles, when to apply them, and how they relate to each other.

The contractual model of interpretation involves a two-stage process: the “intention” stage and the “ambiguity” stage.⁹⁷ The grounding for the process is, of course, the text of the policy itself. The intention stage attempts to discern the objective intention of the parties in the insurance bargain. This involves using the policy text as a reference to figure out what the insurer and policyholder meant when they struck the bargain. At this stage, the text of the policy is examined to discern the plain meaning of the insurance policy, read as a whole. The goal is to determine the commercially sensible result intended by the parties to the policy. To aid in this plain-meaning analysis, words are to be given their

also *Gibbens*, [2009] 3 S.C.R. at para. 23; *Jesuit Fathers of Upper Can. v. Guardian Ins. Co. of Can.*, [2006] 1 S.C.R. 744, para. 28 (Can.); *Non-Marine Underwriters, Lloyd’s of London v. Scalera*, [2000] 1 S.C.R. 551, para. 70 (Can.).

93. *Knutsen*, *supra* note 11, at 724.

94. *See, e.g.*, *Fletcher v. Manitoba Pub. Ins. Co.*, [1990] 3 S.C.R. 191, para. 80 (Can.); *Scott v. Wawanesa Mut. Ins. Co.*, [1989] 1 S.C.R. 1445, 1455–59 (Can.); *Consol.-Bathurst Exp. Ltd. v. Mut. Boiler & Mach. Ins. Co.*, [1980] 1 S.C.R. 888, 901–02 (Can.).

95. *Knutsen*, *supra* note 11, at 724.

96. *See Progressive Homes Ltd. v. Lombard Gen. Ins. Co. of Can.*, [2010] 2 S.C.R. 245, 260 (Can.); *Gibbens*, [2009] 3 S.C.R. at para. 20; *Jesuit Fathers*, [2006] 1 S.C.R. at para. 27; *Scalera*, [2000] 1 S.C.R. at paras. 70–71; *Derksen v. 539938 Ont. Ltd.*, [2001] 3 S.C.R. 398, para. 49 (Can.); *Reid Crowther & Partners Ltd. v. Simcoe & Erie Gen. Ins. Co.*, [1993] 1 S.C.R. 252, 269 (Can.); *Brissette*, [1992] 3 S.C.R. at para. 43; *Wawanesa*, [1989] 1 S.C.R. at 1455–59; *Consol.-Bathurst*, [1980] 1 S.C.R. at 901.

97. *Knutsen*, *supra* note 11, at 724; *see also BILLINGSLEY*, *supra* note 7, at 137–39; CRAIG BROWN, *INSURANCE LAW IN CANADA* § 8.2 (8th Student ed. 2013) (looseleaf).

ordinary, literal and non-technical meanings. The policy is to be interpreted as a whole. Additionally, Canadian courts very frequently make use of dictionary definitions to aid in construction of policy terms,⁹⁸ despite some strong Canadian jurisprudence cautioning against such a practice.⁹⁹ As has been mentioned above, the starting point for analysis is typically reference to other court decisions interpreting similar policy terms. If insurance coverage for obvious risks insured against by the policy would be nullified because of the plain meaning interpretation arrived at by the court, Canadian courts will not maintain such an interpretation.¹⁰⁰ The intention stage of the Canadian contractual model owes its genesis to the traditional English textualist, contractual approach to insurance policy interpretation. It is nearly identical to the English approach. But it is the first in a two-stage process.

The second stage, the ambiguity stage of the process, owes its genesis to the consumer-protectionist principles found in American insurance law. If, in attempting to discern the intention of the parties in the intention stage, a court determines the policy term is ambiguous, the court is to proceed to the “ambiguity” stage to solve the ambiguity.¹⁰¹ The finding of ambiguity is the gatekeeper to these principles. At this stage, the fiction of the bargain gives way to the notion that standard form insurance policies are contracts of adhesion. To that end, to redress the imbalance of bargaining power, courts are to interpret coverage clauses broadly and exclusion clauses narrowly. A court may also construe any ambiguous term *contra proferentem*, as against the insurer. A court may also give effect to the reasonable expectations of the parties in order to resolve ambiguity. There is a significant difference in the reasonable expectations doctrine as espoused in Canadian law as compared to its American counterpart: in Canada, it is the reasonable expectations of insurer *and* policyholder, not just policyholder, that are to be considered in construing an ambiguous policy term.

Canadian courts generally purport to uphold the inadmissibility of parol evidence in an insurance context,¹⁰² but there are some very notable

98. See, e.g., *Appel v. Dominion of Can. Gen. Ins. Co.*, [1998] 1 W.W.R. 592, para. 68 (Can. B.C. C.A.) (welcoming the dictionary usage in interpretation because insurance policies are to be understandable to laypersons); *Wellington Guarantee v. Evangelical Lutheran Church in Can.*, 1996 CanLII 8316, para. 21 (Can. B.C. C.A.).

99. See, e.g., *Stats v. Mut. of Omaha Ins. Co.*, [1978] 2 S.C.R. 1153, para. 25 (Can.).

100. See, e.g., *Excel Cleaning Serv. v. Indem. Ins. Co. of N. Am.*, [1954] S.C.R. 169, paras. 34–35 (Can.); *Cabell v. Pers. Ins. Co.* (2011), 331 D.L.R. 4th 460, para. 14 (Can. Ont. C.A.) (determining coverage for damage to pool would be nugatory under literalist interpretation when endorsement itself was solely for property damage to pool).

101. Knutsen, *supra* note 11, at 724.

102. See, e.g., *Ryan v. Sun Life Assurance Co. of Can.* (2005), 249 D.L.R. 4th 628, para.

exceptions which, in practice, appear to mean that Canadian courts readily consider much in the way of extrinsic evidence. Extrinsic evidence is allowed in Canadian courts at the ambiguity stage to resolve an ambiguity.¹⁰³ Evidence of the surrounding circumstances, or factual matrix, which would reasonably be known to the parties, is also admissible at any time in the construction exercise.¹⁰⁴ So is evidence of drafting history¹⁰⁵ and other coverage or wordings in other policies in the marketplace.¹⁰⁶ Evidence from brokers and underwriters is also admissible,¹⁰⁷ as is insurer marketing literature.¹⁰⁸ The limit to the actual use of extrinsic evidence appears to be only the limit of the creativity of legal counsel.

