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### Timeless and Ahead of Its Time: Lach's v. Fidelity & Casualty of New York

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# LACHS V. FIDELITY & CASUALTY CO. OF NEW YORK: TIMELESS AND AHEAD OF ITS TIME

Jeffrey W. Stempel\*

The publication of Judge Keeton's important article "inventing" the reasonable expectations doctrine in 1971 is notable for infusing a good deal of intellectual energy into the study of insurance law, particularly judicial decisions about insurance coverage.<sup>1</sup> Keeton's article, which deduced from cases the principle that courts tended to interpret policies to vindicate the objectively reasonable expectations of the insured,<sup>2</sup> has rightly been viewed as a milestone.<sup>3</sup> It clarified an area of law long seen as inconsistent or result-oriented. It spurred additional important scholarship in the area and elevated insurance caselaw from something of a backwater to at least a respectable academic discipline, even if not quite an exciting one.<sup>4</sup>

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\* Professor of Law, William S. Boyd School of Law, University of Nevada, Las Vegas. Thanks to the Symposium participants and the *Law Journal* staff for providing a forum for the underappreciated charms of favorite insurance cases. Tabitha Fiddymment provided valuable research assistance. Special thanks to Gene Comey, who forced me to see *Lachs* as something more than just a case about vending machine insurance. Preparation of the article was supported by a grant from the James E. Rogers Research Fund.

<sup>1</sup> See Robert E. Keeton, *Insurance Law Rights at Variance with Policy Provisions I*, 83 HARV. L. REV. 961 (1970) [hereinafter *Rights at Variance*].

<sup>2</sup> *Id.* at 967.

<sup>3</sup> This particular Keeton article has been cited hundreds of times and has been the subject of considerable academic commentary. See, e.g., Jeffrey W. Stempel, *Unmet Expectations: Undue Restriction of the Reasonable Expectations Approach and the Misleading Mythology of Judicial Role*, 5 CONN. INS. L.J. 181 (1998). See generally Peter N. Swisher, Symposium Introduction, *The Insurance Law Doctrine of Reasonable Expectations after Three Decades*, 5 CONN. INS. L.J. 1 (1998).

<sup>4</sup> "Backwater" is perhaps harsh. Prior to the *Rights at Variance* article, there were, of course, well-regarded texts about insurance law and a number of significant articles, many of them also by Keeton. See, e.g., EDWIN W. PATTERSON, *ESSENTIALS OF INSURANCE LAW: AN OUTLINE OF LEGAL DOCTRINES IN THEIR RELATIONS TO INSURANCE PRACTICES* (2d ed. 1957) (republished in 1985); WILLIAM REYNOLDS VANCE, *HANDBOOK OF THE LAW OF INSURANCE* (1904); Robert E. Keeton, *Liability Insurance and Responsibility for Settlement*, 67 HARV. L. REV. 1136 (1954); Robert E. Keeton, *Preferential Settlement of Liability-Insurance Claims*, 70 HARV. L. REV. 27 (1956); William R. Vance, *The History of the Development of the Warranty in Insurance Law*, 20 YALE L.J. 523 (1911).

However, insurance law scholarship prior to Keeton's *Rights at Variance* article was generally less plentiful, more formalistic and wooden and less intellectually reflective than that found in many areas of law. Since the *Rights at Variance* article, insurance law has seen an explosion of casebooks, treatises, and scholarly commentary, much of it by the participants in this Symposium. See JEFFREY W. STEMPEL, *LAW OF INSURANCE CONTRACT DISPUTES* (2d ed. 1999 & Supp. 2001) (bibliography listing insurance law books and articles reflects greater activity during 1980s and 1990s than during the first two-thirds of the century). Although some of this results simply from the growth of the legal profession and the

But as important as Keeton's article was, it to some extent perhaps even understated the extent to which courts had long utilized the reasonable expectations concept without mentioning it by that name. It also tended to underplay the degree to which courts construed insurance contracts in light of their intended purpose, irrespective of whose expectations were involved.<sup>5</sup> Most important for purposes of this Symposium topic, Keeton's seminal article cited *Lachs v. Fidelity & Casualty Co. of New York*<sup>6</sup> only in passing. The short treatment seems unusual in that *Lachs* is a most interesting case from the then-largest state in the nation, a case that utilized not only the reasonable expectations principle, but also an array of contract concepts designed to illuminate the apt meaning of the insurance policy.

Furthermore, Keeton arguably mischaracterizes *Lachs* as a case that is straining to construe the insurance policy to provide coverage. He suggested that *Lachs* had "tortured" the policy language and in effect applied a sub silentio strong form of the reasonable expectations doctrine that protects policyholder expectations even in the face of clear contrary policy language.<sup>7</sup> To be sure, *Lachs* utilized the reasonable expectations approach and did so nearly twenty years before Keeton coined the term and introduced the reasonable expectations concept to the academic world. But *Lachs* used other contract construction tools to appropriately find coverage and, in my view, hardly "tortured" the policy language. Rather, *Lachs* took a comprehensive, context-sensitive, eclectic approach to policy construction, an approach in which policyholder expectations were a part of the analysis rather than a trump card for the policyholder.<sup>8</sup>

Unfortunately, *Lachs* has long been either overlooked or treated as something of a novelty case because of its subject matter – "vending machine" or "self-service" flight insurance. On closer examination, *Lachs* provides not only an interesting (if tragic) fact pattern but also illustrates with understated grace the appropriate approach to resolving insurance coverage disputes with consideration to questions of text, party intent, purpose, expectations, and public policy.

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legal academy, this trend also reflects the increasing focus upon insurance law by scholarly commentators, including practitioners.

<sup>5</sup> See, e.g., *Gaunt v. John Hancock Mut. Life Ins. Co.*, 160 F.2d 599 (2d Cir. 1947), *cert denied*, 331 U.S. 849 (1947) (court, in Learned Hand opinion, finds coverage under conditional receipt issued pursuant to life insurance sale); *Bird v. St. Paul Fire & Marine Ins.*, 120 N.E. 86 (N.Y. 1918). *Gaunt* is typically characterized as a case that simply construed ambiguous policy language against the insurer. On closer examination, *Gaunt* reflects use of the reasonable expectations concept as a major pillar of the decision. See also Stempel, *supra* note 3, at 189-94 (discussing cases from which Keeton's *Rights at Variance* article drew its conclusions); Robert H. Jerry II, *Insurance, Contract, and the Doctrine of Reasonable Expectations*, 5 CONN. INS. L.J. 21, 31-32 (1988) (discussing *Bird* and other older, pre-Keeton *Rights at Variance* article cases utilizing reasonable expectations concept).

<sup>6</sup> 118 N.E.2d 555 (N.Y. 1954), *reh'g denied*, 120 N.E.2d 216 (N.Y. 1954).

<sup>7</sup> See Keeton, *supra* note 1, at 970, 976.

<sup>8</sup> The *Lachs* version of reasonable expectations does not fit neatly into the traditional classification, but is, if anything, a "weak" version of the approach, one that must first find some significant uncertainty in the wording of the insurance policy before the court will consider expectations as affecting the interpretation of the policy. See *infra* text accompanying notes 64-74 (discussing reasonable expectations doctrine in greater detail).

From a distance of nearly fifty years, the *Lachs* case continues to provide an example of the appropriate judicial approach to insurance coverage disputes – one that looks to the whole package, including policy text, party intentions, transaction purpose, party expectations, and public policy. At the same time, *Lachs* also illustrates how fragile the position of such comprehensive and enlightened adjudication can be. Judge Conway's majority opinion commanded only a 4-3 vote of the Court. Ironically, it was the highly regarded Judge Fuld who with two others mistakenly but vigorously dissented. In a twenty-first century faced with frequently difficult coverage disputes over pollution, product liability, construction problems, e-commerce, computers, and the respective rights and obligations of insurers and policyholders, *Lachs* remains a case worth keeping in mind.

### I. THE *LACHS* DECISION

In *Lachs v. Fidelity & Casualty Co. of New York*,<sup>9</sup> the Court of Appeals, New York's highest court, was required to determine whether benefits would be paid on a "flight insurance" policy purchased by machine at the airport by a passenger moments before she boarded a plane destined for a fatal crash. The policy provided that it covered only flights on "scheduled" airlines. The policyholder died flying what the insurer considered a "non-scheduled" airline. The case is relatively well-known as one of the handful of leading cases regarding flight or vending machine insurance and is commonly cited in casebooks and treatises.<sup>10</sup>

On December 16, 1951, New York resident Sadie Bernstein went to Newark Airport to take a flight to Miami, Florida. She happened upon a vending machine that offered "AIRLINE TRIP INSURANCE" underwritten by Fidelity & Casualty Company of New York. She bought a \$25,000 policy for \$25 in premium, paid through deposit into the machine.<sup>11</sup> She named her daughter (Marion Lachs, subsequently the plaintiff in the case) as the beneficiary. Bernstein later boarded the plane, which appears to have crashed almost immediately upon takeoff, killing the policyholder (and apparently all fifty-six

<sup>9</sup> 118 N.E.2d 555 (N.Y. 1954).

<sup>10</sup> See, e.g., JEFFREY W. STEMPEL, INTERPRETATION OF INSURANCE CONTRACTS § 29.3 (1994) (also suggesting that the *Lachs* majority tacitly applied the reasonable expectations approach to resolve the case); ROBERT H. JERRY II, UNDERSTANDING INSURANCE LAW § 33, at 148, n.41 (1987) and ROBERT H. JERRY II, UNDERSTANDING INSURANCE LAW § 32, at 192, n.58 (2d ed. 1996). Professor Jerry, however, classifies the *Lachs* decision as holding that the unscheduled airlines exclusion was "otherwise clear" but became ambiguous because the flight insurance vending machine was near the ticket counter of an "nonscheduled" airline (like me, Professor Jerry also failed to catch a typographical error in the first edition, citing the case as "*Lacks*" rather than the correct "*Lachs*," a glitch carried over to the second edition of Jerry's outstanding treatise).

The differing views of two insurance law professors highlights the fuzzy nature of this part of insurance law. Regarding the actual views of the *Lachs* majority, Professor Jerry is in my view incorrect. The *Lachs* majority saw the disputed term as facially ambiguous while the dissenters thought it facially clear and enforceable. See *infra* notes 11-24.

<sup>11</sup> See *Lachs*, 118 N.E.2d at 556. The capitalization of "AIRLINE TRIP INSURANCE" is the court's. According to the court, the words were "in letters ten times larger than any other words on the machine and in prominent lighting." See *id.* at 557.

passengers and crew on board).<sup>12</sup> Later, her daughter sought to collect the death benefit under the policy. The insurer denied coverage, taking the position that the policy only applied to “scheduled” flights – those operated at regular times by major airlines. According to the insurer, the flight Lachs took was “nonscheduled” – operated irregularly by a non-major air service.

Unfortunately, the *Lachs* opinion, despite its many legal strengths, is thin on factual description. Even the dissent, which argues that laypersons know the difference between scheduled and nonscheduled flights, provides no detail as to the plane flight and the carrier’s operation. The reader is not told what type of airplane was used in the fatal flight. Nor is the operator of the flight described. The Miami Airlines flight was what we would now call a charter. It was large enough that when it crashed, fifty-six people (including, of course, Bernstein) perished.<sup>13</sup> The plane was not a small, “puddle-jumper” or crop-duster.<sup>14</sup> In other words, Bernstein boarded a charter flight in a reasonably large plane carrying other New Yorkers to Miami to escape the Northeastern winter or perhaps to visit relatives during the holidays.<sup>15</sup> In this ambiguous situation, at a

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<sup>12</sup> See *id.* at 556-57. “She later entered the plane after a delay, the reason for which is not disclosed in the record, and in less than an hour was dead as the result of a crash.” The court is both melodramatic and cryptic. News accounts of the tragedy are scarce but it appears that all on board were killed in a takeoff-related problem or difficulties experienced early in the flight.

