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Chapman Law Review

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Editor's Note

It is my honor to introduce *Chapman Law Review*'s first Issue of Volume Twenty-Four. This Issue is the first of two general law review Issues in this year's Volume and publishes scholarship with a wide array of topics that span many legal areas.

Professor Denis Binder opens this Issue with an Article analyzing the cases that form the foundation of modern American environmental law and protection. In his Article, Professor Binder bases his analysis of those cases on five decades in environmental law, using historical perspective to look at the environmental, procedural, and substantive impacts and significance of the case decisions.

Next in this Issue is Mr. Daniel P. Schley, CFA's Article, which reconsiders whether corporate shareholders would benefit from the application of tort law principles to a limited shareholder liability analysis. In this Article, Mr. Schley argues that tort law would address limited shareholder liability under a negligence and not a strict liability regime, and that a negligence regime would produce results similar to those produced under the current corporate law framework. Mr. Schley finds that tort law, like corporate law, would uphold limited shareholder liability.

Professor Joshua M. Silverstein's Article follows and explores the area of contract interpretation. In his Article, Professor Silverstein aims to clarify various legal concepts and principles that play a critical role in interpreting case law and secondary literature. By untying some of the knots that entangle contract interpretation and the parol evidence rule, Professor Silverstein hopes his Article will aid in addressing interpretive issues in the contexts of adjudication, contract drafting, scholarship, and teaching.

Mr. Carl C. Jones wrote the following Comment in this Issue. Mr. Jones graduated from Chapman University Fowler School of Law in 2021 and has served on the *Chapman Law Review* as a dedicated Staff Editor, Executive Board member, and Senior Articles Editor. His work and contribution to the *Chapman Law Review* were invaluable in the publication of this Volume. Mr. Jones' article seeks to coherently summarize the broad cultural and legal conversations about loot boxes in the United States video game industry. His

Comment argues that existing case and statutory law are sufficient for a court to conclude that loot boxes can have value and are legally equivalent to gambling.

This Issue ends with a Comment by Mr. Ashton E. Stine, another graduate of Chapman University Dale E. Fowler School of Law class of 2021, and *Chapman Law Review* member. Mr. Stine served as a Staff Editor and Executive Board member of the *Chapman Law Review*. In his last year of law school, Mr. Stine held the critical position of Production Editor and, in that capacity, was instrumental in the production and publication of this Volume. Mr. Stine's Comment discusses the background and purpose of collective bargaining in American professional sports, the consequences of collective bargaining failure, and the results of player dissatisfaction. His Comment describes the interconnected relationship between antitrust law and labor law in sports and details a current problem in the collective bargaining agreements of the NFL and the NHL.

This past year, as we experienced a challenging time both because of the restrictions and effects of COVID-19 and the tumultuous political and social climate, the *Chapman Law Review* triumphed. We would not have been able to do so without the continued support of the members of the administration and faculty that made the publication of this Issue possible, including: Dean of Chapman University Dale E. Fowler School of Law, Matthew Parlow; our faculty advisor, Professor Celestine Richards McConville; and our faculty advisory committee members, Professor Deepa Badrinarayana, Professor Ernesto Hernandez, Professor Kenneth Stahl, Professor Richard Redding, and Professor Lan Cao. A special thank you goes to the Research Librarians of the Hugh & Hazel Darling Law Library for their tireless work for the *Chapman Law Review*.

I want to express my sincerest gratitude to the incredible students who served as the Executive Board members of the *Chapman Law Review*—without your countless hours of work, adaptability, and perseverance, this Volume would not have been possible. It has been such a pleasure and honor working alongside you. Last but certainly not least, I thank the staff of the 2020–2021 *Chapman Law Review*. Your remarkable, committed, and tireless work was paramount to the publication of this Volume. I feel truly honored and privileged to have been part of this journal and been allowed to serve and lead the *Chapman Law Review* this past year.