It is surprising that extrinsic evidence is actually having a limited impact in Canadian insurance interpretation cases. In most cases, extrinsic evidence has been limited to the use of dictionary definitions,¹⁰⁹ a resort to which Canadian courts unfortunately often fall—and sometimes with troubling results. In a few cases,¹¹⁰ the extrinsic evidence has been the marketing and promotional literature of the insurer about the policy, evidence of industry or underwriting practice, drafting history of policy provisions, historical revisions of insurance policy language, and

25 (Can. N.S. C.A.).

103. See, e.g., *Grand & Toy Ltd. v. Aviva Can. Inc.* (2010), A.C.W.S. 3d 219, para. 3 (Can. Ont. C.A.).

104. *Creston Moly Corp. v. Sattva Capital Corp.*, [2014] 2 S.C.R. 633, paras. 47, 61 (Can.).

105. *Zurich Ins. Co. v. 686234 Ont. Ltd.* (2002), 62 O.R. 3d 447, paras. 13–16 (Can. Ont. C.A.) (considering drafting history of a pollution liability exclusion clause).

106. See, e.g., *Jesuit Fathers of Upper Can. v. Guardian Ins. Co. of Can.*, [2006] 1 S.C.R. 744, para. 63 (Can.) (noting the availability of other clauses on the market that the insured could have purchased); *Bridgewood Bldg. Corp. v. Lombard Gen. Ins. Co. of Can.* (2006), 266 D.L.R. 4th 182, para. 21 (Can. Ont. C.A.) (considering that other coverage was available which the insurer had not offered to the policyholder); *Derksen v. 539938 Ont. Ltd.*, [2001] 3 S.C.R. 398, 416–17, paras. 46–48 (Can.) (noting availability of clearer language in other policies that would have avoided problem insurer faced, had insurer used similar language).

107. See, e.g., *Pietrangelo v. Gore Mut. Life Ins. Co.* (2010), 198 A.C.W.S. 3d 1120, para. 10 (Can. Ont. Sup. Ct. J.) (considering evidence from broker and underwriter about purpose of marijuana grow operations exclusion), *aff'd*, (2011), 198 A.C.W.S. 3d 812 (Can. Ont. C.A.).

108. See, e.g., *Wigle v. Allstate Ins. Co. of Can.* (1984), 5 D.L.R. 4th 327, para. 3 (Can. Ont. C.A.); *Chilton v. Co-operators Gen. Ins. Co.* (1997), 143 D.L.R. 4th 647 (Can. Ont. C.A.); *Pietrangelo*, 198 A.C.W.S. 3d at para. 19 (considering letter from insurer to policyholders explaining addition of new marijuana grow operations exclusion to policy).

109. See, e.g., *Ricketts v. Moore* (2001), 206 D.L.R. 4th 273, para. 14 (Can. Ont. C.A.) (using dictionary definition of “motorized land vehicle” to control interpretation of phrase in homeowner’s policy; coverage excluded for accident resulting from child’s ride-on toy go-kart, when such would never be covered under standard automobile insurance policy either).

110. See cases cited *supra* notes 106.

experience in other jurisdictions with this particular policy language. Of course, those cases that have a fuller record of extrinsic evidence have made a far greater impact on Canadian insurance law and have produced far more sensible and defensible insurance law decisions. It is thus a mystery as to why more policyholder counsel do not adduce extrinsic evidence more frequently when mounting their cases.

Finally, questions of insurance policy interpretation have been determined to be questions of mixed law and fact, attracting a higher standard of appellate review.¹¹¹ This is a recent development in Canadian law and one which differs from American and English approaches to this question. The thinking behind this is that the application of a set of facts to contractual language (including, apparently, insurance policy language) is not a purely legal question because it involves discerning the intention of the parties. The meaning must come from the context of the bargain and the surrounding circumstances. That, therefore, is a factual question. It remains to be seen what effect this will have on future insurance policy interpretation jurisprudence.

b. The Legislative Model

In stark contrast, the Canadian legislative model of insurance policy interpretation produces highly consistent interpretive results. The jurisprudence is a much more stable body of law. This may in part be because it is the standard work of courts to construe legislation. They are good at it. But it is also likely due to the fact that the approach has a set of simple, consistent interpretive tools that are easy to apply in a like manner and produce publicly acceptable results. That may, therefore, be a strong indication that this approach would produce superior interpretive results for even non-legislated insurance policy interpretation as well, as will be discussed below.

At present, the legislative model of insurance policy interpretation is reserved only for automobile insurance policies that have been drafted as legislation by provincial governments. However, these policies are worded nearly verbatim to their contractual counterparts in other jurisdictions like the United States and England. They have identically worded coverage clauses¹¹² and exclusions.¹¹³ The only difference is they are

111. See *Creston Moly Corp. v. Sattva Capital Corp.*, [2014] 2 S.C.R. 633, paras. 49, 66 (Can.) (finding errors of mixed law and fact subject to the palpable and over-riding error standard of appellate review).

112. For example, coverage for “ownership, use, and operation” of an automobile.

113. For example, exclusions for driving without a valid driver’s license, or without the consent of the owner of the vehicle.

blessed by the provincial legislature and enshrined in a statute or regulation. That allows a court, apparently, to use a legislative model to interpret the policy.

The legislative model is the same model Canadian courts use for any statutory interpretation exercise. Canada employs a purposive and holistic approach to construing legislation. The model requires that “the words of an Act . . . be read in their entire context and in their grammatical and ordinary sense harmoniously with the scheme of the Act, the object of the Act, and the intention of Parliament.”¹¹⁴

The legislative model contains a decidedly purposive element to it that is missing in the contractual model. It does not rely on a finding of ambiguity first before considering the scheme, object, and intention of the coverage-granting instrument. Therefore, these purposive inquiries about the policy and its job it should be doing in society are part of the entire interpretive exercise. The model is thus a real-life example of Jeff Stempel’s notion of treating the insurance policy as statute.¹¹⁵ And, in the main, it works.