<sup>13</sup> See *Crash, Competition Hit Nonskeds*, AVIATION WEEK, Dec. 24, 1951, at 54. Note that this article headline refers to charter flights such as the Miami Airlines plane, as “nonskeds” or nonscheduled airlines. However, the article was in *Aviation Week*, which suggests to me that the term “nonsked” had a technical meaning even if a layperson like Bernstein had been realistically able to read and analyze the flight insurance policy in question.

<sup>14</sup> The plane in question was a “twin-engine Curtiss Commando.” It had heater and brake maintenance problems prior to the crash and was thought to have crashed due to breakout of a fire after takeoff. See *id.* at 54.

At the time of the crash, there had been an ongoing debate about the relative safety of scheduled and nonscheduled airlines. In 1951, there were 5.2 passenger fatalities per million passenger miles for “nonskeds,” which may have included small private planes as well as charters, compared to 1.5 fatalities per million passenger miles for scheduled airlines. In 1950, the relative rates were 3.7 and 1.3, the difference largely owing to the Miami Airlines crash and its many victims. *Id.* at 54. Although this difference supports the underwriting rationale for insurers distinguishing the types of flights covered, it hardly excuses lack of clarity in an insurance policy. Also, the risk differential is hardly dramatic. Even in a year with a tragedy such as the Miami Airlines crash, the death rate from flying nonscheduled airlines was far below the fatality rate for driving by automobile. And, it should be remembered, the policy sold to Bernstein was not like ordinary automobile insurance applied to airplanes. It was like auto insurance that provided coverage only for one round trip from New York to Florida.

It appears that, in 1951, scheduled airlines primarily served business and official travel (e.g., government, military) and that there was comparatively little recreational air travel among the public at large. See *id.* at 54 (Civil Aeronautics Board had “urged the regular airlines to go into the air travel mass market.”).

All this may suggest that perhaps laypersons such as Bernstein appreciated the distinction between charters and noncharters, at least if the issue was consciously raised, a point the dissent pressed in arguing that the terms scheduled and nonscheduled were clear. To me, however, the most this shows is simply some ambiguity as to what the terms might mean if read in an insurance policy.

<sup>15</sup> Miami Airlines, the airline flown by Bernstein, may have been a super-charter carrier or the functional equivalent of a major airline for that purpose. “Plaintiff claims that Miami

time when air travel was still considered something of an adventure rather than a commonplace event, Bernstein apparently decided that buying a bit of life insurance covering the trip might be a good idea.

The vending machine was “situated in front of the Consolidated Air Service counter” where the airline ticket was purchased.<sup>16</sup> In return for inserting the premium in the slot of the machine, an application was dispensed. The vending machine was also decorated with “a well-illuminated display of airplanes flying round and round, and in large characters appeared the words and numerals ‘25 [dollars] For Each \$5,000 Maximum \$25,000.’”<sup>17</sup> There was also a large-lettered placard that stated (“in letters *many times* the size of the other words” on the machine):<sup>18</sup>

“DOMESTIC”

AIRLINE TRIP INSURANCE

25 FOR EACH \$5,000 MAXIMUM \$25,000<sup>19</sup>

After this advertisement prominent on the face of the machine, the placard set forth the more problematic language that became the focus of the dispute:

Covers first one-way flight shown on application (also return flight if round trip airline ticket purchased) completed in 12 months within or between United States, Alaska, Hawaii or Canada or between any point therein and any point in Mexico, Bermuda or West Indies on any scheduled airline. Policy void outside limits. For “international” coverage see airline agent.”<sup>20</sup>

. . .

1: This insurance shall apply only to such injuries sustained following the purchase by or for the Insured of a transportation ticket from . . . a Scheduled Airline . . . during any portion of the first one way or round airline trip covered by such transportation ticket in consequence of: (a) boarding, riding as a passenger in, alighting from or coming in contact with any aircraft operated on a regular or special or chartered flight by a Civilian Scheduled Airline maintaining regular, published schedules and licensed for interstate, intrastate or international transportation of passengers by the Governmental Authority having jurisdiction over Civil Aviation . . .

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Airline, Inc. maintained regular, published schedules of fares and schedules showing passenger mile rates and that it held itself out as maintaining regular schedules of flights and ticket were sold for stated hours of departure and that it was licensed by the Civil Aeronautics Board to carry passengers and freight with large aircraft in interstate, overseas, and foreign air transportation. We think there is a question of fact presented [as to the status of Miami as a “scheduled” airline, thereby triggering the principle that ambiguous language should be construed against the insurer which drafted the contract.] See *Lachs*, 118 N.E.2d at 559. In addition to Bernstein and the fifty-five other decedents, the plane carried former Secretary of War and United States Court of Appeals Judge Robert Patterson. See *Disasters: Last Flight; Fighting Judge*, TIME, Feb. 4, 1952, at 12.

<sup>16</sup> See *Lachs*, 118 N.E.2d at 557. According to the court, the plaintiff “claims” this was the machine’s location. The location, however, does not appear to have been seriously disputed by the court or the insurer. A full reading of the case suggests that the vending machine was indeed close to the point where the passenger/policyholder finalized her ticket arrangements.

<sup>17</sup> *Id.*

<sup>18</sup> *Id.* (emphasis the court’s).

<sup>19</sup> *Id.*

<sup>20</sup> *Id.*

The application form asked the “applicant” for information about the airline trip but apparently did not ask for the name of the airline or the nature of the flight.<sup>21</sup> After the application is inserted into the machine, the purchaser received the policy, which the court described as follows:

The policy is approximately eleven inches in height and is printed on both sides – thus there are twenty-two inches of printed matter. However, the purchaser does find across the front of the policy in type many times larger than all the other printing on the page and obliterating some words of the policy: “THIS POLICY IS LIMITED TO AIRCRAFT ACCIDENTS READ IT CAREFULLY.” There is also an envelope in the machine to mail to the beneficiary for the insured is not expected to read the policy on the plane. The envelope has printed on it: “AIRLINE TRIP INSURANCE.”

Plaintiff says that some but not all machines have a specimen policy attached and that it has not been established that the machine from which decedent purchased her pol-

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<sup>21</sup> See *id.* Calling the purchaser of this sort of insurance an “applicant” is technically correct perhaps but a bit of a misnomer. The insurer is not in a position to “reject” the applicant or even to do any underwriting. Essentially, the vending machine becomes a cash-and-carry operation (absent fraud, which gives the insurer another defense). Bernstein paid a premium and received a policy covering travel with an “application” that does not even explore the scheduled-nonscheduled distinction deemed so important by the insurer after it knew that the plane had crashed and Bernstein had died.

The insurer is willing to essentially issue no questions asked coverage because there are fewer problems of potential adverse selection or moral hazard. The passenger-policyholder is unlikely to seek higher risk flights as a means of adding to the family assets. Neither is the passenger with insurance more likely to exercise less care because of the presence of insurance – by definition the flight is under the control of the pilot and others (including the airport, the Civil Aeronautics Board, the Federal Aviation Administration, etc.).

Consequently, the risk distribution of such insurance is quite good for the insurer, even if it is forced to cover small, unscheduled flights. Unless there is a group of suicidal policyholders hellbent on taking a dangerous flight or making the flight more dangerous (which is farfetched for flights of this size, even in the wake of the September 11<sup>th</sup> terrorist attacks), the insurer is sure to enjoy the benefit of large numbers and the law of averages in spreading the risk.

Furthermore, the premium charged for the coverage that lasts only a few hours is very high. For example, Bernstein paid \$1 per \$1,000 of life insurance “protection” that was limited to at most a few hours of flying to Miami and back. A typical life insurance policy costs between \$1 and \$4 per thousand for *an entire year* of coverage for untimely death resulting from any non-excluded cause. Also, the flight insurance policy has a relatively low maximum face value. It is hard to have overinsurance absent the taking out of several policies, which the insurer can prohibit. As long as the insurer sells enough of these policies, the line is sure to be profitable.

That said, I need to put in a word on the side of the insurer and what the insurer was probably trying to do in setting forth the “scheduled-nonscheduled” flight distinction. In a truly private plane setting, the issues of risk distribution, adverse selection, and moral hazard can become less advantageous for the insurer. A CEO trying to make a big meeting or a lawyer running late for a court date may hound a private pilot into flying when conditions are too rough (although this, too, is limited by the need to get flight clearance from the airport). A sociable group of passengers and pilots may be more tempted to depart from safe flight practices: consider the notorious crashes of private planes carrying popular music stars where there have at least been concerns that drug use on the plane extended to pilots.

That, of course, is why it is important to me to know whether Bernstein flew her own private plane or was simply on a charter or minor airline flight to Miami. If it was the latter, which it appears to be when one reads the *Lachs* opinion’s connotative meaning, Bernstein’s flight presented no realistically problematic risk for the insurer.

icy had a specimen attached. Be that as it may, the defendant has presented as an exhibit a specimen policy and the words quoted (*supra*): "THIS POLICY IS LIMITED TO AIRCRAFT ACCIDENTS READ IT CAREFULLY" obliterate the words: "Civilian Scheduled Airline" in the coverage clause so that they cannot be read."<sup>22</sup>

The court decided in favor of the policyholder primarily on the ground that the terms "scheduled" and "non-scheduled" were unclear to the average lay passenger purchasing the policy and that the *contra proferentem* rule of construction (ambiguities in a contract are construed against the drafter, a rule of thumb so commonly invoked for insurance cases that many courts and commentators, including me, no longer italicize despite the Latin terminology) compelled a finding for the policyholder. Attempting to avoid the *contra proferentem* doctrine, the insurer introduced what its judicial supporters described as

a veritable mountain of material – contained in statute and regulations, in opinions and reports, in newspapers and magazines – to demonstrate that the term "scheduled airline" has gained a wide and general currency, and that it is a term of clear and precise meaning, which has become part and parcel of the ordinary person's everyday vocabulary. Defined by any standard and from any point of view, and compressed into a sentence, it simply and solely denotes a common carrier permitted to operate, or to hold out to the public that it operates, one or more airplanes between designated points regularly, or with a reasonable degree of regularity, in accordance with a previously announced schedule.<sup>23</sup>

The majority viewed this mountain of evidence as topography of ambiguity rather than certainty:

The attempt of defendant to establish that the term "Civilian Scheduled Airline" has a clear and definite meaning has caused it to bring forward and present an enormous amount of proof extrinsic to the policy including a statute, regulations, newspaper and magazine articles, etc. By this mountain of work it seems to us that defendant has established that "Civilian Scheduled Airline" is not at all free from ambiguity and vagueness – if it were not so the contract of insurance itself would disclose within its four corners the intent of the parties entering into it.<sup>24</sup>

Although New York is not generally regarded as a state that follows the reasonable expectations doctrine, *Lachs* can be seen as a reasonable expectations case as well as an ambiguity case. For example, the court stressed that the insurer had placed the flight insurance vending machine near the ticket counter for the "non-scheduled" airline. Regardless of the purported prohibition on coverage for these flights, the court suggested that the policyholder had reasonably assumed she was covered under the policy when she flew from an airline so close to the insurer's vending machine. In reaching this decision, the court applied the sort of holistic approach to contract construction that is a significant underpinning of both the reasonable expectations doctrine and modern contract interpretation.

We have never departed from our statement in *Kenyon v. Knight Templar & Masonic Mut. Aid Assn.*: "It may be preliminarily observed that, as a general rule, the construction of a written instrument is a question of law for the court to determine, but

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<sup>22</sup> See *id.*

<sup>23</sup> *Id.* at 561 (Fuld, J., dissenting).