Sirine Maria Yared
Editor-in-Chief

The Pillars of Modern American Environmental Law

*Denis Binder**

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* Professor of Law, Dale E. Fowler School of Law, Chapman University, A.B. 1967, J.D. 1970, University of San Francisco, LL.M. 1971, S.J.D. 1973, University of Michigan. This Article is the fourth in a personal series of the history of environmental law. *See* Denis Binder, *Perspectives on Forty Years of Environmental Law*, 3 GEO. WASH. J. ENERGY & ENV'T L. 143 (2012); Denis Binder, *Looking Back to the Future: The Curmudgeon's Guide to the Future of Environmental Law*, 46 AKRON L. REV. 993 (2013); Denis Binder, *NEPA at 50: Standing Tall*, 23 CHAP. L. REV. 1 (2020). I spent two years at the University of Michigan taking every course offered by Professor Joseph Sax to whom I am deeply indebted. My thanks to Sherry Leysen, Heather Joy, and Tamara Carson, wonderful librarians at the Law School, and David Arburn, my research assistant. My special thanks to Professor J. K. Ruhr for his incisive comments.

I. INTRODUCTION

January 1, 1970 marks the unofficial start of the Environmental Age. The National Environmental Policy Act (NEPA) became effective at 12:01 AM on January 1.[1] The Council on Environmental Quality (CEQ) and the Environmental Protection Agency (EPA) came into being in 1970 while the inaugural Earth Day was April 22, 1970.[2] The paradigm switched from resource exploitation to resource conservation. Several environmental protection statutes were enacted at this time.[3]

America's economy for roughly a decade and a half, from the onset of the Great Depression in 1929 through the end of World War II in 1945, stagnated. Economic expansion was stalled, unemployment soared, and consumer expenditures depressed. Peace unleashed a period of sustained economic growth and development. Pent-up demand was released like a pressure cooker. The United States emerged from the war, unlike the rest of the world, with a vibrant, undamaged industrial base, which could switch to consumer goods from war production.

Detroit built large, popular, gas-guzzling cars as conspicuous consumption became the norm. Consumers purchased homes, cars, and appliances.[4] Higher education ballooned. Downtowns boomed. A college degree was almost a guarantee of meaningful employment. America built up its infrastructure: airports, highways, bridges, dams and channels, power plants, transmission lines, and pipelines. Congress enacted the National Interstate and Defense Highways Act of 1956.[5] A frenzy ensued to build the roughly 41,000 miles of the interstate highway system; the creation of the nation's highways fueled the move to the booming suburbs. The dawn of the environmental era marked the end of highway building, especially through cities.

Progress was the credo. A country which could place a man on the moon was seemingly capable of anything, but apparently not protecting the environment. Emphasis was on the quantity of

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1 National Environmental Policy Act of 1969, Pub. L. No. 91-190, 83 Stat. 852.

2 *Environmental History Timeline*, ENV'T HIST. TIMELINE, http://environmentalhistory.org/20th-century/seventies-1970-79/ [http://perma.cc/W8WN-3EXM] (last visited Mar. 3, 2021).

3 Richard J. Lazarus, *The Greening of America and the Graying of United States Environmental Law*, 20 VA. ENV'T L.J. 75, 77–79 (2001).

4 Lizabeth Cohen, *A Consumers' Republic: The Politics of Mass Consumption in Postwar America*, 31 J. CONSUMER RSCH. 236, 237.

5 Federal-Aid Highway Act of 1956, Ch. 462, 70 Stat. 374 (codified as amended in scattered statutes in 23 U.S.C. and 26 U.S.C.).

life–not the quality of life.

The preceding seven decades represented the Conservation Era. The theme of the century old City Beautiful[6] and Conservation Movements continued into the earlier 1960s with enactment of the National Historic Preservation Act,[7] Wilderness Act,[8] and the Wild and Scenic Rivers Act,[9] all conservation measures.

The ethos of the Conservation Era was to preserve and conserve that which was there. The ethos of the Environmental Era is to both conserve and preserve, but more significantly to clean up, bring back, and restore.

The environment was lost in the quest for economic expansion. Four events alerted the public to the degradation of the environment. The first was Rachel Carson's epic *Silent Spring*,[10] published in 1962, focusing national attention on the risks of toxic chemicals. The second was the Santa Barbara Oil Blowout of January 28, 1969.[11] The national coverage coupled with photos of oil covered sea birds was riveting.[12] The third was the growing smog problem, especially in Los Angeles.[13] Finally was the Cuyahoga River catching on fire as it flowed through Cleveland on June 22, 1969.[14]

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6 The City Beautiful Movement championed building parks, including pocket parks, in the nation's cities and other forms of beautifying the cities of the day. *See* WILLIAM WYCKOFF, HOW TO READ THE AMERICAN WEST 296–97 (2014). Frederick Law Olmstead designed many of the great gardens and open spaces of modern America. *See* JUSTIN MARTIN, GENIUS OF PLACE: THE LIFE OF FREDERICK LAW OLMSTEAD 1–2 (2011).