This purposive inquiry has led Canadian courts to recently adopt a nuanced understanding of the role of automobile liability insurance in the Canadian accident-compensation system. Two recent Canadian court of appeal decisions have held that, in interpreting automobile insurance policy terms, courts must be mindful of the role of automobile insurance in society and interpret the terms with an eye to the policy being more of a “social contract” with Canadian society.¹¹⁶ Automobile insurance is a highly regulated, mandatory insurance that provides the all-important backbone to society’s accident compensation needs. To that end, a broad and purposive approach that considers the compensatory nature of this insurance must be employed in any interpretive exercise. This notion of automobile insurance as a social contract drives Canadian insurance law, at least in the auto context, and is parallel to Jeff Stempel’s idea of insurance as a social institution.¹¹⁷

Despite the seemingly efficient and wholesome application of the legislative model in the auto context in Canada, most Canadian courts

114. *Marche v. Halifax Ins. Co.*, [2005] 1 S.C.R. 47, para. 54 (Can.) (quoting ELMER A. DRIEDGER, *CONSTRUCTION OF STATUTES* 87 (2d ed. 1983); *accord* Knutsen, *supra* note 11, at 723.

115. *See* Jeffrey W. Stempel, *The Insurance Policy as Statute*, 41 MCGEORGE L. REV. 203 (2010).

116. *See* *Niedermeyer v. William Charlton & Ziptrek Ecotours Inc.*, 2014 CanLII 165, para. 101 (Can. B.C. C.A.) (adopting this idea from Knutsen, *supra* note 11, at 717); *accord* *Abarca v. Vargas*, 2015 CanLII 4, paras. 38, 40 (Can. Ont. C.A.).

117. *See* Jeffrey W. Stempel, *The Insurance Policy as Social Instrument and Social Institution*, 51 WM. & MARY L. REV. 1489 (2010).

interpreting legislated automobile insurance policies actually incorrectly follow the contractual model.¹¹⁸ The contractual model, in the auto context, has resulted in decisions which have left troubling gaps in coverage and produced difficult-to-resolve precedential conflicts in the auto policy interpretation jurisprudence, especially in instances involving overlapping insurance coverage between auto and non-auto policies. This, in turn, has resulted in a costly increase in unnecessary litigation about the same policy terms over and over again, as court results are unpredictable because the interpretive model choice is itself unpredictable in result. The reason for this switching of models may be simply that neither counsel nor courts at the trial level know any better—an unfortunate thing.

III. ELEMENTS OF AN INSURANCE POLICY INTERPRETATION FRAMEWORK

The Canadian approach to insurance policy interpretation, when contrasted with both the American Principles' proposed approach and the British approach, helps to reveal some of the pluses and pitfalls of the Principles. The key benefits of Canada's patchwork amalgam of contextualism and textualism can be retained in any new model for interpretation. The troubling detriments of the amalgam can hopefully be avoided.

A. *Contract, Policy, or Something Else?*

The starting point for informing any decisions as to what interpretive tools are required for insurance policy construction should be to figure out first what, precisely, is the target of construction. What is an insurance policy? The innate qualities of the instrument being interpreted need to inform this initial screening of what doctrinal tools may or may not be necessary for the job. Various models exist for attempting to define the nature of insurance policies and thus how they should be treated in the law. Interestingly, each model incorporates a

118. Knutsen, *supra* note 11, at 725, 733-35; *see, e.g.*, Somersall v. Friedman, [2002] 3 S.C.R. 109 (Can.); Derksen v. 539938 Ont. Ltd., [2001] 3 S.C.R. 398 (Can.); Fletcher v. Manitoba Pub. Ins. Co., [1990] 3 S.C.R. 191, para. 80 (Can.); Scott v. MacNab, [1999] O.J. No. 3260 (Can. Ont. C.A.) (QL); Morton v. Rabito (1998), 42 O.R. 3d 161 (Can. Ont. C.A.) (using contractual model to construe definition of "automobile" in provincially legislated automobile liability insurance policy); Regele v. Slusarczyk (1997), 33 O.R. 3d 556 (Can. Ont. C.A.); Wigle v. Allstate Ins. Co. of Can. (1984), 5 D.L.R. 4th 327 (Can. Ont. H.C.J.); Chilton v. Co-operators Gen. Ins. Co. (1997), 143 D.L.R. 4th 647 (Can. Ont. C.A.).

move away from strict textualism, toward a more nuanced and purposive approach to interpretation.

Jeff Stempel has argued that insurance policies should be treated akin to statutes or social institutions, whereby the policy should be treated in a similar fashion to legislation and the social purpose of insurance needs to be taken into account.¹¹⁹ Daniel Schwarcz has called for a products liability approach to insurance policy construction where policies should be regulated as consumer goods and a legal regime should be developed for policing defective policies offered on the insurance market in a similar fashion to how defective products are dealt with.¹²⁰ The author of this Article has made a case that insurance policies, at least in the auto context, should be treated as social contracts—highly regulated instruments affecting larger, public-minded goals in the fabric of the accident compensation web in society.¹²¹ Such an approach should draw from public law legislative traditions and incorporate societal and market considerations into how insurance policies are interpreted. While English courts and commentators maintain that insurance policies are commercial contracts, American and Canadian courts and commentators make compelling cases that insurance policies are something more. At the very least, they are contracts on steroids. As such, they deserve special doctrinal treatment to be loyal to their special purpose as contracts “plus.”

The Principles consistently refers to an insurance policy as a “policy.”¹²² It has avoided using the term “insurance contract.” One can assume this was by conscious choice. The Principles acknowledges the policy is a contract of adhesion, where the consumer has no choice as to wording of the terms. The choice of the descriptor “policy” could be seen to implicitly hint that this written instrument is something different—not just any bargained-for “contract.” Liability insurance policies are the compensatory backbone of the accident compensation system.¹²³ Mandatory automobile insurance for drivers is the classic example.

119. Stempel, *supra* note 115, at 205; Stempel, *supra* note 117, at 1495, 1498.

120. Daniel Schwarcz, *A Products Liability Theory for the Judicial Regulation of Insurance Policies*, 48 WM. & MARY L. REV. 1389, 1396–98 (2007).

121. Knutsen, *supra* note 11.

122. See PRINCIPLES OF THE LAW OF LIAB. INS. (AM. LAW INST., Tentative Draft No. 1, 2013).

123. See generally Tom Baker, *Liability Insurance as Tort Regulation: Six Ways that Liability Insurance Shapes Tort Law in Action*, 12 CONN. INS. L.J. 1 (2005); Knutsen, *supra* note 11; Erik S. Knutsen, *Confusion About Causation in Insurance: Solutions for Catastrophic Losses*, 61 ALA. L. REV. 957 (2010); Erik S. Knutsen, *Fortuity Victims and the Compensation Gap: Re-envisioning Liability Insurance Coverage for Intentional and Criminal Conduct*, 21 CONN. INS. L.J. 209 (2014).