<sup>24</sup> *Id.* at 560.



when the language employed is not free from ambiguity, or when it is equivocal and its interpretation depends upon the sense in which the words were used, in view of the subject to which they relate, the relation of the parties and the surrounding circumstances properly applicable to it, the intent of the parties becomes a matter of inquiry, and the interpretation of the language used by them is a mixed question of law and fact." Was the decedent entitled to believe that she had purchased "AIRLINE TRIP INSURANCE" through a policy "LIMITED TO AIRCRAFT ACCIDENTS"? It seems to us that a jury could find that when decedent purchased her policy on an application for "AIRLINE TRIP INSURANCE" from a machine having in prominent lighting those same three words, before obtaining her ticket from a counter in front of which the machine stood, she was covered on her flight, since the minds of the decedent and the company had met on that basis. In other words, since defendant put one of its automatic vending machines in front of the ticket counter of the Consolidated Air Service, which, according to an affidavit submitted by defendant "was utilized by all non-scheduled airlines operating out of the Newark Airport, as a processing point for their passengers, and before any passenger on a non-scheduled airline could receive his ticket he was required to present his 'exchange order' at said counter" we think a jury might find that the defendant was inviting those passengers to insure themselves by its "AIRLINE TRIP INSURANCE."<sup>25</sup>

In particular, the court noted that the insurer through the scheduled-non-scheduled airline defense to coverage was using an argument that "draws the line of construction very finely" and noted that according to the policyholder's side of the story, her flight qualified as a scheduled airline by any reasonable definition of the term.<sup>26</sup> Under these circumstances, the court found that a number of factors pointed to a construction in favor of coverage.

The precise holding of the court was only that the insurer could not prevail on summary judgment and that the beneficiary could proceed to jury trial. The practical effect of the holding was to rule against the insurer as to contract meaning by invoking a comprehensive approach to contract construction that involved policy language, party intent, purpose of the insuring arrangement, estoppel, reasonable expectations, and public policy.<sup>27</sup>

The dissent staked out a much more textualist position, invoking the now familiar nye-on-to-hackneyed reference to Alice in Wonderland, and Humpty Dumpty's famous boast that when he uses a word, it "means just what I choose it to mean."<sup>28</sup> The dissent intended this to be a slap at the majority, which in the dissent's view had adopted an idiosyncratic view of the terms "scheduled" and "non-scheduled." But one might as easily read the invocation of Lewis Carroll as a jab at the insurance company, which could have defined the term in the policy but did not and which could have alerted prospective customers to this limitation of coverage but did not.

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<sup>25</sup> *Id.* at 558-59 (citations omitted; italics in original).

<sup>26</sup> *Id.* at 559.

<sup>27</sup> *Id.* at 558-60. The *Lachs* majority opinion thus provided the intellectual grounding for the perhaps more well-known *Steven v. Fidelity & Casualty Co.*, 377 P.2d 284 (Cal. 1962), which found coverage under similar circumstances and held that coverage-limiting language such as the restriction of coverage to civilian scheduled flights must be "conspicuous, plain, and clear" to be enforceable. *Steven* also can be read as more expressly embracing the reasonable expectations concept.

<sup>28</sup> *Lachs*, 118 N.E.2d at 560 (Fuld, J. dissenting).

The dissent makes at least two fundamental errors. First, it adopts the belief that those who do not read the term “civilian scheduled airline” in the same manner as does the insurer (after the fact, when it knows it has a claim) are simply not reasonable people reading English. In effect, the dissent is arguing for a reasonable expectations doctrine protecting insurers.<sup>29</sup>

Alternatively, the dissent silently argues a position that turns contract law principles on their head. It seeks a reverse *contra proferentem* where unclear language is construed in favor of the contract drafter and it seeks to accord insurance policy language a highly technical meaning rather than the ordinary meaning applicable to the laypersons who purchase such policies.<sup>30</sup> It seems to attach no consequence at all to the insurer’s failure to define a term it later argued was key to the coverage.<sup>31</sup>

The second, and perhaps more grievous error of the dissent is to focus exclusively, even myopically on text. Unlike the majority, the dissent has no appreciation of the nontextual factors surrounding the sale of the life insurance product: the policy was advertised through a vending machine without a learned agent intermediary; the vending machine was placed in an area where nonscheduled airlines regularly flew; the premium charged was very high for limited coverage; the need to protect the public from potentially deceptive practices; and, of course, the policyholder’s perspective, understanding, and expectations. All these things are ignored by the dissent in favor of a preferred but by no means obvious reading of the text.<sup>32</sup>

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<sup>29</sup> See Kenneth S. Abraham, *Peril and Fortuity in Property and Liability Insurance*, 36 TORT & INS. L.J. 777 (2001) (suggesting that courts invoking concepts of risk assumed may tacitly create unwritten rules favoring insurers and would render better decisions focusing on the insurance contract itself). The *Lachs* dissent does, of course, focus on contract language. But it does so with an implicit, overly generous regard for the insurer’s desire to limit its risk exposure to only “civilian scheduled airlines” even though it established a marketing system that was sure to take money from those flying other airlines in the terminal. See *Lachs*, 118 N.E.2d at 560-64 (Fuld, J. dissenting).

<sup>30</sup> See Kenneth S. Abraham, *A Theory of Insurance Policy Interpretation*, 95 MICH. L. REV. 531, 567-69 (1996) (concluding that rule of construing policy terms against insurer/drafter deservedly is key foundation of proper judicial approach to insurance policy construction because it provides a relatively simple and fair method of rendering apt decisions in light of the operation of insurance and contracting markets).

<sup>31</sup> See Abraham, *supra* note 29, at 778-79 (noting that enforcement of *contra proferentem* maxim against insurers serves the purpose of forcing insurer/contract drafter to provide greater information). In the context of airport vending machine insurance, however, the forcing of a clear policy definition is far less likely to reach the purchaser. In other instances, such as the purchase of a commercial liability policy by a business, the information-forcing value of the *contra proferentem* default rule is likely to be significant.

<sup>32</sup> In this regard, the *Lachs* dissent provided the intellectual pedigree for the leading case finding no coverage under similar circumstances. See *Mut. of Omaha Ins. Co. v. Russell*, 402 F.2d 339 (10th Cir. 1968), *cert. denied*, 394 U.S. 973 (1969) (applying Kansas law) (no coverage for decedent policyholder who purchased flight insurance with duration of four days but was forced to delay return, dying in crash twelve hours after expiration of the policy). However, *Russell* is more defensible than the *Lachs* dissent. Unlike the term “civilian scheduled airline,” the time limit in a policy is a term capable of clear lay understanding. If a court is willing to overlook the hurried point-of-sale marketing of airline flight insurance, a court could justifiably place the risk of delayed travel on the policyholder as part of the insurance “bargain.”

Rather than think about these factors, the dissent invokes the technical case law of airline regulation – a factor at least as removed from the insuring transaction as the nontextual considerations invoked by the majority. Yet the dissent accuses the majority of roving too far from the policy in making its decision.

The dissent's reverence for its reading of the text is particularly odd under the circumstances of the sale. Even if Sadie Bernstein had shared the insurer's view of the meaning of "civilian scheduled airline," she had no realistic opportunity to read the policy. Few airline passengers arrive at the terminal with sufficient time on their hands to read and study a specimen policy dangling from a vending machine. As a practical matter, she bought a prepackaged product she assumed covered her on any flight she took out of the airport. She paid her money first and then received her goods, much like a buyer in any over-the-counter retail transaction. But Bernstein had no salesperson with whom she could talk. Even a supermarket shopper has more opportunity to seek guidance and more opportunity to inspect the goods before purchase. The dissent remained indifferent to these factors.

## II. *LACHS* AND THE LEGAL LANDSCAPE

Because *Lachs* involved the unusual circumstances of vending machine insurance and flight insurance, both non-mainstream forms of marketing and coverage, there is a tendency to see *Lachs* as simply an interesting case in an odd subset of insurance law.<sup>33</sup> As I hope the preceding discussion of the case has shown, *Lachs* is a good case for illustrating the range of considerations applicable in any insurance coverage dispute and for illustrating the differing judicial approaches to these disputes. There may also be a temptation to explain *Lachs* as result-oriented because of its unusual circumstances and the understandable sympathy a court might have for the victim of an airline disaster and her family. But on closer examination, the approach of the *Lachs* majority reflects quite well the overall approach to insurance disputes taken by courts, at least when courts are performing at their best.

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However, this approach can still be criticized in view of the high premiums charged and limited coverage offered. As a matter of unconscionability and public policy, coverage under such a flight policy should not be cut off by the relatively minor extension of the time limit set forth in the policy so long as the policyholder did not make major changes in travel plans that did not increase the insurer's risks. For example, what if Russell's plane crashed at the completion of the return flight only twenty minutes after expiration of the policy? Under these circumstances, the insurer's risk is not greatly increased – it is still well paid for limited coverage – while the consequences of such strict construction can be devastating for the beneficiary. Of course, the passenger is foolish if flight insurance is all that he or she has provided for his or her dependents in the event of death, opening the question of whether the flight insurance product should be more heavily regulated or banned altogether – but that's a regulatory topic for another day.

<sup>33</sup> Certainly, I have fallen prey to this tendency. See STEMPEL, *supra* note 4, at 3-123-6 (discussing the vending machine insurance cases as their own universe). See also ROBERT H. JERRY II, UNDERSTANDING INSURANCE LAW §32 (2d ed. 1996) (taking the same approach).

### A. General Ground Rules of Contract and Insurance Coverage

New York has the standard contract law ground rules of most American jurisdictions. Contracts are to be interpreted consistently with the intent of the contracting parties.<sup>34</sup> Contracts are to be interpreted to fulfill their purpose.<sup>35</sup> The language of the contract is normally the best indication of the intent of the parties, the purpose of the contract, and the expectations of the parties. Consequently, when contract text is clear and unambiguous and does not lead to absurd results, courts generally enforce the contract according to its text, irrespective of the bargaining power of the parties or whether the contract is one of adhesion.<sup>36</sup> In addition, New York, like other American states, will not enforce contracts that are illegal under its substantive law or that violate state public policy.<sup>37</sup>

When contract text is unclear (either because it is vague or ambiguous), courts are to construe the contract in order to reasonably uphold the intent of the parties and the purpose of the contract.<sup>38</sup> The contract is intended to be read as a whole, and the courts attempt to give effect to all contract provisions if that is possible without violating other contract construction precepts.<sup>39</sup> Where contract text is unclear or would lead to unacceptable results if literally applied, courts look to extrinsic evidence and the function the contract is intended to serve.<sup>40</sup> In apt cases, courts will review a wide variety of extrinsic

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<sup>34</sup> See *Record Club of Am., Inc. v. United Artists Records, Inc.*, 890 F.2d 1264, 1267 (2d Cir. 1989) (applying New York law as are all federal appellate cases in this article unless otherwise indicated); *Kenevan v. Empire Blue Cross & Blue Shield*, 791 F. Supp. 75 (S.D.N.Y. 1992); *Uniroyal, Inc. v. Home Ins. Co.*, 707 F. Supp. 1368, 1373-74 (E.D.N.Y. 1988); *W.W.W. Assocs. Inc. v. Giancontieri*, 566 N.E.2d 639, 642 (N.Y. 1990).

<sup>35</sup> See *Newmont Mines, Ltd. v. Hanover Ins. Co.*, 784 F.2d 127, 136-37 (2d Cir. 1986); *Lavanant v. Gen. Accident Ins. Co. of Am.*, 595 N.E.2d 819, 822 (1992); *Ace Wire & Cable Co., Inc. v. Aetna Cas. & Sur. Co.*, 457 N.E.2d 761, 764 (N.Y. 1983).