7 Act of Oct. 15, 1966, Pub. L. No. 89-665, 80 Stat. 915 (codified at 16 U.S.C. §§ 470x–470x-6; renumbered as scattered statutes in 54 U.S.C.).

8 Wilderness Act of 1964, Pub. L. No. 88-577, 78 Stat. 890 (codified as amended at 16 U.S.C. §§ 1131–1136).

9 Wild and Scenic Rivers Act of 1968, Pub. L. No. 90-542, 82 Stat. 906 (1968) (providing for a National Wild and Scenic Rivers System) (codified as amended at 16 U.S.C. §§ 1271–1287).

10 RACHEL CARSON, SILENT SPRING (1962). The impact of Rachel Carson is the focus of *American Experience: Rachel Carson* (PBS television broadcast Jan. 24, 2017).

11 *See* Harry Trimborn, *Battle Shaping Up Over Offshore Oil*, L.A. TIMES, Feb. 2, 1969, at A1.

12 The Santa Barbara Oil Blowout was a seminal moment in American environmental law. It led to enactment of the Coastal Zone Management Act of 1972, Pub. L. No. 92-583, 86 Stat. 1280 (1972) (codified at 16 U.S.C. §§ 1451–1666), and the Ports and Waterways Safety Act of 1972, Pub. L. No. 92-340, 86 Stat. 424 (1972) (codified at 33 U.S.C. §§ 1221–1236). Union Oil Co. v. Oppen, 501 F.2d 558 (9th Cir. 1974) was the only major case arising out of the blowout. It opened up civil liability in oil spill cases.

13 *See* Gene Sherman, *Where We Stand on Smog Problem, What's Been Done, What's Ahead*, L.A. TIMES, Jan. 8, 1961, at C1. I. I remember flying through Los Angeles International Airport around two o'clock in the afternoon in the mid-1970's and seeing what appeared to be a beautiful sunset. The orange glow was, of course, smog.

14 *See The Cities: The Price of Optimism*, TIME, Aug. 1, 1969, at 41. Check out Randy Newman's classic "Burn On." RANDY NEWMAN, *Burn On*, *on* Sail Away (Reprise Records 1972).

The vast majority of public environmental law is administrative law.[15] Consequently, many of the landmark environmental cases involve administrative law issues. The threshold issues at the onset of the Environmental Era were standing, reviewability, and agency discretion—beginning with standing for access to the courts. The presumption was that the administrative agencies were charged with protecting and promoting the public interest so that their decisions should not be questioned by the public they were sworn to protect.

This Article analyzes the cases that form the foundation of modern American environmental law and protection. Professors J. B. Ruhl and Jim Salzman provide a valuable study of environmental law cases by surveying environmental professionals in 2001, 2009, and 2019 to select the top ten environmental cases. They found four constant cases in the top ten,[16] while two others appear in the newer surveys.[17]

My approach is more subjective. It is based on five decades in environmental law looking at environmental protection from a historical perspective of the environmental, procedural, and substantive impacts and significance of the decisions. These cases are selected either for their legal significance or contributions to environmental improvement. Other professors and professionals could easily choose different cases because scores of significant environmental cases have been decided.[18]

II. THE PRECURSOR CASES

The Environmental Era did not suddenly pop up. Three infrastructure cases developing in the late 1960s continuing into the 1970s provided strong signals that the times "were a changing."[19]

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15 Private compensatory remedies are usually taught in a Toxic Torts course.

16 J. B. Ruhl & Jim Salzman, *American Idols*, ENV'T F., May–June 2019, at 40. The four perennial cases are *Chevron, U.S.A. v. Nat. Res. Def. Council, Inc.*, 467 U.S. 837 (1984), *Tenn. Valley Auth. v. Hill*, 437 U.S. 153 (1978), *Sierra Club v. Morton*, 405 U.S. 727 (1972), and *Citizens to Pres. Overton Park, Inc. v. Volpe*, 401 U.S. 402 (1971). *Id.* at 43. Professor Lazarus has also written on the history of environmental law. RICHARD J. LAZARUS, THE MAKING OF ENVIRONMENTAL LAW (2004).