Therefore, an insurance policy's construction requires special doctrinal tools and considerations not found in commercial contract law. Those tools may bridge the gap between a textualist and contextualist approach, recognizing that pure textualism is inappropriate for a product on the market whose terms a consumer either takes or leaves.

English law, by contrast, consistently refers to insurance policies as "contracts." England adopts a purely contractual, textualist bargain theory approach to insurance policy interpretation.¹²⁴ There is no room for any consumer protectionist doctrine in the interpretive approach used.¹²⁵

Canada strikes an uneasy middle ground with the definition of what is insurance, similar to the Principles' attempt to straddle both extremes. While Canadian courts will often use the term "contract" in decisions, the interpretive process incorporates concepts that expressly recognize the adhesionary nature of insurance policies and the imbalance of power between insurer and policyholder. The problem is that, by using the term "contract" and grounding the first stage of interpretation in a largely textualist approach (the "intention" stage), most Canadian cases start and finish as a textualist interpretive endeavor. They never get to the second "ambiguity" stage at all.¹²⁶ The recognition of an insurance policy as something as a "contract plus" does not get a chance to come into play in the analysis. Only when there is ambiguity, in the more contextualist "ambiguity stage" of analysis, does the discussion move to a broader conception of an insurance policy as something more than a mere "contract."¹²⁷ The major exception in Canadian insurance jurisprudence is the treatment of automobile insurance policies, as noted above, where automobile policies have recently been interpreted as keeping with their public purpose as part of the necessary compensatory fabric of a regulated society. The Canadian approach to "what is insurance" is thus peripatetic—and does little to ground the interpretive analysis. That is

124. LOWRY & RAWLINGS, *supra* note 57, at 223.

125. *Id.*

126. A superlative example of this is the majority decision in *Scott v. Wawanese Mutual Insurance Co.*, [1989] 1 S.C.R. 1445 (Can.). In that case, a teen set fire to his home and his parents were denied insurance coverage for the loss as the teen was considered an "insured" under their policy and there was an exclusion clause removing coverage for intentional acts of "insureds." *Id.* at 1445. The majority of the Supreme Court of Canada found the definition of "insured" in a homeowners policy to be perfectly clear and unambiguous on its face, thus stopping the interpretive analysis at the first "intention" stage and relying solely on a textualist approach. *Id.* However, the dissent found the exclusion to be anything but perfectly clear and unambiguous in this scenario and proceeded with a contextualist approach resulting in finding coverage for the family. *Id.* at 1454–62.

127. Knutsen, *supra* note 11, at 724.

unfortunate as it creates an inconsistent fabric of interpretation jurisprudence that is problematic for insurers and policyholders alike.

Therefore, any interpretive framework should, before being designed at the outset, clearly define what an insurance policy is for the purposes of the framework. That includes a frank acknowledgement of the differences between insurance policies and standard commercial contracts, including both the adhesionary nature of insurance policies as well as the public compensatory purpose of insurance. From there, knowing what the instrument is—as a category of thing to be construed—should drive what doctrinal tools and perspectives are necessary to construe a meaning that fits the purpose of the instrument and avoids conflicting results.

B. The Order of Analytic Steps

Once a legal system has sorted out what exactly an insurance policy is, it must give careful consideration to the order of any analytic steps in any proposed interpretive process. Most contractual interpretation processes in the common law world have a set of principles that courts are to apply in construction exercises. However, these principles always seem easier to apply in theory than in practice.

For example, the practical upshot of Canada's two-stage analytic structure, which is an amalgam of English textualism and American contextualism, is that it breeds significant inconsistency. It does so for two reasons: lack of a clear order of priority for principles and a confusing gatekeeper effect involving a two-stage interpretive process. Courts consistently mix up which concept in which stage can be applied at which time. Even the Supreme Court of Canada mashes together a number of interpretive concepts into varying orders and permutations from case to case.¹²⁸ It appears, in the jurisprudence, as if a number of principles about textual interpretation conjoin at the intention stage of the analysis, and then a number of consumer protectionist principles can be employed only if ambiguity is found at the ambiguity stage. Yet, even within that two-stage process, there is no priority as to what principle takes precedence over what nor is there any idea as to what, outside of the policy itself, a court can consider in construing the intention of the parties. There is supposed to be a two-stage interpretive process, where plain meaning is to be sought from the text and only if ambiguity arises are consumer protectionist principles applied. However, countless Canadian cases start and stop with a simple statement from a court that

128. See cases cited *supra* note 94.

the policy is “clear and unambiguous” on its face¹²⁹—a nod to the fact that the court will not proceed past the intention stage. Typically, a dictionary definition of a term is cited as the only evidence for this conclusion.¹³⁰ This may be because the intention stage is not focused solely on the text but on construing the meaning of the text as it is to be understood by two opposing parties. It may also be due to a lack of clear guidelines as to when and how extrinsic evidence may be used at the intention stage.¹³¹

What the Canadian experience shows is that the intention stage with its textualist bent can jarringly switch to a contextualist approach at the ambiguity stage—and the two approaches often do not jive. How can a court reliably switch from a textual analysis, devoid of context, to an analysis of ambiguity as gatekeeper to contextualist consumer protection principles like *contra proferentem* and reasonable expectations? How the court gets through that ambiguity gatekeeper is the problem. Most court decisions hang right there, stopped at the pure textual approach. Add to that the fact that Canadian litigants typically do not adduce extrinsic evidence at any stage of the interpretive process (probably because there is no guideline as to what would even be considered).