<sup>36</sup> See *United States v. 0.35 Of An Acre Of Land, More Or Less, Situated In Westchester County, State of N.Y.*, 706 F. Supp. 1064, 1070 (S.D.N.Y. 1988); *Slatt v. Slatt*, 477 N.E.2d 1099, 1100 (N.Y. 1985); *Breed v. Ins. Co. of N. Am.*, 385 N.E.2d 1280, 1282. See Charles C. Marvel, Annotation, *Division of Opinion Among Judges on Same Court or Among Other Courts or Jurisdictions Considering Same Question, As Evidence That Particular Clause of Insurance Policy is Ambiguous*, 4 A.L.R.4th 1246 (1981).

<sup>37</sup> See *Drutman Realty Co., Ltd P'ship v. Jindo Corp.*, 865 F. Supp. 1093, 1100-01 (S.D.N.Y. 1994); *Metro. Life Ins. Co. v. Noble Lowndes Int'l, Inc.*, 643 N.E.2d 504, 509 (N.Y. 1994); *Goldfarb v. Goldfarb*, 86 A.D.2d 459 (N.Y. 1982). For example, even a clear exculpatory clause will not apply to protect a party from willful or grossly negligent acts. See *Kalisch-Jarcho, Inc. v. City of N.Y.*, 448 N.E.2d 413, 416 (N.Y. 1983).

<sup>38</sup> See *McGrail v. Equitable Life Assurance Soc'y of the U.S.*, 55 N.E.2d 483, 486 (N.Y. 1944).

<sup>39</sup> See *Cruden v. Bank of N.Y.*, 957 F.2d 961 (2d Cir. 1992); *Chase v. Columbia Nat'l Corp.*, 832 F. Supp. 654, 661 (S.D.N.Y. 1993); *Giancontieri*, 566 N.E.2d at 642 (N.Y. 1990); E. ALLAN FARNSWORTH, *CONTRACTS* §§ 7.8-7.14 (3d ed. 1999). See also *Westchester Resco Co., L.P. v. New England Reinsurance Corp.*, 648 F. Supp. 842, 846 (S.D.N.Y. 1986), *aff'd*, 818 F.2d 2 (2d Cir. 1987) (applying New York law); *Employers Commercial Union Ins. Co. v. Firemen's Fund Ins. Co.*, 384 N.E.2d 668 (N.Y. 1978) (entire contract to be construed may include binder, application, or other documents in addition to four corners of the policy per se).

<sup>40</sup> See *Stonewall Ins. Co. v. Asbestos Claims Mgmt. Corp.*, 73 F.3d 1178, 1187 (2d Cir. 1995) (assessing case according to both New York and Texas law, which were found to be equivalent on most contested issues); *Stoney Run Co. v. Prudential-LMI Commercial Ins.*

evidence, including witness testimony (on the stand or by affidavit), statements by the parties or their agents, contract documents, correspondence, notes, insurer records, the customary use of terms in the trade, the course of dealing between the parties, the negotiation history of the instrument, and the drafting history of the contract, as well as the function and nature of the contract in light of the context and surrounding circumstances affecting the contract. Applicable law and public policy may also be considered.

When applying the literal language of a contract would create an absurd result or an outcome that cannot reasonably have reflected the parties' contemplation, language must be given its reasonable rather than literal application.<sup>41</sup> Even clear contract text that does not lead to an absurd result may not be enforced strictly where the text is clearly contradicted by other evidence of intended meaning or where consideration of nontextual matter is necessary to prevent a fraud or intentional forfeiture.<sup>42</sup>

Where a contract term is ambiguous, extrinsic evidence will be heard by the court to interpret, explain, or amplify the term in dispute, and perhaps even to refine it.<sup>43</sup> A word, term, provision, or clause of a contract is ambiguous when it is capable of more than one reasonable interpretation.<sup>44</sup> Ordinarily, courts make most of their determinations regarding whether the relevant words are ambiguous by examining the words themselves in isolation, giving words their "plain, ordinary, popular and non-technical sense."<sup>45</sup> Put another way, contractual language can be said to be clear or unambiguous only if "it has definite and precise meaning unattended by danger of misconception in purport of the contract itself and concerning which there is no reasonable basis for difference of opinion."<sup>46</sup> As part of the process of interpreting a disputed contract, however, courts will examine the entire contract text and the context of the transaction.

After this analytic exercise, a term that is seemingly ambiguous may become clarified or a competing construction may become viewed as unreasonable. In addition, a term that is seemingly clear standing alone may become viewed as ambiguous after other provisions of the contract and the entire trans-

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Co., 47 F.3d 34, 36-37 (2d Cir. 1995); *Kimmins Indus. Serv. Corp. v. Liberty Mut. Ins. Co.*, 748 F.2d 760, 765 (2d Cir. 1984).

<sup>41</sup> See *Burger King Corp. v. Horn & Hardart Co.*, 893 F.2d 525, 529 (2d Cir. 1990); *Reape v. N.Y. News, Inc.*, 504 N.Y.S.2d 469, 470 (App. Div. 1986).

<sup>42</sup> See *Bersani v. Gen. Accident Fire & Life Assurance Corp., Ltd.*, 330 N.E.2d 68, 70 (N.Y. 1975); *Katzman v. Aetna Life Ins. Co.*, 128 N.E.2d 307 (N.Y. 1955); *Whipple v. Brown Bros. Co.*, 121 N.E. 748, 751 (N.Y. 1919).

<sup>43</sup> See *Stonewall Ins. Co. v. Asbestos Claims Mgmt. Corp.*, 73 F.3d 1178, 1187 (2d Cir. 1995); *U.S. Fire Ins. Co. v. Gen. Reinsurance Corp.*, 949 F.2d 569, 571 (2d Cir. 1991); *Chimart Assocs. v. Paul*, 489 N.E.2d 231, 234 (N.Y. 1986); *Brady v. Nally*, 45 N.E. 547, 548 (N.Y. 1896).

<sup>44</sup> See *U.S. Fire Ins. Co.*, 949 F.2d at 572; *Vargas v. Ins. Co. of N. Am.*, 651 F.2d 838, 840 (2d Cir. 1981).

<sup>45</sup> See *Rocon Mfg., Inc. v. Ferraro Co.*, 605 N.Y.S.2d 591, 592 (App. Div. 1993). *But see* *Saunders v. Agric. Ins. Co. of Watertown*, 60 N.E. 635 (N.Y. 1901) (insured property described as "barn" ambiguous given contracting history and context of loss).

<sup>46</sup> See *John Hancock Mut. Life Ins. Co. v. Amerford Int'l Corp.*, 22 F.3d 458, 461 (2d Cir. 1994) (quoting *Hunt Ltd. v. Lifschultz Fast Freight, Inc.*, 889 F.2d 1274, 1277 (2d Cir. 1989)); *Seiden Assocs., Inc. v. ANC Holdings, Inc.*, 959 F.2d 425 (2d Cir. 1992).

action are reviewed.<sup>47</sup> As one court put the matter, “clarity in a contract is a property of the correspondence between the contract and the things or activities that it regulates, and not just the semantic surface.”<sup>48</sup>

When a court must construe an ambiguous or unclear contract provision and resort to extrinsic evidence does not resolve the question, the term in dispute is construed against the drafter of the contract. This is the well-known *contra proferentem* rule discussed in the *Lachs* case and is a staple of New York’s general contract law as well as its insurance contract law.<sup>49</sup> Lack of clarity of meaning typically arises from a few recurring types of situations. For example, one might distinguish between vagueness and ambiguity. Most American contract and insurance scholars would agree that a term is vague when it is generally understandable but becomes imprecise when applied in relatively unusual situations.<sup>50</sup>

If the text of the primary disputed provision of a contract (including, of course, an insurance policy) has several apt meanings, application of the term can become unclear in a particular situation. This constitutes what is commonly referred to as “ambiguity of term” – words that themselves admit of more than one reasonable meaning. For example, a contract may refer to the ship “Peerless,” a term that in a famous contract case literally applied to two different ships.<sup>51</sup>

If the text in dispute is unclear because of the manner in which terms are used, the contract exhibits “syntactical” ambiguity. For example, an insurance policy might exclude expense incurred due to any “disease of organs of the body not common to both sexes.” Under this language, it is textually unclear whether it is the disease that must occur in only one gender in order to trigger the exclusionary language or whether it is sufficient that the bodily organ be distinctly male or female to exclude coverage of even diseases occurring in

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<sup>47</sup> See *Kenevan v. Empire Blue Cross & Blue Shield*, 791 F. Supp. 75, 79 (S.D.N.Y. 1992).

<sup>48</sup> See *AM Int’l, Inc. v. Graphic Mgmt. Assocs., Inc.*, 44 F.3d 572, 575 (7th Cir. 1995) (Posner, J.) (applying Illinois law).

<sup>49</sup> See *Record Club of Am., Inc. v. United Artists Records, Inc.*, 890 F.2d 1264, 1271 (2d Cir. 1989); *Uniroyal, Inc. v. Home Ins. Co.*, 707 F. Supp. 1368 (E.D.N.Y. 1988); *Tri Town Antlers Found., Inc. v. Fireman’s Fund Ins. Co.*, 559 N.E.2d 1283 (N.Y. 1990).

<sup>50</sup> See E. ALLAN FARNSWORTH, *CONTRACTS* (3d ed. 1999); E. Allan Farnsworth, *Meaning in the Law of Contracts*, 76 *YALE L.J.* 939 (1967). For example, all would agree that an accident is a covered “occurrence” under the typical American automobile policy. But if a car spinning on slippery pavement hits three cars, it is textually unclear whether there has been one occurrence or three and a controversy regarding coverage limits of “\$20,000 per occurrence” cannot be resolved by focus on contract text alone. See ROBERT H. JERRY II, *UNDERSTANDING INSURANCE LAW* § 25A, at 94 (1987), from which this illustration is taken and which cites cases taking opposing views on the matter. Compare *Liberty Mut. Ins. Co. v. Rawls*, 404 F.2d 880 (5th Cir. 1968) (two occurrences), with *Olsen v. Moore*, 202 N.W.2d 236 (Wis. 1972) (one occurrence).

<sup>51</sup> See *Raffles v. Wichelhaus*, 2 H. & C. 906, 159 Eng. Rep. 375 (Excheq. 1864). The *Raffles v. Wichelhaus* court reached the sensible conclusion that neither party was bound by the other’s concept of which “Peerless” vessel would carry the shipments. In determining which of two equally plausible meanings of “Peerless” applied, a court would decide based on the intent and expectations of the parties if extrinsic evidence revealed those intentions or expectations. If no such basis for decision were available, the contract would fail under classic contract law because of mutual mistake. See FARNSWORTH, *CONTRACTS* § 7.9, at 463 (3d ed. 1990).

both men and women. Thus, it is textually unclear whether a policyholder is covered for health care costs occasioned by a tumor of the uterus since a tumor can occur in any male or female organ but the specific tumor at issue in the coverage dispute occurred in an organ found only in women. As a prominent insurance scholar observed "[t]he words of the policy are relatively precise; the problem is one of syntax."<sup>52</sup>

Insurance policies are contracts and insurance law is to a large degree a subspecies of contract law. The rules established for the construction and interpretation of written contracts apply to insurance policies.<sup>53</sup> The better reasoned decisions recognize, however, that contract interpretation will often be affected by the manner in which insurance policies differ from other contracts. Apart from the obviously more active government intervention affecting insurance than exists for other contracts,

[T]he distinctive nature of insurance contracts and refinements in the parts and clauses thereof have given rise to certain standards and rules which, even if not entirely limited in their application to the construction of insurance contracts are of little practical significance apart from such contracts. Among these special rules are the rules of liberal construction in favor of the insured, the construction against exceptions and limitations, and the construction against forfeitures.<sup>54</sup>

New York law provides that interpretation of insurance policies as contracts must fulfill the intent and purpose of the transaction.<sup>55</sup> The notion that insurers have somewhat different obligations to their customers than do other merchants is well established and does not constitute a slanted or uneven approach to construing insurance policies. Rather, recognition of the special responsibilities of insurers simply provides the context in which basic contract

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<sup>52</sup> See JERRY, *supra* note 50, § 25A, at 95 (1987). Professor Jerry draws this example from Professor Farnsworth's *Meaning in the Law of Contracts*, *supra* note 50, which borrowed it from an actual case: *Business Men's Assurance Ass'n v. Read*, 48 S.W.2d 678 (Tex. Civ. App. 1932) (coverage found for policyholder). Where one contract provision is seemingly clear but is in conflict with another policy provision, there exists ambiguity of organization in the policy. This ambiguity of organization also occurs where the policy contains two or more terms seemingly clear in isolation but in apparent conflict when juxtaposed. For example, a policy subject to the law of State X may in one section state that it does not provide coverage for reckless or intentional behavior but in another section state that it covers punitive damage awards, which in State X may be awarded upon a showing of recklessness. The provisions of the policy, clear in isolation, are in apparent conflict over whether coverage exists for a policyholder against whom a judgment is entered for punitive damages arising out of reckless conduct.