17 Ruhl & Salzman, *supra note* 16, at 43. *See* Massachusetts v. EPA, 549 U.S. 497 (2007); *see also* Lujan v. Defs. of Wildlife, 504 U.S. 555 (1992).

18 I have not included any of the myriad of wetlands cases because no clear constitutional standards have yet arisen.

19 *Cf.* BOB DYLAN, *The Times They Are-a-Changin'*, *on* THE TIMES THEY ARE-A-CHANGIN' (Columbia Records 1964).

A. *Scenic Hudson Preservation Conference v. Federal Power Commission*[20]

The East Coast suffered a massive electrical blackout on November 9, 1965. It was a cascading power failure up and down the East Coast and Ontario. The Great Northeast Blackout of 1965 resulted in over thirty million people losing power. The proposed solution was to have standby electrical sources that could immediately power up. One way to accomplish that goal was the construction of pumped storage facilities. Water would be pumped up to a hilltop reservoir during slack times, such as nighttime. It would then flow down during peak or emergency times.[21] A 1,168-megawatt pumped storage facility was erected at Northfield Mountain in Massachusetts. A second one was planned in 1962 for Storm King Mountain on the Hudson River fifty miles north of New York City. Storm King was announced three years before the Blackout, but the promoters used the Blackout to justify the plant's construction. The intake and outflow sites were planned in the prime spawning grounds of the Atlantic striped bass.

The Federal Power Commission (FPC) issued a permit for the facility. The Second Circuit overturned the license for failure to consider alternatives, such as interconnects, gas turbines, nuclear power, underground transmission lines, or a combination of them.[22] It criticized the agency for acting as an "umpire blandly calling balls and strikes" rather than affirmatively protecting the public interest.[23] The right of the public "must receive active and affirmative protection at the hands of the Commission."[24] The D.C. Circuit recognized that standing can be based on "aesthetic, conservational, and recreational" injuries.[25]

The FPC's decision on remand said:

> Just as the mountain has swallowed the scar of the highway, the intrusive railroad structure and fills, and tolerates both the barges and scows which pass by it and the thoughtless humans who visit it without seeing it, so it will swallow the structures which will serve the needs of people for electric power.[26]

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20 Scenic Hudson Pres. Conf. v. Fed. Power Comm'n, 354 F.2d 608 (2d Cir. 1965).

21 Pumped storage facilities are technically energy inefficient since pumped storage requires about two kilowatt hours of electricity in exchange for one kilowatt hour generated in the discharge. The value is in the timing.

22 *Scenic Hudson*, 354 F.2d at 621–23.

23 *Id.* at 620.

24 *Id.*

25 *Id.* at 616. The court also extended standing to those whose activities and conduct show a "special interest" in the area. *Id.*

26 Consol. Edison Co. of N.Y., Inc., 44 F.P.C. 350, 384 (1970), *aff'd sub nom.* Scenic

The FPC's Chairman Nassikas stated "I'm a conservationist too," but recognized the agency's first mission is to encourage "an abundant supply of electric energy throughout the United States."[27]

Extensive agency proceedings and litigation ensued. The proposal was dropped in 1980. The pump storage facility was never built.[28] Ironically, the Storm King Mountain proposal was announced on September 27, 1962—the same day Rachel Carson's *Silent Spring* was published.[29]

A subsequent casualty of the Storm King litigation was the Westway Highway project. A section of Manhattan's Westside Highway collapsed. The proposal was to replace it by filling in 242 acres, of which 31 acres would be for interchange ramps, 110 acres for new development, and 93 for a recreational park. Half the new road would be underground. Westway was enjoined because of the failure to deal with the striped bass issue.[30]

B. The Cross Florida Barge Canal[31]

The Cross Florida Barge Canal, like the Ford Edsel, seemed a good idea at the time. The dream of a canal linking the Gulf Coast to the Atlantic harkens back to the early days of the Spanish exploration of Florida. The onset of World War II accelerated the apparent need for the Canal.[32] Congress authorized it in 1942. The Canal would cut through north central Florida from Jacksonville to the Gulf of Mexico—bifurcating the state. Construction began in 1964. Decisions remained to be made when NEPA came into effect on January 1, 1970. The canal was roughly "one-third complete and approximately $74 million