129. See *supra* note 126 and accompanying text.

130. See, e.g., *Ricketts v. Moore* (2001), 206 D.L.R. 4th 273, para. 14 (Can. Ont. C.A.).

131. For examples of these inconsistent trends in the jurisprudence over time, see the chains of cases interpreting common clauses in standard Canadian homeowners policies such as “vacancy” exclusions or the definition of “household” in coverage clauses. In the “vacancy” cases, courts over time have utilized a combination of dictionary definitions and contextual factors such as evidence of indicators that a policyholder is actually living in the dwelling (like clothing kept there, meals eaten there, number of times policyholders slept over). See, e.g., *Iacobelli v. Fed’n Ins. Co. of Can.* (1975), 7 O.R. 2d 657, para. 6 (Can. Ont. H.C.J.) (holding that house rented by outlaw motorcycle gang was “vacant” and thus there was no coverage because members did not sleep there); *Nicoli v. Liberty Mut. Ins. Co.* (1996), 31 O.R. 3d 326, para. 21 (Can. Ont. Gen. Div.) (holding that seasonal residence was not vacant, despite policyholders not sleeping there); *Wu v. Gore Mut. Ins. Co.* (2009), 100 O.R. 3d 131, para. 87 (Can. Ont. Sup. Ct. J.) (holding rental property to be vacant while landlords were in between tenants, despite daily visits to property, because of lack of indicia of policyholders living there). In the “household” cases, courts have used dictionary definitions and, in some cases, other contextual factors such as living patterns to attempt to construe who is a member of the policyholder’s “household” and thus insured under a homeowners liability policy. See, e.g., *Wawanesa Mut. Ins. Co. v. Bell*, [1957] S.C.R. 577, para. 5 (Can.) (giving “household” a large and liberal interpretation, in contextual fashion, despite lack of definition in policy itself); *Eichmanis v. Wawanesa Mut. Ins. Co.* (2007), 84 O.R. 3d 668, para. 20 (Can. Ont. C.A.) (finding teen staying with uncle and aunt was a member of their household, and thus insured); *Canadian Univs.’ Reciprocal Ins. v. Halwell Mut. Ins. Co.* (2002), 61 O.R. 3d 113, para. 25 (Can. Ont. C.A.) (holding that a university student staying in dormitory was a member of his parents’ household and thus insured under their policy even while at school); *Arsenault v. Fitzgerald* (1985), 66 N.B.R. 2d 232, para. 15 (Can. N.B. Q.B.) (holding that daughter who lived sometimes with mother, and sometimes separately with father, was a member of both parents’ households because of her pattern of living).

The value of the approach suggested in the Principles is that the presumption of an initial textualist “plain meaning” can be rebutted at that stage with extrinsic evidence of what a reasonable policyholder would think the policy term means.¹³² This overt nod to the use of extrinsic evidence as being assistive right out of the gate in the interpretive process is key. Litigants will know what to do here. The path to displacing the plain meaning is clear. Also, the interpretive perspective of that path is clear: what would a reasonable policyholder think. Finally, the kind of evidence that can be considered is also delineated. Part of the problem with the Canadian approach, discussed more below, is the Solomon-esque impossibility of attempting to discern what the parties—insurer and policyholder—intended by somehow construing the policy wording itself in a vacuum. This is probably impossible to do, and merely acts as a judicial backfiller, justifying plain meaning as coming from a “shoot from the hip” read of the policy alone. The Principles’ process for overtly dealing with the use of extrinsic evidence tells litigants what to do if the text-only plain meaning needs to be displaced. The Canadian approach lacks this mechanism and, as a result, decisions rise and fall on the judge’s reading of the policy, often without more adduced to assist the court in the analysis. Insurance decisions made without context often produce unsatisfactory results.¹³³ The Principles’ rebuttable plain meaning mechanism avoids this problem and underscores the importance of having the interpretive process clearly delineated in discernible chunks for litigants and courts alike. Otherwise, the principles of interpretation can easily go off the rails and exist in various permutations, resulting in inconsistent decisions.

C. *The Interpretive Perspective*

Another key element in the interpretive process is the interpretive perspective that the court is to apply. The meaning of a policy term is relative as to who is interpreting it. Therefore, the interpretive

132. PRINCIPLES OF THE LAW OF LIAB. INS. § 3 & cmt. a (AM. LAW INST., Tentative Draft No. 1, 2013).

133. The classic Canadian literalist paradigm is *Charania v. Travelers Indemnity Co. of Canada* (1984), 47 O.R. 2d 705 (Can. Ont. C.A.). In that case, a jewelry store was denied coverage under its theft insurance policy because the door locks were picked by a thief. *Id.* at para. 2. The definition of “burglary” in the theft insurance policy required there be “visible marks to the exterior of the premises.” *Id.* at para. 3. The Court of Appeal for Ontario held that this definition, read literally, could not include visible marks made on the inside of a lock. *Id.* at para. 10. For a scathing criticism of the results in this case, see Reuben Hasson, Commentary, *The Rape of the Lock: A Comment on Charania v. Travelers Indemnity Co. of Canada*, 10 CANADIAN BUS. L.J. 373 (1985).

perspective must be crystal clear from the outset. It should also make some realistic sense. Is it the perspective of the reasonable policyholder or the subjective perspective of the parties or some kind of imbued objective perspective of the parties?

The problems with the Canadian response to this issue reveal the wisdom in the Principles' use of the perspective of the reasonable policyholder in the policyholder's circumstances. Canadian courts construing insurance policies have one goal: to attempt to discern the intention of the parties—insurer and policyholder. This goal comes from the notion of insurance as a bargain, an import from the British legal tradition.¹³⁴ This is an ephemeral task for a number of reasons and it simply does not work in practice.

First, the Canadian insurance interpretation principles do not make it clear whether the “parties” refers to the specific subjective beliefs of the parties themselves or to some objective reasonable policyholder and reasonable insurer. Although Canadian courts seem to suggest that only objective intent is considered,¹³⁵ the fact that courts also entertain evidence of drafting intent and broker and underwriting evidence seems to skew the analysis. This makes a difference in the results in the cases because the value placed on extrinsic evidence of intent is higher if the court is using what can really only be the actual parties' real subjective intentions. If the court is instead using a more objective approach, courts have a tendency to simply imply what the parties' interests are, without regard to evidence as to context (or even without regard to evidence as to a potential objective context for the parties either). Courts then just employ a purely textualist approach to the policy wording and “guess” at the intentions of the parties.

Second, not clarifying the interpretive perspective has the tendency to negate the unique nature of the insurance policy as something different from standard commercial contracts. If a court does not recognize an insurance policy as a contract of adhesion and does not address the power imbalance imbedded in the insurance relationship, the interpretive process starts and finishes as a purely textualist approach. It then does not matter what the intentions of the parties are because such an inquiry is not necessary in interpreting the text. Perpetuating the myth of the bargain theory of insurance actually leads courts to ignore special considerations that are, in reality, very much in play between an insurer who has the drafting power and the policyholder who has no

134. See Lowry & Rawlings, *supra* note 58, at 315.

135. See, e.g., *Lloyds Syndicate 1221 v. Coventree Inc.*, 2012 CanLII 341, para. 16 (Can. Ont. C.A.).

choice but to purchase the product or not (and even then, in many instances, such as automobile insurance or for a homeowner who has a mortgage, not purchasing insurance may not be an option at all).