<sup>53</sup> See *Skandia Am. Reinsurance Corp. v. Schenck*, 441 F. Supp. 715, 723 (S.D.N.Y. 1977) (noting that insurance policies, like other contracts, may be subject to different treatment when they are contracts of adhesion); *F.S. Royster Guano Co. v. Globe & Rutgers Fire Ins. Co.*, 168 N.E. 834 (N.Y. 1929).

<sup>54</sup> See 69 NEW YORK JURISPRUDENCE 2D INSURANCE § 692, at 80 (1988) (citations omitted).

<sup>55</sup> See *Stoney Run Co. v. Prudential-LMI Commercial Ins. Co.*, 47 F.3d 34, 37 (2d Cir. 1995); *Cont'l Cas. Co. v. Rapid-Am. Corp.*, 609 N.E.2d 506 (N.Y. 1993) ("practical" construction must be given where insurance policy text is unclear). The distinction between insurance policies and "ordinary" contracts is at the margin appreciated by even laypersons, a point pithily made in a *New York Times* financial column: "Unlike other corporations, whose first loyalty is to their owners, or shareholders, insurance companies have long been regulated under the philosophy that their primary obligation is to policyholders." Michael Quint, *Market Place: Who Would Win in a Split-Up Cigna? It Depends Who is Asked*, N.Y. TIMES, Dec. 8, 1995, at D8.

law is applied to adjudicate insurance controversies. Although the insurer-policyholder relationship is not technically a fiduciary relationship, it has been described as "fiduciary in nature" in both New York and other American jurisdictions.<sup>56</sup> Breach of the insurer's duties to the policyholder can give rise to the tort claim of bad faith and a resulting judgment may include exemplary damages. Although the insurer-policyholder relationship is largely one of contract under New York law, special traits of the relationship are important to the courts' adjudication of insurance disputes and give rise to particular rights and responsibilities on the part of both insurers and policyholders.<sup>57</sup>

In difficult cases, however, courts take cognizance of the nature of insurance, its function in a modern industrial society, its relation to the American tort system of personal injury compensation, the degree to which risk-spreading contributes to business and consumer welfare, the context in which the insurance policy is issued, and the reasonable expectations of the policyholder.<sup>58</sup>

New York law, like that of other American jurisdictions, recognizes that estoppel principles may affect insurance coverage questions. New York recognizes the concepts of both "equitable estoppel," a situation in which the insurer, by virtue of inequitable conduct toward its policyholder, is deemed to be stripped of a coverage defense that would otherwise be available to it under the policy,<sup>59</sup> and promissory estoppel or contract by detrimental reliance.<sup>60</sup> Where

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<sup>56</sup> See *Sucrest Corp. v. Fisher Governor Co.*, 371 N.Y.S.2d 927, 941 (Colo. 1975) ("there is authority elsewhere declaring the relationship to be of a fiduciary nature, akin to that of principal and agent. Whatever the relationship, there is an obligation of full disclosure and extreme good faith by the insurer in its dealings with its insured.").

<sup>57</sup> See *Gordon v. Nationwide Mut. Ins. Co.*, 285 N.E.2d 849, 858 (N.Y. 1972) ("doctrine that a liability insurer owes a duty of good faith to protect its insured, including the good faith consideration of opportunities to settle, because of its exclusive control in the management of claims has deep roots in New York") (Breitel, J., dissenting). See also *Rocanova v. Equitable Life Assurance Soc'y*, 634 N.E.2d 940, 945 (N.Y. 1994) (under New York law, all contracts carry with them an implied covenant of good faith and fair dealing; although punitive damages are not available against insurer for mere breach of contract, independent tort or breach of legal duty of fair dealing may give rise to exemplary damages).

<sup>58</sup> See *Ace Wire & Cable Co. v. Aetna Cas. & Sur. Co.*, 457 N.E.2d 761 (N.Y. 1983); *Tri Town Antlers Found., Inc. v. Fireman's Fund Ins. Co.*, 550 N.Y.S.2d 953 (App. Div. 1990). *Little v. Blue Cross of W. N.Y., Inc.*, 424 N.Y.S.2d 553, 555-56 (App. Div. 1980), summarizes New York law well on this point:

[T]he terms of a contract as a whole must be examined in determining the intent of the parties, and where the meaning of a policy of insurance is in doubt or is subject to more than one reasonable interpretation, all ambiguity must be resolved in favor of the policyholder and against the company which issued the policy; the reasonable expectation of the insured, from his reading of the policy, must control.

See also 69 NEW YORK JURISPRUDENCE 2D INSURANCE § 706, at 100 (1988):

The meaning of coverage and exclusion provisions of a liability insurance policy is to be resolved in the light of the reasonable expectation and purpose of an ordinary businessman in making the contract of insurance. If an insurance company desires to limit its liability in a drastic manner it must express the limitation in language that will reasonably convey its meaning to an intelligent layman or person of ordinary business intelligence.

<sup>59</sup> See *Triple Cities Constr. Co. v. Md. Cas. Co.*, 151 N.E.2d 856 (N.Y. 1958); *Tel-Tru Mfg. Co. v. N. River Ins. Co.*, 456 N.Y.S.2d 287 (App. Div. 1982); NEW YORK JURISPRUDENCE 2D INSURANCE § 1238 (1988). For example, if the policy text clearly provided that a proof-of-loss form must be submitted within sixty days of the loss but the adjuster instructed the policyholder to "take as much time as you need; 90 days, whatever," the insurer would be



one party reasonably relies to its detriment upon the representations of another, the representing party is bound and a contract exists to the extent of the reliance. New York courts recognize and apply the doctrine of waiver as well as both equitable estoppel and promissory estoppel to appropriate insurance coverage cases. Waiver results when the insurer has (either through express statements or conduct tantamount to statements) knowingly and voluntarily relinquished a right it would have pursuant to the policy.<sup>61</sup>

New York, like other jurisdictions, requires that the policyholder bear the burden of persuasion to show that a given loss falls within the scope of the policy coverage. Once that initial burden has been satisfied, it is the insurer's burden of persuasion to show the applicability of any asserted exclusion in the policy. Courts usually take a functional view of exclusions, finding that any policy provision that tends to defeat coverage is an "exclusion," even if not denominated as such on the face of the policy.<sup>62</sup> For example, New York courts have treated the "expected or intended" language found in most liability policies as an exclusion even though these words are ordinarily found in the insuring agreement itself or the definitions section of the policy.<sup>63</sup>

All of these "hornbook" principles of insurance law are perfectly consistent with the *Lachs* decision.<sup>64</sup> Unfortunately, *Lachs* has unfairly been characterized as a decisional oddity prompted by an unusual situation and decided in contravention of clear contract language.<sup>65</sup> Upon closer examination, *Lachs*, to

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equitably estopped from rigidly enforcing the sixty-day proof-of-loss time limit. Unfair conduct by the insurer that operates to prejudice the policyholder will estop the insurer from invoking provisions of the policy affected by the unfair conduct.

<sup>60</sup> See generally RESTATEMENT (SECOND) OF CONTRACTS § 90 (1981); *I & I Holding Corp. v. Gainsburg*, 12 N.E.2d 532 (N.Y. 1938); *Allegheny Coll. v. Nat'l Chautauqua County Bank of Jamestown*, 159 N.E. 173 (N.Y. 1927). Indeed, one of America's most famous promissory estoppel cases (reprinted in several casebooks and discussed at length in virtually every major treatise) stems from New York law. See *Hamer v. Sidway*, 27 N.E. 256 (N.Y. 1891) (nephew who refrains from "drinking liquor, using tobacco, swearing and playing cards or billiards for money" until age twenty-one in reliance on payment promised by uncle entitled to funds). See also *Spiegel v. Metro. Life Ins. Co.*, 160 N.E.2d 40 (N.Y. 1959) (policyholder was awarded coverage sought when court treated the coverage in question as part of an expanded remedy under the policy in force rather than as the remedy provided by a new contract created via promissory estoppel).

<sup>61</sup> See *Clark v. West*, 86 N.E. 1 (N.Y. 1908); *Robertson v. Metro. Life Ins. Co.*, 88 N.Y. 541 (1882).

<sup>62</sup> See *Stonewall Ins. Co. v. Asbestos Claims Mgmt. Corp.*, 73 F.3d 1178 (2d Cir. 1995) ("under New York law, the exclusionary effect of policy language, not its placement, controls allocation of the burden of proof"); *Seaboard Sur. Co. v. Gillette Co.*, 476 N.E.2d 272 (N.Y. 1984); *Utica Mut. Ins. Co. v. Prudential Prop. & Cas. Ins. Co.*, 477 N.Y.S.2d 657, 660 (App. Div. 1984) ("It is the insurer which [sic] has the burden of proof to establish that a claim is encompassed by an exclusion in a policy . . . and any limitation in coverage must be described in clear and explicit language"), *aff'd*, 478 N.E.2d 1305 (N.Y. 1985).

<sup>63</sup> See *City of Johnstown, N.Y. v. Bankers Standard Ins. Co.*, 877 F.2d 1146 (2d Cir. 1989); *Town of Moreau v. Orkin Exterminating Co. Inc.*, 568 N.Y.S.2d 466 (App. Div. 1991).

<sup>64</sup> See *supra* text accompanying notes 8-26 (describing *Lachs* decision and its methodology).

<sup>65</sup> See STEMPER, LAW OF INSURANCE CONTRACT DISPUTES, *supra* note 4, §3.18 (describing *Lachs* as case that found for policyholder despite clear language regarding no coverage for "unscheduled" airlines); Roger Henderson, *The Reasonable Expectations Doctrine After Two Decades*, 51 OHIO ST. L.J. 823, 836-37 (1990) (same). See also Leon Wein, *Maladjusted*

a large extent, encompasses and vindicates basic contract construction principles and prevailing insurance law norms. In particular, as the discussion of the case reflects, it is by no means crystal clear that the term "civilian scheduled airline" meant that Sadie Bernstein's fateful Miami Airlines flight was uncovered. If nothing else, then, the grundnorm of insurance law that insurers bear the burden to show the applicability of exclusionary language would constitute sufficient grounds for the *Lachs* holding.

### *B. Lachs and Reasonable Expectations Analysis*

But even if one is persuaded that the term "civilian scheduled airline" has the clear meaning proffered by the insurer, *Lachs* continues to look rightly decided, perhaps more today than when it was rendered. Many American cases have specifically adopted a "reasonable expectations" doctrine for application to insurance coverage disputes.<sup>66</sup> Although courts have been doing this prior to *Lachs*, reasonable expectations analysis has been referred to as a doctrine with a name during only the past thirty years since the publication of Keeton's famous *Rights at Variance* article.<sup>67</sup> Depending on who is counting, when one counts, and how one counts, the reasonable expectations "doctrine" can be said to have been accepted in one-third to one-half of the states.