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Hudson Pres. Conf. v. Fed. Power Comm'n, 453 F.2d 463 (2d Cir. 1971). Simon & Garfunkel's *The Sound of Silence* "people hearing without listening" characterized the FPC decision. *See* SIMON & GARFUNKEL, *The Sound of Silence*, *on* WEDNESDAY MORNING, 3AM (Columbia Records 1964).

27 Edward Cowan, *Power: To Use Or Not To Use*, N.Y. TIMES, July 2, 1972, at F12.

28 The Storm King saga is the basis of ROBERT D. LIFSET, POWER ON THE HUDSON: STORM KING MOUNTAIN AND THE EMERGENCE OF MODERN AMERICAN ENVIRONMENTALISM (2014).

29 *Id.* at 5–6.

30 *See* Action for Rational Transit v. W. Side Highway Project, 536 F. Supp. 1225 (S.D.N.Y. 1982).

31 For a detailed history of the Cross Florida Canal, see STEVEN NOLL & DAVID TEGEDER, DITCH OF DREAMS: THE CROSS FLORIDA BARGE CANAL AND THE STRUGGLE FOR FLORIDA'S FUTURE (2009).

32 German U-Boats were torpedoing ships off the Florida coast after the United States entered World War II. *See* Ed Offley, *Germany Brought WWII to the Florida Coast in 1942*, LEDGER (June 23, 2019, 7:15 PM) http://www.theledger.com/news/20190623/germany-brought-wwii-to-florida-coast-in-1942 [http://perma.cc/PAD4-MXVL].

had been spent on land acquisition and construction"[33] when a court issued an injunction. The project's Rodman Dam was completed in 1968 on the Ocklawaha River. Thirteen thousand acres of partially cleared land in the Ocklawaha Valley were flooded. A total of 1,135 acres of large hardwood trees were left standing prior to the flooding to serve as fish habitat. The flooding was now progressively killing the trees.

The court followed the standard requirements for preliminary injunctive relief:

> (1) a substantial likelihood that plaintiff will prevail on the merits, (2) a substantial threat that plaintiff will suffer irreparable injury if the injunction is not granted, (3) that the threatened injury to plaintiff outweighs the threatened harm the injunction may do to defendant, and (4) that granting the preliminary injunction will not disserve the public interest.[34]

The background to the opinion is the understanding that President Nixon was going to scuttle the canal, which he did three days later on January 19, 1971.[35]

The court did not address an interesting issue in its short opinion. Preliminary relief is supposed to preserve the status quo pending the final trial on the merits.[36] The question is what is the status quo? Partially flooded trees? Draining the lake to preserve the trees? We know the answer; Rodman Dam still stands with the lake behind it.

Opposition to the canal was led by Marjorie Harris Carr. The cessation of construction left the state with a right of way up to a mile wide along the canal right of way. The path is named the Marjorie Harris Carr Cross Florida Greenway.

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33 GEOCACHING, *Marjorie Harris Carr Cross Florida Greenway* https://www.geocaching.com/geocache/GCN147_marjorie-harris-carr-cross-florida-greenway?guid=00b941a3-0676-40e4-9f75-0432db7a08c6 [http://perma.cc/5SCX-EM46] (last visited Mar. 7, 2021).

34 Canal Auth. of State of Fla. v. Callaway, 489 F.2d 567, 570, 572 (5th Cir. 1974).

35 *Stop Order from President Richard Nixon*, FLA. MEMORY, http://www.floridamemory.com/onlineclassroom/primarysourcesets/water/documents/nixon/ [http://perma.cc/AKY8-V62G]. The canal was formally deauthorized in 1990. Cross Florida Barge Canal, 16 U.S.C. § 460tt (2020).

36 *Callaway*, 489 F.2d at 576.