Third, it is highly questionable what an inquiry into the intention of both parties could actually add to the interpretive process. Instead, as noted above, the inquiry distracts courts from treating insurance as a special category of contract and drives them to a reductionist literal reasoning style because “intention” cancels itself out. It does so because, in the insurance context, the intention of the parties cannot ever really be anything different from case to case. The intention of the insurer in the dispute is to avoid coverage. The intention of the policyholder is to seek coverage. There can be no other subjective intentions.

If, by intention of the parties, Canadian courts mean “what did the insurer mean to cover” and “what did the policyholder expect to buy,” even that inquiry leads to answers that cancel each other out.¹³⁶ The insurer is entirely incentivized in the litigation context to provide as its answer an off-coverage position. The policyholder likewise is seeking coverage and is incentivized to explain that she or her reasonable stand-in meant to purchase insurance that precisely covered her loss at issue. The intention of the parties, then, cannot be discerned as anything higher than that by reading the bare text of the policy alone. Extrinsic evidence must be adduced as to drafting intent, drafting history, marketing, and industry practice. In Canada, that type of evidence almost never shows up in an insurance dispute. Therefore, the intention of the parties becomes what the judge guesses them to be, based on only a reading of the policy text. And each party can only have the exact opposite intention. So the inquiry adds nothing to interpretation.

This is borne out in Canadian cases where the interpretive exercise has triggered the second ambiguity stage in the contractual model of interpretation. Although one interpretive principle Canadian courts can employ is the reasonable expectations of the parties, because the first intention stage itself is supposed to have, as its goal, the intention of the parties, merely looking at this issue again is meaningless. In fact, not one Canadian case involving ambiguous terms has ever had its results charted by referring to the reasonable expectations of the parties.¹³⁷ It is a step that is simply given air time and is, in fact, without substance in application.

136. Marvin Baer, Commentary, *The Reasonable Expectation of Unfair Exclusions in Insurance Contracts*, 29 CANADIAN BUS. L.J. 438, 447 (1998).

137. See Knutsen, *supra* note 11, at 745.

The Principles' choice of interpretive perspective of the reasonable policyholder in the circumstances of the policyholder actually holds the potential to make a real difference in the interpretive process. It avoids the stalemate that unavoidably happens in the Canadian or English approaches. It focuses instead on the view of the reasonable policyholder, recognizing the importance of consumer protection and rejecting the unrealistic theory of the bargain as the tie that binds insurance law. By allowing for extrinsic evidence, the Principles' approach provides a mechanism by which a litigant can displace the purely textual plain meaning arrived at. The Canadian contractual approach does not do this and, as described above, is very often cemented in a purely textual approach that is then buttressed by imbuing the reasoning with guesses about parties' intentions, despite evidence to indicate any of it.

D. A Purposive Approach—Where and How?

The Canadian experience with the legislative model for automobile insurance policy interpretation suggests that there is value in incorporating a purposive approach into the insurance policy interpretation doctrine.¹³⁸ The cases decided using the legislative approach are streamlined, predictable, and produce a fulsome analysis of all contextual factors, thereby increasing public acceptance of construed meaning. The Canadian contractual model of interpretation, by contrast, does not employ a purposive inquiry beyond examining the text of the policy as a whole. The jurisprudence decided under this model spans a far more unpredictable scope, from purely textualist decisions relying solely on the text of the policy¹³⁹ to purely contextualist decisions that appear to almost entirely divorce from the text of the policy.¹⁴⁰ The Principles makes mention of purposive considerations but does so only in Comments,¹⁴¹ not in the text of the black letter law itself nor in any explicit doctrinal steps in the proposed analytic framework. There may be real opportunities to improve on the American Principles' interpretive process by somehow incorporating a purposive analysis as a mandatory consideration when interpreting insurance policies. The Principles'

138. *Id.* at 741.

139. *See supra* note 133 and accompanying text.

140. *See, e.g.,* Zurich Ins. Co. v. 686234 Ont. Ltd. (2002), 222 D.L.R. 4th 655, paras. 15–21, 38 (Can. Ont. C.A.) (using American drafting history of absolute pollution exclusion to construe exclusion very narrowly to exclude from coverage only losses resulting from industrial-scale polluters, despite no indication of this in text of policy).

141. *See, e.g.,* PRINCIPLES OF THE LAW OF LIAB. INS. § 2 cmt. b (AM. LAW INST., Tentative Draft No. 1, 2013).

sought-after middle ground approach between textualism and contextualism lends itself, almost necessarily, to an explicit purposive consideration to some degree, at some stage in the analysis.

A purposive consideration may best be considered as a grounding inquiry, to be made before any close analysis of policy text occurs. It is doubtful an inquiry as to the purpose of the particular policy and what the particular term is actually trying to do would ever supplant a more reasonable meaning than came from the plain meaning analysis utilizing the text alone. But such an inquiry would certainly go a long way to streamlining what that sensible plain meaning is. To arrive at a plain meaning without first considering the purpose of the policy term—what it is trying to do—seems counterintuitive and inefficient. Would courts not get it wrong?

An example from Canadian insurance law demonstrates this concern. In *Pietrangelo*, two successive courts denied homeowners property insurance coverage to a landlord for damage resulting from an accidental house fire.¹⁴² A youth who lived with his mother in the rental home unintentionally started a fire while attempting to make hashish in the bathroom during his first drug experimentation.¹⁴³ He had tried to learn how to do this on the Internet.¹⁴⁴ The standard Canadian homeowners policy had recently been reworded to exclude from coverage any damage resulting from anything to do with drugs—a controlled substance as delineated in a Canadian criminal statute.¹⁴⁵ The reason this exclusion had been placed into the policy was to curb the high payouts for damage to property caused by large, secret marijuana grow operations that were popping up inside rented dwellings in British Columbia.¹⁴⁶ The grow operations would cause extensive property damage because the growers were basically turning the rented apartments into marijuana gardens.¹⁴⁷ When the growers left or were arrested, the apartments were a mess and it was expensive to fix them up again. Insurers wanted to avoid paying such expensive claims and also hoped to put some onus on landlords to do what they could to monitor renters who might be putting the property at risk from this extensive kind of damage from drug growers.¹⁴⁸ Of course, in *Pietrangelo*, the accident resulted from the one-off foray into drug

142. *Pietrangelo v. Gore Mut. Life Ins. Co.* (2010), 198 A.C.W.S. 3d 1120, paras. 4-5 (Can. Ont. Sup. Ct. J.), *aff'd*, (2011), 198 A.C.W.S. 3d 812 (Can. Ont. C.A.).