The reasonable expectations "doctrine" in its "pure" form is most succinctly summarized by Keeton's phrase that under the doctrine, coverage in a disputed case may be found to exist where the policyholder held objectively reasonable expectations of coverage even if painstaking study of the policy language would have negated those expectations. New York is commonly viewed as perhaps the most prominent American jurisdiction with a high court that has never expressly embraced the Keeton doctrine in this formula.<sup>68</sup> However, federal courts applying New York law and intermediate New York appellate cases have endorsed the reasonable expectations doctrine in essentially "pure" form where policyholder expectations can overcome even clear and reasonable policy language negating coverage.<sup>69</sup> One treatise has even concluded, apparently without reservation, that New York has adopted the Keeton reasonable expectations doctrine.<sup>70</sup> New York courts indeed place a good deal of

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*Contrivances and Clumsy Automation: A Jurisprudential Investigation*, 9 HARV. J.L. & TECH. 375 (1996); Leon Wein, *The Responsibility of Intelligent Artifacts: Toward an Automation Jurisprudence*, 9 HARV. J.L. & TECH. 103 (1992) (both times describing *Lachs* decision as prompted by judicial distrust of machines).

<sup>66</sup> See STEMPER, *supra* note 4, § 4.09 (summarizing adoption of doctrine in approximately one-third to one-half the states).

<sup>67</sup> See Keeton, *supra* note 1.

<sup>68</sup> See Henderson, *supra* note 65, at 836-37 n.74 ("New York Court of Appeals has never embraced the doctrine as articulated by Professor Keeton.").

<sup>69</sup> See, e.g., *Fried v. N. River Ins. Co.*, 710 F.2d 1022 (4th Cir. 1983); *Bd. of Educ., Yonkers City Sch. Dist. v. CNA Ins. Co.*, 647 F. Supp. 1495 (S.D.N.Y. 1986), *aff'd*, 839 F.2d 14 (2d Cir. 1988); *Champion Int'l Corp. v. Cont'l Cas. Co.*, 400 F. Supp. 978 (S.D.N.Y. 1975), *aff'd*, 546 F.2d 502 (2d Cir. 1976), *cert. denied*, 434 U.S. 819 (1977), *Atl. Cement Co., Inc. v. Fid. & Cas. Co. of N.Y.*, 459 N.Y.S.2d 425 (1983), *aff'd*, 471 N.E.2d 142 (N.Y. 1984); *IQ Originals, Inc. v. Boston Old Colony Ins. Co.*, 447 N.Y.S.2d 174 (1982), *aff'd*, 444 N.E.2d 1004 (N.Y. 1982); *Riordan v. Auto Club of N.Y., Inc.*, 422 N.Y.S.2d 811 (1979).

<sup>70</sup> See BARRY R. OSTRANGER & THOMAS R. NEWMAN, *HANDBOOK ON INSURANCE COVERAGE DISPUTES* § 1.03[b] (10th ed. 2000).

weight upon the policyholder's expectations regarding the policy in question even when not applying a reasonable expectations doctrine as such.<sup>71</sup>

Keeton summarized his assessment in the now-famous words:

objectively reasonable expectations of applicants and intended beneficiaries regarding the terms of insurance contracts will be honored even though painstaking study of the policy provisions would have negated those expectations.<sup>72</sup>

When courts apply "pure" reasonable expectations theory, the court mandates coverage consistent with the policyholder's expectations even if relatively clear policy language is to the contrary.<sup>73</sup>

*Lachs* clearly is considering the reasonable expectations of the policyholder who purchased the flight insurance at issue in the case. A more difficult question is whether *Lachs* was using a "strong" form of the Keeton reasonable expectations approach (one that found coverage even though the policy language was clear) or a moderate-to-weak version of the approach (one that considered the policyholder's expectations in order to determine the construction to give to unclear policy text). After having read *Lachs* intermittently over the years and reading it with some renewed vigor for this Symposium, I am quite certain that the court was using only a mild form of the reasonable expectations approach. *Lachs* in large part rested on context and the purpose of the insuring agreement as well as the difficult policy language and the principle of contra proferentem.

In *Lachs*, the policyholder's expectations did not overbear clear text or other clear indicia of intent. Rather, policyholder expectations helped to resolve the controversy as to the meaning of the legal policy because this datum fit so well with other indicia of contract meaning. This view of *Lachs* is also quite consistent with decades of New York jurisprudence, in which New York courts have frequently resolved insurance coverage disputes by using policyholder (and insurer) expectations as a factor for decision but have always

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<sup>71</sup> See, e.g., *New York v. AMRO Realty Corp.*, 936 F.2d 1420 (2d Cir. 1991); *J.A. Brundage Plumbing & Roto-Rooter, Inc. v. Mass. Bay Ins.*, 818 F. Supp. 553 (W.D.N.Y. 1993), vacated by 153 F.R.D. 36 (W.D.N.Y. 1994); *Album Realty Corp. v. Am. Home Assurance Co.*, 607 N.E.2d 804 (N.Y. 1992); *Ace Wire & Cable Co., Inc. v. Aetna Cas. & Sur. Co.*, 457 N.E.2d 761 (N.Y. 1983); *Thomas J. Lipton, Inc. v. Liberty Mut. Ins. Co.*, 314 N.E.2d 37 (N.Y. 1974); *Bird v. St. Paul Fire & Marine Ins. Co.*, 120 N.E. 86 (N.Y. 1918).

<sup>72</sup> See Keeton, *supra* note 1, at 967. In addition, the Keeton article posited additional principles creating policyholder rights beyond the terms of insurance policy text. According to Keeton, "If the enforcement of a policy provision would defeat the reasonable expectations of the great majority of policyholders to whose claims it is relevant, it will not be enforced even against those who know of its restrictive terms." *Id.* at 974.

<sup>73</sup> The rationale for the approach is based on several factors: complexity of policy language; standardization of policies; the adhesion nature of most insurance policies; the contracting process, in which insured almost never see the full policy until after it is in force and seldom read it; and the need to protect unsophisticated or vulnerable insured. *Id.* at 963-85; see also Mark C. Rahdert, *Reasonable Expectations Reconsidered*, 18 CONN. L. REV. 323, 324-30 (1986); Kenneth S. Abraham, *Judge-Made Law and Judge-Made Insurance: Honoring the Reasonable Expectations of the Insured*, 67 VA. L. REV. 1151, 1153-55 (1981).

stopped short of full embrace of the approach as outlined in the Keeton article.<sup>74</sup>

Well prior to *Lachs*, New York courts resisted policy construction inconsistent with the reasonable expectations of the policyholder in light of the nature of the coverage purchased. For example, the court in *Ira S. Bushey & Sons v. American Insurance Co.*,<sup>75</sup> stated:

We are construing a policy of insurance and we are not bound by the niceties of definition that might otherwise be proper. When a builder takes out builders' risk insurance, delivers his materials on the ground, and does some manifest act evidencing his intention to incorporate them into a building, and when there is and can be no dispute about his intention, it would be a harsh rule to require that he should protect himself by a general open policy on stock in order to cover a loss sustained before he had actually joined one timber to another. It was reasonable for the insured to believe that it had covered the risk of loss by fire of its materials when it took out the policy in suit. The ordinary builder would agree with the plaintiff's [policyholder's] witness that "the building of the boat starts just as soon as you start getting that material ready" and that such a construction of the policy expresses the fair and reasonable understanding of the risk.<sup>76</sup>

In practice, then, the reasonable expectations of the policyholder have proven vitally important for use in construing the policy's terms and meaning well before there was a "reasonable expectations doctrine" as such and well after the doctrine was enunciated. Courts continue to utilize the expectations concept in construing insurance policies even though they may continue to talk primarily in the more traditional language of textual meaning, ambiguity, contra proferentem, absurd results, benefit of the bargain, and so on.

### III. LAW WITHOUT LABELS: *LACHS* AND THE LONGSTANDING BUT UNDERAPPRECIATED COMPREHENSIVE APPROACH TO INSURANCE POLICY CONSTRUCTION

Most important in *Lachs* was that the court was not imprisoned by any one factor, approach, or doctrine in seeking to render the correct construction of the insurance policy at issue. Rather, the *Lachs* majority was deploying a variety of tools for assessing contract meaning. In essence, the *Lachs* court was zeroing in on the legally controlling meaning of the policy and the transaction as its consideration of text, intent, purpose, policyholder expectations, context, practicality, and public policy all led the court to conclude that Sadie Bernstein was indeed covered under the policy and that her beneficiary could collect the modest death benefit she had purchased at a relatively high premium cost.

The use of a vending machine to sell the insurance was a factor, but not the overarching factor traditionally thought by most commentators. Rather, the vending machine, like the specimen policy with the words obscured, the location of the sale, and the circumstances of the trip, was just part of the overall context that the court properly considered in order to interpret the policy and

<sup>74</sup> See, e.g., *In re Prudential Lines, Inc.*, 170 B.R. 222 (S.D.N.Y. 1994); *Cont'l Cas. Co. v. Rapid-Am. Corp.*, 609 N.E.2d 506 (N.Y. 1993); *Maurice Goldman & Sons, Inc. v. Hanover Ins. Co.*, 607 N.E.2d 792 (N.Y. 1992).

<sup>75</sup> 142 N.E. 340 (N.Y. 1923).

<sup>76</sup> *Id.* at 342.

decide a case involving an insurance policy with problematic language. *Lachs* was not a case embracing a pumped-up version of the reasonable expectations doctrine or torturing language in search of an ambiguity. It was a case decided upon context and common sense.

In opposition to the decision, the dissent largely embraced, with a vengeance, a highly textual approach to construing the policy. One sees this scene played again and again when courts address coverage disputes. Some judges search for a textual basis for their decision in the belief that a decision on any other basis imperils contract law and perhaps law itself.<sup>77</sup> Other judges give more consideration to surrounding circumstances, statements and conduct reflecting on textual meaning, or the overall objective of the contract.<sup>78</sup> This dichotomy in contract interpretation has existed as long as contract law itself and is most famously reflected in the differing views of the twentieth century's giants of contract scholarship: Harvard Law's more textualist Samuel Williston and Yale Law's more context-oriented Arthur Corbin.<sup>79</sup> In the modern statu-

<sup>77</sup> See, e.g., *E. Assoc. Coal Corp. v. Aetna Cas. & Sur. Co.*, 632 F.2d 1068, 1075 (3d Cir. 1980), *cert. denied*, 451 U.S. 986 (1981) (applying Pennsylvania law) (courts must not "torture" language of insurance policy in order to find ambiguity that can be construed in favor of policyholder); *Mut. of Omaha Ins. Co. v. Russell*, 402 F.2d 339, 346 (10th Cir. 1968) (applying Kansas law) ("The printed contract controls. There it ends").

<sup>78</sup> Compare *Kent Farms, Inc. v. Zurich Ins. Co.*, 998 P.2d 292, 295 (Wash. 2000) (considering overall purpose of policy, context of injury leading to claim, and seeking to give common sense application to absolute pollution exclusion) and *Morton Int'l v. Gen. Accidental Ins. Co.*, 629 A.2d 831 (N.J. 1993), *cert. denied*, 512 U.S. 1245 (1994) (utilizing drafting history of qualified pollution exclusion to resolve coverage controversy in favor of policyholder) with *Northville Indus. Corp. v. Nat'l Union Fire Ins. Co.*, 679 N.E.2d 1044, 1049 (N.Y. 1997) (reading language of qualified pollution exclusion to bar coverage for claims arising out of gradual discharge); *Technical Coating Applicators, Inc. v. U.S. Fid. & Guar. Co.*, 157 F.3d 843 (11th Cir. 1998) (applying Florida law) (holding that absolute pollution exclusion bars coverage for claims against insulation manufacturer because fumes emitted by insulation that caused injury were chemical "irritants" even though injury arose from use as intended on job sight and not from waste discharge).