III. THE ADMINISTRATIVE FOUNDATIONS

A. Reviewability: *Citizens to Preserve Overton Park v. Volpe*[37]

The third case involved both a freeway siting through an urban park and the reviewability of agency action. *Sierra Club v. Morton* decided the fundamental issue of standing to get into federal court.[38] *Citizens to Preserve Overton Park v. Volpe* lays out the parameters for deciding the standards for reviewing administrative decisions once in court.[39]

The proposal was to build a six-lane highway through downtown Memphis slicing through Memphis' Overton Park.[40] The highway would sever the zoo from the park and destroy 26 acres of the 342 acre park.[41] The proposed extension of I-40 would cut directly through Memphis instead of rerouting drivers around the existing bypass.[42] The Federal Highway Administration (FHA) approved the route in 1966.[43]

No formal findings of fact accompanied the approval.[44] Congress enacted the Federal Transportation Act—section 4(f) prohibited the construction through parkland unless no "feasible and prudent" alternative existed, and even then, only if all possible methods for reducing harm to the park were taken.[45]

The plaintiffs alleged a violation of section 4(f) and the failure to provide formal findings.[46] The agency claimed it had discretion to approve the project.[47]

The Supreme Court held an agency's discretion should be measured within the context of the relevant statutes.[48] The Administrative Procedures Act (APA) normally applies in laying out the standards of review.[49] A presumption of reviewability exists under the APA.[50] An agency's discretion is unreviewable only if "there is a statutory prohibition on review or where

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37 Citizens to Pres. Overton Park, Inc. v. Volpe, 401 U.S. 402, 406–07 (1971).
38 *See* 405 U.S. 727 (1972).
39 401 U.S. 402, 406–07 (1971).
40 *Id.* at 406.
41 *Id.*
42 *Id.*
43 *Id.* at 407.
44 *Id.* at 408.
45 23 U.S.C. § 138 (2020).
46 *Citizens to Pres. Overton Park, Inc.*, 401 U.S. at 408–09.
47 *Id.* at 409.
48 *Id.* at 410.
49 *Id.*
50 *Id.*

'agency action is committed to agency discretion by law.'"[51] The Supreme Court held this exception applies only when "statutes are drawn in such broad terms that in a given case there is no law to apply."[52]

Section 4(f) provides specific restrictions on the FHA's discretion.[53] Therefore, there is law to be applied. The FHA failed to meet the 4(f) standards.[54]

The Court also explained the various standards of review. For example, the substantial evidence test applies when the agency action is undertaken pursuant to a rulemaking provision of the APA or when the agency action is based on a public adjudicatory hearing.[55] An agency decision should be set aside if the action is "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law or if the action failed to meet statutory, procedural, or constitutional requirements."[56]

The Court agreed no formal findings of fact were required,[57] but the Administrator had to provide justifications for the decision. Post hoc rationalizations should be critically reviewed.[58] The FHA subsequently amended its regulations to require formal findings of fact.

Overton Park had two major consequences. First, the Court substantially reined in agency's "unreviewable" discretion. Second, the practical result of Storm King Mountain, The Cross Florida Barge Canal, and Citizens to Preserve Overton Park is that infrastructure is no longer sacrosanct. The environmental laws apply to infrastructure projects. These cases also represented the change in paradigms from the "master builder"[59] to the environmentalist.

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51 *Citizens to Pres. Overton Park, Inc.*, 401 U.S. at 410 (citing 5 U.S.C. § 701).

52 *Id.* (citing S. Rep. No. 752, 79th Cong., 1st Sess., 26 (1945)).

53 *Id.* at 411.

54 *Id.* at 411–12.

55 *Id.* at 414.

56 *Id.* (internal quotations omitted).

57 *Id.* at 409.

58 *Id.* at 420. Post hoc rationalizations have traditionally been viewed as an "inadequate basis for review." *Id.* at 419.

59 Robert Moses is the penultimate master builder/master planner. He was in charge of planning and public works in both the city and state of New York. His legacy includes 13 bridges, 416 miles of parkways, 28,000 housing units, and 658 playgrounds in New York City. He turned tenements into public housing. His legacy includes the Triborough Bridge, Verrazano Narrows Bridge, Bronx-Whitestone Bridge, Throgs Neck Bridge, Brooklyn-Queens Expressway, Cross Bronx Expressway, Cross Bronx Expressway, Westside Highway, Van Wyck Expressway, Henry Hudson Parkway, Jones Beach, Lincoln Center, United Nations Headquarters, and Shea Stadium. *See generally* ROBERT A. CARO, THE POWER BROKER: ROBERT MOSES AND THE FALL OF NEW YORK (1974). Robert Moses was blocked when he tried to build the Lower Manhattan highway through Greenwich Village.