143. *Id.* at paras. 1-4.

144. *Id.* at para. 2.

145. *Id.* at paras. 5, 19.

146. *Id.* at para. 92.

147. *See id.*

148. *See id.*

experimentation by a youth. The damage was not caused by grow operations.

The problem in the case was that there was a letter included as extrinsic evidence from the insurer to the policyholder advising of the reason for the change to the policy.¹⁴⁹ In addition, there was insurer testimony that, although the main target of the exclusion was marijuana grow operations, the exclusion was cast widely to catch all drug-related activity.¹⁵⁰ The Ontario Superior Court of Justice held that this extrinsic evidence did not go to the interpretation of the clause, but merely to prove its reason for existence.¹⁵¹ There was therefore no doctrinal structure through which to evaluate this evidence in light of how to interpret the clause. The courts merely resorted to dictionary definitions of the various words in the exclusion.¹⁵² The trial and appellate courts were left with trying to construe the language on its own, divorced from its purpose—which was sitting plainly in front of them. After this case, landlords everywhere would lose coverage if their tenants caused any property damage while simultaneously doing anything with drugs—hardly the result expected for broad spectrum, all risks property coverage. This is a tough (or perhaps impossible) risk for landlords to manage, and probably not a result within the reasonable expectations of a policyholder.

The lack of a structure or principle through which to make a purposive inquiry into a policy term and then direct the use of that purpose in the interpretive process was what produced the troubling result in *Pietrangelo*. The courts in that case simply did not know what to do with the evidence of the purpose of the exclusion. The intention stage only centered on the text of the policy in order to discern the intention of the parties. This evidence was evidence of intention. Because the courts found there was no ambiguity in the language of the policy—any losses whatsoever relating to drugs were excluded—they simply ignored the purpose of the policy exclusion. Had the courts had to consider purpose up front, before the textual analysis, they would have likely come to a more realistic decision. The Canadian legislative model of interpretation would have avoided this result had it been applied instead of the contractual model.

149. *Id.* at para. 19.

150. *Id.* at paras. 92–93.

151. *See id.* at para. 96.

152. *Id.* at para. 85.

E. Consequences of Coverage and Denial

No jurisdiction currently has a palpable mechanism for processing information about how the insurance policy at issue in a case, or the term at issue, is to function in the larger insurance framework. There is, at present, no process as to how a court could consider how a coverage result will affect the interpretation of other overlapping or complementary policies. There is no process to consider whether or not another policy or party, such as a broker, will be left to inefficiently take up the loss. Nor is there a process to consider whether the public welfare system will be inefficiently and inappropriately triggered as a result of an incorrect coverage denial. The Principles makes overtures about the importance of insurance in society, its compensatory purpose, and its key to financial responsibility.¹⁵³ Few Canadian insurance cases that invoke the contractual model of interpretation when a policy term is ambiguous consider such broad, systemic insurance issues. Britain does not consider any such issues in its textualist approach. Yet, if a system of interpretation is to bridge the gap between textualism and contextualism in a realistic way, and is doing so precisely because of perceived discomfort with results proceeding under one or the other approach, then surely these meta-policy questions must be taken up somewhere under the aegis of contextualism. To do otherwise is to still be blinded by a textual approach in some fashion.

To that end, some consideration of the ripple effects of an interpretive insurance decision should properly occur at some stage of the analysis, for these decisions do not occur in isolation. Policy terms that deny coverage in one context may do so because of an expectation of coverage in another. Courts need to be mindful of the effect of such ripples. There is no more common example of this than market segmentation¹⁵⁴ cases that pit a non-auto and auto liability policy in a contest of coverage. An automobile liability policy purports to cover losses arising from the use or operation of an automobile. A standard homeowners or commercial general liability policy covers all risks save and except risks arising out of the use or operation of an automobile. If one loss has the potential to trigger both coverages but only one policy is at issue in the case at one time, the interpretation of coverage under one policy will affect the mirror imaged exclusion in the other. Dangerous and unexpected coverage gaps can be created for unsuspecting reasonable policyholders if

153. PRINCIPLES OF THE LAW OF LIAB. INS. § 2 cmt. b (AM. LAW INST., Tentative Draft No. 1, 2013).

154. See TOM BAKER, INSURANCE LAW AND POLICY: CASES, MATERIALS, AND PROBLEMS 466–67 (2d ed. 2008).

the effect of the interpretive decision on both policies is not considered.¹⁵⁵ The cost of any gaps in coverage can bleed out in inefficient ways, to the state welfare system and beyond.

IV. A HOLISTIC INTERPRETIVE SOLUTION

The Canadian legislative model provides a useful baseline for any common law country tinkering with insurance policy interpretation principles. It avoids the problems noted in the above part, and provides easy-to-reach answers for many of the above noted issues that other approaches simply are not equipped to answer. It also aims at balancing a textualist approach that attempts to be true to the text with a contextualist purposive inquiry. However, it is a model built for legislation, not insurance, and could benefit from greater clarity in breaking down the principles so that courts and litigators can consistently apply what is required in an insurance context. Ideally, an interpretive model for insurance policy interpretation would be more insurance-specific and take into account the special nature of insurance policies in society.