For example, in *Dimmit Chevrolet, Inc. v. Southeastern Fidelity Insurance Corp.*, 636 So. 2d 700 (Fla. 1993) (*Dimmit II*) (overruling *Dimmit I*), the Florida Supreme Court reflected this jurisprudential split both internally and as an institution. In *Dimmit I*, a majority of the court was persuaded that the qualified or "sudden and accidental" pollution exclusion (which covers pollution liability only if the discharge is sudden and accidental) applied to gradual discharges that were not intended to cause injury based on the drafting history of the exclusion. In *Dimmit II*, the court granted rehearing and reversed itself, holding that the word "sudden" so clearly implied a temporal element of abruptness to the exclusion's requirement for coverage that nontextual factors could not be considered to vary the meaning of the words.

<sup>79</sup> See, e.g., ARTHUR C. CORBIN, *THE LAW OF CONTRACTS* § 1, at 1 (1950) (One Volume Edition) (articulating reasonable expectations as basis for contract meaning – twenty years prior to Keeton's *Rights at Variance* article). Although Williston was more of a textualist and formalist than Corbin, he was not rigidly textualist as commonly thought. His treatise on occasion reflects this, as do his other writings. See generally SAMUEL WILLISTON, *CONTRACTS* (1st ed. 1920 through 4th ed. 1990) (noting at various points that contract meaning can be a product of factors). See, e.g., Samuel Williston, *Freedom of Contract*, 6 CORNELL L.Q. 365, 374 (1921) (noting that legal effect of contract text must on occasion yield to public policy concerns). See also NEIL DUXBURY, *PATTERNS OF AMERICAN JURISPRUDENCE* 21 (1995) (Williston was not as formalistic as commonly thought and in fact differed at times with Harvard Dean Christopher Langdell on this point); Jean Braucher, *The Afterlife of Contract*, 90 NW. U. L. REV. 49, 58-60 (1995) (modern contract literalists have overstated

tory and administrative state, this historical fissure of the law is now also frequently apparent on matters of statutory interpretation.<sup>80</sup> *Lachs* is a well-decided and instructive case because it appreciates the importance of policy language, but does so with regard to context and other important factors.

A textualist approach to insurance coverage is supported by several arguments suggesting that reverence for text is necessary to: (a) provide predictability in the law; (b) protect individual and social expectations; (c) prevent contract disputes from being decided upon nonlegal factors, such as post-hoc sympathy for a party; and (d) streamline judicial decision-making (if text is by far the most important factor in construction it may save resources because it focuses most on text and may avoid or reduce the search costs entailed in examining other indicia of contract meaning).

Driven by these considerations, which are perfectly persuasive as a general matter (and in cases where the textual meaning is in fact clear on its face), courts can fall prey to hyper-literalism and interpret a term according to a dictionary or technical definition even though this lends a result that is absurd or at odds with contract purpose, party expectations, justice, or public policy. The lure of textualism can also be sufficiently blinding that courts see contract language as clearer than it really is.

The *Lachs* dissent arguably succumbed to this temptation. It embraced the notion that "civilian scheduled airline" had a meaning clear to all and controlling as a matter of law with a zeal that is out of proportion to the actual linguistic clarity of the words in question. The words are unclear on their face. Only if a technical definition is employed (and even this is a stretch) are the words relatively clear in meaning. But deciding the case on this basis turns insurance law on its head by giving a term a technical meaning and applying it against the policyholder, exactly the opposite of the hornbook law of insurance even as set forth by formalists.

To be fair, the *Lachs* dissent also considered context as well as text.<sup>81</sup> Oddly, it did so in a manner that was both broader and narrower than the methodology of the majority. The dissent had a narrow view of context in that it was unwilling to consider important factors such as the vending machine, its location, the circumstances, and the equities of the arrangement. Airline passengers are seldom ambling through the airport just itching to read dense pack form contracts. Even today, only the most wired layperson could hope to analyze the *Lachs* policy in a manner that would suggest the meaning proffered by the insurer. In the pre-Internet, pre-Lexis and Westlaw, pre-laptop computer,

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Williston's intellectual support for their position). *But see* Swisher, *infra* note 98 (Williston remains most notable apostle of contract formalism).

<sup>80</sup> See WILLIAM N. ESKRIDGE, JR. & PHILIP K. FRICKEY, *LEGISLATION: STATUTES AND THE CREATION OF PUBLIC POLICY* Ch. 7 (2d ed. 1995) (reviewing theories of statutory construction and alternative approaches, including textualism, legislative intent, social purpose, and public policy); Jeffrey W. Stempel, *The Rehnquist Court, Inertial Burdens, and a Misleading Theory of Democracy*, 22 U. TOL. L. REV. 583, 588 (1991) (summarizing schools of statutory interpretation).

<sup>81</sup> The text-context dichotomy is not my original organizing description of judicial activity. See James M. Fischer, *Why Are Insurance Contracts Subject to Special Rules of Interpretation?: Text Versus Context*, 24 ARIZ. ST. L.J. 995 (1992).

pre-cellular phone world of 1951, this was a complete impossibility not only for Sadie Bernstein but for any airline passenger of the time.

But despite eschewing any consideration of most of the context of the insurance transaction, the *Lachs* dissent is willing to range far and wide in American society to find evidence that the lay public should know what an insurer means when referring to scheduled and nonscheduled airlines. The dissent invokes such authoritative chronicles of the American condition as *Fortune*, *Harper's*, *Time*, and *Cosmopolitan* magazines (presumably in an era when cleavage was less central to the *Cosmo* cover).<sup>82</sup> The dissent's inconsistency is a little startling: it is willing to scan popular periodicals for any use of the terms scheduled and non-scheduled but is unwilling to consider that the insurer had of its own volition placed the policyholder in a position where she simply could not read the policy, reflect on its consequences, and (perhaps) come to the same understanding as the insurer. Nor did the insurer bother to define the term.

Worse yet, the dissent refuses to consider issues of risk involved in the context of the transaction. The airline insurance policy's limitation of coverage to scheduled flights is a proxy for the airline's desire to avoid covering passengers riding on smaller planes operated by less experienced pilots and airlines. But decedent Sadie Bernstein appears to have been flying on an aircraft that was something more than a puddle-jumper. By contrast, policyholder-decedent George Steven, of *Steven v. Fidelity & Casualty Co. of New York*,<sup>83</sup> arguably the leading case in the area finding coverage for the insured, was clearly catching a ride on just such a "nonscheduled" flight when he found himself stranded in the Terre Haute, Indiana airport en route to Chicago.<sup>84</sup> The *Steven* Court applied much of the approach of *Lachs* in finding for the beneficiary and the cases are usually classified together. But the *Lachs* facts appear to present a more compelling case for coverage.

Finally, at the risk of sounding like Robin Hood or Karl Marx, I cannot resist criticizing the dissent for failing to appreciate what is at stake in *Lachs*. *Lachs* is not a battle for the future of contract consistency. It is a case about a single policyholder on a single flight with one beneficiary of a modest \$25,000 policy. Finding for the beneficiary, as the majority does, will hardly break the bank for this insurer or even make a dent in the insurance industry. The majority opinion gives the insurer a road map for the future if it wishes to avoid coverage in doubtful cases: make the limitations of the policy more conspicuous, both with clearer language and better placement; change the location of the vending machine; consider sales through agents who can check the flight in question and disclaim coverage if it is not a covered flight.

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<sup>82</sup> *Lachs v. Fid. & Cas. Co. of N.Y.*, 118 N.E.2d 555, 562-63 (N.Y. 1954). Perhaps more forceful is the dissent's citation of *Collier's Encyclopedia* 266-72, 279 (1949). See *id.* at 563. However, the *Collier's* entry hardly indicates that laypersons possess an understanding of a technical term that is, quite literally, "encyclopedic."

<sup>83</sup> 377 P.2d 284 (Cal. 1962).

<sup>84</sup> See *Id.* at 286-87. George Steven and several other stranded passengers negotiated a special flight with nonscheduled carrier Turner Aviation and were flying a small Piper Tri-Pacer airplane when the craft crashed, killing Steven. The *Steven* case has 233 Shepard's citing references as compared to the 138 citing references found for *Lachs* as of my LEXIS search of June 6, 2001.

Under the *Lachs* approach, the policyholder and her beneficiary are treated fairly but an insurer that wishes to continue to sell the flight insurance product can, with a few modifications, continue to sell the product and limit its risk quite handily. For example, in *Mutual of Omaha Insurance Co. v. Russell*,<sup>85</sup> which is often cited as the antithesis of *Lachs*, the insurance policy in question was considerably clearer, it provided coverage only for a set period of time and this was known to the policyholder at the time of purchase.<sup>86</sup> When her departure was delayed by hours and the *Russell* court ruled that her death was outside coverage, this may have been tragic but it was not the result of an unclear and obscure provision of the type at issue in *Lachs*. Consequently, although *Lachs* and *Russell* reflect different receptiveness to empathy for the beneficiary and nontextual means of contract construction, the cases are quite reconcilable.

*Lachs* may be more pro-policyholder than insurers would prefer, but it is hardly a left-wing stab at the heart of the sanctity of contract text. Rather, *Lachs* stands as a good example of an understated, comprehensive, eclectic approach to insurance coverage. Without becoming theologically zealous in favor of any single approach or factor, it is an exercise in practical reason that produces a most defensible opinion.<sup>87</sup> At the time *Lachs* was decided, the world of contracts jurisprudence (and by implication the world of insurance jurisprudence) was aligned according to the Williston/formalism-vs-Corbin/realism and instrumentalism debate.

Despite the passage of time and dramatic changes in society and the law, the same divide continues to animate insurance coverage disputes as reflected in the different decisions regarding the qualified pollution exclusion, the absolute pollution exclusion, administrative cleanup response costs, the insured-vs-insured exclusion in D & O policies, coverage of “experimental” medical treatment, business risk exclusions, and a variety of other contemporary disputes. Airline flight insurance and vending machines may have receded from the legal consciousness, but the *Lachs* holding and method continues to hold persuasive force.

How persuasive was the comprehensive approach of *Lachs*? And what are the implications for this continuing tension of insurance and contract law? Recall that *Lachs* was a 4-3 decision, with the celebrated Judge Stanley Fuld in dissent<sup>88</sup> to the lesser known Judge Albert Conway’s majority opinion.<sup>89</sup>

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<sup>85</sup> 402 F.2d 339 (10th Cir. 1968) (applying Kansas law).

<sup>86</sup> See *id.* at 341-42.

<sup>87</sup> See ESKRIDGE & FRICKEY, *supra* note 80, at 604-06 (reviewing scholarship on practical reason and statutory interpretation); William N. Eskridge, Jr. & Philip P. Frickey, *Statutory Interpretation as Practical Reason*, 42 STAN. L. REV. 321 (1992).

<sup>88</sup> Fuld was one of the most prestigious judges in the history of the Court of Appeals and was viewed as a mid-century Cardozo by many. See Symposium, 71 COLUM. L. REV. 531 (1971) (collection of articles praising Fuld, with issue of *Law Review* dedicated to Fuld in recognition of twenty-five years of “distinguished service.”). See, e.g., John M. Harlan, *Chief Judge Fuld: A Salute from Washington*, 71 COLUM. L. REV. 535 (Justice Harlan lauds Judge Fuld); Thomas E. Dewey, *The Making of a Judge*, 71 COLUM. L. REV. 537 (1971) (former New York Governor and presidential candidate praises Fuld as “born to judge”; Fuld had been an assistant to Dewey when Dewey emerged on the public and political scene as a crusading prosecutor); Michael I. Sovern, *Chief Judge Stanley H. Fuld*, 71 COLUM. L. REV.



Across the history of the case, the pro-coverage position has more, if perhaps less prominent, adherents. The trial judge found for the beneficiary<sup>90</sup> as did the intermediate appellate court, by a 4-1 margin.<sup>91</sup> The final tally of judicial view on *Lachs*, then, is a rather resounding 9-4, suggesting substantial judicial support for the eclectic, comprehensive approach to policy construction.

The small sample of "scheduled airlines" vending machine insurance cases does, however, illustrate the overall close division of judges and the legal profession on these matters. The California trial judge in *Steven v. Fidelity & Casualty* found the scheduled airlines language clear and ruled that there was no coverage for the policyholder.<sup>92</sup> The California Supreme Court famously reversed in a 5-2 vote, with its most famous member, former University of California law professor Roger Traynor, generally viewed as a contracts "liberal" and intellectual of the law, in dissent.<sup>93</sup> On petition for rehearing, the vote

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545 (1971) (Dean of Columbia Law School lauds Fuld as "whiz kid" who has "analytical power and decisional influence in a wide range of substantive and procedural fields" noting that "comparison with Cardozo is inevitable"). Fuld's legacy was further burnished by the success of his former law clerks, who included Jack B. Weinstein, now a celebrated federal district judge, Maurice Rosenberg, who became a prominent Columbia Law School professor (as was Weinstein prior to being appointed to the bench), and Kenneth R. Feinberg, a nationally known expert on mass torts and dispute resolution, recently appointed as Special Master administering the United States Government compensation fund for September 11<sup>th</sup> victims. All three wrote tributes to Fuld in the *Columbia Law Review* symposium issue on Fuld.

<sup>89</sup> By contrast to Fuld, Conway was a respected but hardly celebrated judge and was regarded as a politician and public servant more than as an intellectual. *See, e.g., Judge Albert Conway, 80, Dead; Headed State Court of Appeals*, N.Y. TIMES, May 19, 1969, at B20 (obituary of Conway notes judicial and government service, emphasizing that he was a "protege of John H. McCooey, the Brooklyn Democratic leader, and of Franklin D. Roosevelt."). Conway appears not to have been the subject of any sustained law review or other scholarly commentary as was Fuld. On the day of Conway's obituary, the death of Marion Morehouse Cummings, third wife of poet E.E. Cummings (and also, to be fair, a prominent fashion model and accomplished photographer), was noted with an obituary that was just as prominent and nearly as long as that of Conway. *See Marion Morehouse Cummings, Poet's Widow, Top Model, Dies*, N.Y. TIMES, May 19, 1969, at B20.

<sup>90</sup> *See Lachs v. Fid. & Cas. Co. of N.Y.*, 121 N.Y.S.2d 230, 232 (App. Div. 1953) (trial court ruled that flight insurance policy language regarding civilian scheduled airlines was sufficiently ambiguous to trigger contra proferentem principle and decision in favor of beneficiary).

<sup>91</sup> *See id.* (per curiam opinion affirming trial court is supported by Justices Glennon, Dore, Van Voorhis, and Bergan with Justice Peck in dissent). Justice Peck viewed the term "scheduled airline" as clear and was "unable to see that any further development of the facts at trial that could lead to any conclusion other than that the policy in question did not cover the flight in question." *See id.* Unlike the Court of Appeals dissent, the Peck dissent does not invoke *Cosmopolitan* or other popular periodicals to make its case of linguistic meaning.

<sup>92</sup> *See Steven v. Fid. & Cas. Co. of N.Y.*, 377 P.2d 284 (Cal. 1962) (noting trial court decision, from which insurance company sought Supreme Court review by petition).

<sup>93</sup> *See id.* at 298. *See also* Stewart Macauley, *Justice Traynor and the Law of Contracts*, 13 STAN. L. REV. 812 (1961) (praising Traynor and discussing his contract law opinions at length, finding most of them comprehensive and progressive in approach). Noting to any degree the articles celebrating Traynor's jurisprudence would be even more space-consuming than mentioning those lauding New York Court of Appeals Judge Fuld. *See supra* note 89, regarding Fuld.

was 4-3.<sup>94</sup> In the 1950s and 1960s, as today, there appears to be a judicial preference for contextual contract construction, but it may be a fragile majority rule.

Interestingly, the anti-coverage position in *Lachs* and *Steven* was championed by two of the most famous state supreme court jurists of the twentieth century Stanley Fuld and Roger Traynor. One must be careful about reading too much into this but I cannot help but think that this is more than coincidence. Law historically has celebrated not only text but the presumed value of text in fostering the legal values of certainty, predictability, efficiency, and private, market-based arrangements. Law has also historically celebrated hard-headedness in legal analysis, the notion that courts write to make systemic rules at least as much as to decide individual cases. Reverence for these goals of the system can lead even the best judges to overstate the clarity of text or the primacy of text in comparison to other factors surrounding a contract. In my view, both Fuld and Traynor made this mistake in adopting the anti-coverage position under the circumstances of *Lachs* and *Steven*.

By contrast, the far less famous Conway rendered in *Lachs* an opinion that may not have fit the linear mode of neoclassical contract theory but made both a good decision in the case at hand and rendered good law for the future in its more comprehensive examination of the insurance policy at issue. The lack of syllogistic precision in *Lachs* may make it seem unimpressively result oriented to some. I see it as a strength. *Steven* has similar strengths but reads more as a public policy manifesto and can be faulted by legal purists on these grounds.<sup>95</sup>

#### IV. CONCLUSION: SPEAKING PROSE ALL ALONG

Without appropriate nomenclature, it is difficult if not impossible to even discuss matters with care and accuracy. Consider the not uncommon problem of two native speakers of different languages attempting to communicate. Even when each has been taught the other's language, communication breaks down if both languages do not have words for the same concept. For example, German has two words for the English word "law," "gesetz" (the written code of positive law) and "recht" (the law of fairness or what Anglophones call justice). The American speaking German may miscommunicate if he simply substitutes "gesetz" for "law" in all her translations. If the correct term is used, better focus on the concept follows as a matter of course.<sup>96</sup>

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<sup>94</sup> See *Steven*, 377 P.2d at 298 (noting subsequent history) (Justices Traynor, Schauer, and McComb indicated they supported the rehearing petition).

<sup>95</sup> *Steven* also undermines to some extent the mini-thesis of this paragraph: that smart judges can be overly beguiled by the false gods of textual meaning and contract certainty while judges perhaps wrongly regarded as less cerebral may often render better opinions by being less imprisoned by the traditional dictates as to what constitutes sound legal analysis. *Steven* was authored by Justice Matthew Tobriner, a prestigious jurist, but one regarded as something of an ultra-liberal, perhaps because he so strongly invoked public policy in his opinions, arguably elevating it over contract groundrules and other legal doctrine.

<sup>96</sup> See George P. Fletcher, *Two Modes of Legal Thought*, 90 YALE L.J. 970, 980 (1981) (using Gesetz-Recht analogy to illustrate similar point regarding law generally and legal scholarship in particular). See also George P. Fletcher, *The Right and the Reasonable*, 98 HARV. L. REV. 949 (1985) (continuing exploration on this topic).

So it is with insurance coverage. A full explanation of a court's analysis and holding proves difficult when the language of the decision is insufficiently appreciative of the court's approach. *Lachs* at first blush reads as though it is primarily an ambiguity-based opinion or perhaps one unduly influenced by judicial sympathy. With hindsight, some commentators have seen it as a reasonable expectations opinion handed down before the concept was fully defined. But both characterizations do not fully and fairly explain the decision. *Lachs* is an eclectic and comprehensive opinion, one that considered with care the facial language of the policy, the context of the transaction, the purpose of the insurance policy, and the jurisprudential tides pulling in different directions for insurer and policyholder. In a way, *Lachs* is not so much a reasonable expectations opinion prior to the "birth" of the doctrine as it is a post-modern opinion before post-modernism was consciously recognized.<sup>97</sup> *Lachs* is an example of pragmatism and practical reason before these terms were common features of legal scholarship. If one had to label *Lachs*, one should probably call it pragmatic, comprehensively analytical, contextual, or holistic rather than trying to pigeonhole it as a case of ambiguity, reasonable expectations, or some other school of thought.

One should, however, acknowledge that *Lachs* was decided during something of a quieter era of insurance coverage disputes. *Lachs* itself involved only one policy and one insured life, it was not the tip of a mass tort or insurance iceberg as were the cases triggering asbestos coverage. The fate of no industry hung in the balance and the court of appeals was refreshingly free of such pressure. The past twenty years have seen an explosion of insurance law scholarship, but much of it is the work of high-powered practitioners who specialize in representing one side or the other in high stakes cases. As a result, insurance law scholarship can be "cacophonous" (to borrow Judge Posner's description of statutory interpretation writing),<sup>98</sup> as can the holdings of state courts, which have been diametrically opposed on some of the leading insurance questions of the modern era.<sup>99</sup> Although *Lachs* was of course affected by

<sup>97</sup> See Peter Schanck, *Understanding Postmodern Thought and Its Implications for Statutory Interpretation*, 65 S. CAL. L. REV. 2505 (1992) (suggesting that acceptance of some postmodern precepts, such as social construction of knowledge, auger in favor of less foundationalist and more comprehensive approaches to statutory interpretation).

<sup>98</sup> See Richard A. Posner, *Legislation and Its Interpretation: A Primer*, 68 NEB. L. REV. 431, 434 (1989). See, e.g., STEMPER, *supra* note 4; BARRY R. OSTRAGER & THOMAS R. NEWMAN, *HANDBOOK OF INSURANCE CONTRACT DISPUTES* (10th ed. 2000); Peter Nash Swisher, *A Realistic Consensus Approach to the Insurance Law Doctrine of Reasonable Expectations*, 35 TORT & INS. L.J. 729 (2000); Symposium, *The Reasonable Expectations Doctrine After Three Decades*, 5 CONN. INS. L.J. 1 (1998-99); Kenneth S. Abraham, *A Theory of Insurance Policy Interpretation*, 95 MICH. L. REV. 531 (1996); Peter Nash Swisher, *Judicial Interpretation of Insurance Contract Disputes: Toward a Realistic Middle Ground Approach*, 57 OHIO ST. L.J. 543 (1996); Michael B. Rappaport, *The Ambiguity Rule and Insurance Law: Why Insurance Contracts Should Not Be Construed Against the Drafter*, 30 GA. L. REV. 171 (1995); James M. Fischer, *Why Are Insurance Contracts Subject to Special Rules of Interpretation?: Text Versus Context*, 24 ARIZ. ST. L.J. 995 (1992); Peter Nash Swisher, *Judicial Rationales in Insurance Law: Dusting Of the Formal for the Function*, 52 OHIO ST. L.J. (1991); Stephen J. Ware, Note, *A Critique of the Reasonable Expectations Doctrine*, 56 U. CHI. L. REV. 1461 (1989).

<sup>99</sup> See STEMPER, *supra* note 4, especially §§ 14.11-14.12 (noting sharp and relatively equal division of states concerning pollution exclusions and coverage for pollution cleanup costs).

the longstanding text/formalism-vs-context/functionalism dichotomy in the law, *Lachs* was undisturbed by these as yet unfelt currents of higher stakes, high theory insurance mega-disputes. As a result, it may have been better able to render a more comprehensive decision even though the opinion lacked the terminology to fully describe what it had done.

*Lachs* demonstrates the degree to which the best judging is broad based and sensitive to facts, fairness, and public policy. It also reflects the degree to which good judicial opinions do not always self-consciously set forth their niche in jurisprudential thought. Optimal insurance policy construction like that in *Lachs* also reflects an appropriate humility as to the certainty of the meaning of words. In short, *Lachs* is something of an underappreciated jewel, one that perhaps should be displayed more often and more prominently to illuminate modern judicial inquiry into the meaning of insurance policies and other contracts.