Taking the best of the interpretive principles from the Canadian legislative model and the Principles' proposed framework, one version of a holistic interpretive solution to insurance policy interpretation could appear as follows:

A. *Step One: Discern the Public Purpose*

The first step would be to discern the public purpose of the coverage-granting instrument as a whole. What is the policy trying to do? What is its purported function in the broader accident compensation scheme? How does the policy fit with other insurance products in the market? Such an inquiry needs to be imbued by the public purpose of insurance. So, courts must seek to answer what the purpose of the policy is for the reasonable policyholder. This inquiry grounds the rest of the steps in the analysis. Any available extrinsic evidence should be considered in fleshing out this inquiry. While this inquiry does not direct the actual interpretive exercise (and it cannot because it is sought without reference to much of the text yet), it does inform the exercise to come. For example, it would be helpful for courts to be reminded that the standard

¹⁵⁵ For descriptions of potential insurance gap problems created by market segmentation clauses, see Knutsen, *supra* note 123, at 963–64, and Knutsen, *supra* note 11, at 733–35.

homeowners liability insurance policy is designed to provide coverage for all risks of loss resulting from the policyholder's behavior, save and except those specific instances not covered or excluded. It would also be helpful for courts to be reminded that such insurance is second only to automobile liability insurance as the second most frequently triggered compensatory backbone of the tort system.

B. Step Two: Discern Intent Behind the Term at Issue

Once the public purpose of the policy is discerned, that purpose then informs an inquiry into what the intent is behind the term or clause at issue. Why is that clause there? What is it supposed to be doing? What were the drafters trying to do or say by employing that language? Of course, here the text of the policy is key. However, the ethos behind this step is that the wording of the policy is not *sui generis*; evidence of intent is often readily available and should be considered. Extrinsic evidence of drafting intent, underwriting history, revisions, marketing, regulatory opinions and approvals, and regulatory filings would be key here. This would ensure that the historical purpose of the term at issue is not divorced from its *de facto* purpose in a specific case. The key would be to try and isolate the specific goal that the particular clause is supposed to be accomplishing, in light of the public purpose of the policy and what a reasonable policyholder would think this clause is doing. So the grounding interpretive perspective is that of the public purpose of the policy plus what a reasonable policyholder would think the clause at issue means, in light of the discerned intent of the clause. Such an approach would probably avoid most ambiguity concerns because the textual reading would be informed by purpose and context without resort to having to make the ambiguity determination. This step frontloads the inquiry instead. Avoiding an ambiguity problem is a useful goal, because that is typically the most unpredictable part of the analysis.

C. Step Three: Consequences of Coverage

The public consequences of the interpretive result, either the granting or withholding of coverage, should next be assessed as a systemic check on the validity of the result and its costs. Here, ripple effects across the insurance system are to be understood and accounted for, if necessary. A court would inquire as to where the loss actually lays depending on the coverage result, whether or not that is an efficient place to lay it, and who is rightly saddled with the risk of loss. Basically, this step inquires into who the coverage affects and how, and what gaps in compensation are created, if any, in the broader compensatory system of

which insurance is a key component. If the loss is typically to be offloaded onto brokers' and agents' liability insurance for negligent selling of coverage, such may be a factor in the court's interpretive decision because, otherwise, very perverse incentives and inefficient gaps are created in the market for insurance. If the loss is instead typically covered by other policies on the market or by some overlapping coverage, such would also be a factor for the court to validate the efficacy of its interpretive result. Perhaps, in a case of coverage denial, the costs of an accident are instead borne by either employer accommodations at work or by the public welfare system. A court should inquire whether, in the particular case, such is the just and efficient result of the coverage denial, based on the insurance arrangement at issue. Perhaps so. But perhaps not. At the very least, courts need to be thinking of the consequences of coverage and what that does in the insurance market and social economy. Thinking about these issues forces courts to take stock of the potential rippling effects of coverage decisions on the market. Because the jurisprudence operates via *stare decisis*, insurance decisions have the capacity to either open floodgates for coverage or redirect coverage to often unintended and inefficient places, if courts are not careful in taking a holistic approach to coverage by examining a decision's effect on the broader compensatory system.

D. Step Four: A Simpler Textual Approach Using Consumer Protectionist Tools

If, by step four, the just meaning of a policy term is not self-evident already, courts should move to a more textualist analysis, supplemented by traditional consumer protectionist interpretive tools if necessary. This textual approach is far safer to do on the back end than on the front end where it traditionally is placed. The reason is simple: nonsensical literalist results are nearly always avoided because courts have already been grounded by being informed about the broader public purpose of the policy, the intent of the term at issue, and the effect of coverage or denial on the broader insurance system. By this point in the analysis, risks of moving to a textualist approach are suppressed because courts have had to go through the broader exercise of situating the analysis in the wider insurance context.

It is quite possible that step four may not be necessary in most interpretation cases. If it is, however, courts can certainly use the text of the policy to try and discern the meaning of a term as it would mean to a reasonable policyholder. In keeping with balancing textualism with contextualism concerns about the adhesionary nature of insurance policies, coverage clauses should be construed broadly and exclusion

clauses narrowly at this stage. Any ambiguities that still remain can certainly be resolved *contra proferentem* but, by this point in the analysis, that doctrine is not being resorted to as simply a tie-breaking device (a criticism it historically receives as a knee-jerk reaction by many courts in all jurisdictions).¹⁵⁶ Ambiguity, then, would have only a mild gatekeeper role in the analytic framework. The key by stage four is to focus on the result of coverage or denial of coverage, not on the purely textual reading of the policy. Thus, meaning of a policy term is always context-driven.¹⁵⁷

The model framework sketched out above would allow courts in a common law jurisdiction to achieve a middle ground balance between textualism and contextualism by reversing the typical order of those principles commonly grouped in the textual camp with those commonly grouped in the contextual camp. Tackling a few contextual problems first, without upsetting the textual analysis to come, situates the analysis and may actually produce more predictable and just interpretive results. The Canadian experience with both contractual and legislative models of interpretation has demonstrated that the legislative model produces superior interpretive results in insurance disputes. This may, at first blush, seem counterintuitive because the legislative approach can appear to be a largely contextualist approach, with a heavy focus on purpose. However, therein lies the secret: the up-front purposive approach, combined with the larger inquiry as to intended effect on the compensatory system actually streamlines the inquiry and makes the doctrinal tools more predictable to apply when courts consider the actual text of the insurance policy itself. This approach, like the approach proposed above, largely avoids future litigation over the same policy terms. That helps to stabilize the insurance law jurisprudence and thus saves time and money for insurers and policyholders alike.

156. PRINCIPLES OF THE LAW OF LIAB. INS. § 4 reporters' note j (AM. LAW INST., Tentative Draft No. 1, 2013).

157. Knutsen, *supra* note 11, at 746.