B. Standng: *Sierra Club v. Morton*[60]

A threshold standard of federal jurisdiction is that the plaintiff must have an injury, a sufficient stake in a justiciable controversy; in essence, to have suffered an injury recognized by federal law. Section 10 of the APA provides: "A person suffering legal wrong because of agency action, or adversely affected or aggrieved by agency action within the meaning of a relevant statute, is entitled to judicial review thereof."[61] An understanding existed prior to the environmental cases that standing entailed an economic injury. Professor Stone asked the question: "Should Trees Have Standing?"[62]

The Supreme Court in *Sierra Club v. Morton*[63] opened up the doors to non-economic standing. The Sierra Club opposed development of a Disney ski resort in Mineral King National Forest nestled in the Sierra Nevada Mountains. It claimed standing in a representative capacity "in the conservation and the sound maintenance of the national parks, game refuges and forests of the country . . . . One of the principal purposes of the Sierra Club is to protect and conserve the national resources of the Sierra Nevada Mountains."[64] It therefore sought standing based on an interest in the problem without a particularized injury in fact.[65]

The Court rejected this broad definition of injury for standing. However, the Court promulgated three critical holdings that opened up standing. First, the Court extended standing to aesthetic and environmental well-being.[66] The Court cited an earlier opinion, *Association of Data Processing Service Organizations, Inc. v. Camp*,[67] which stated an injured interest may reflect "'aesthetic, conservational, and recreational' as well

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60 *See generally* 405 U.S. 727 (1972).

61 5 U.S.C. § 702 (2020).

62 Christopher D. Stone, *Should Trees Have Standing: Toward Legal Rights for Natural Objects*, 45 S. CALIF. L. REV. 450, 450 (1972).

63 *Sierra Club*, 405 U.S. 727. Walt Disney supervised the pageantry at the 1960 Squaw Valley Winter Olympics in the Sierras, and decided he loved ski resorts. The Disney plan for the Mineral King Valley in Sequoia National Forest called for a $35 million complex of motels, restaurants, swimming pools, parking lots, and other structures to accommodate up to 14,000 visitors. Ironically, development of the area was originally supported by the Sierra Club.

64 *Sierra Club*, 405 U.S. at 734 n.8.

65 The Sierra Club pushed the case as a test case, pushing the boundaries of standing. It could have amended its case to show particularized standing, as it quickly did after the Supreme Court decision.

66 *Sierra Club*, 405 U.S. at 734.

67 *See generally* 397 U.S. 150 (1970).

as economic values."[68] Thus an economic injury was no longer a prerequisite for standing.

Second, standing can be extended to organizations in a representational capacity if an individual member satisfies the standing requirements.[69] Thus an environmental organization, NGO, or trade association can act on behalf of its members.[70] The practical significance is that these organizations often have the resources which individuals lack to litigate these problems.

Third, once standing is obtained, the claimant can assert the broader public interest and is not limited to the issue asserted for standing.[71] The successful claimant thereby assumes the role of a private attorney general.[72]

The answer to Professor Stone's question and Justice Douglas' concurring opinion is "Trees technically do not have standing." However, we know from other cases that inanimate objects can be named a plaintiff as long as a named individual or organization has standing. Only one plaintiff need have standing. Standing may be pushed or stretched after *Sierra Club v. Morton*,[73] but the core remains.

The case helped fuel the growth of environmental and public interest organizations on both sides.[74] The Sierra Club effectively won the case on standing, and the underlying environmental dispute. Representative Phil Burton (D. Ca.) crafted a "park barrel" bill modeled after the traditional park barrel legislation with government projects for members of Congress.[75]

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68 *Id.* at 154.

69 *Sierra Club*, 405 U.S. at 739.

70 *Id.*

71 *Id.* at 737.

72 *Id.*

73 *See, e.g.*, United States v. Students Challenging Regul. Agency Procs. (SCRAP), 412 U.S. 669, 687–88 (1973). An individual may have standing even if large numbers are similarly affected.

74 The Environmental Defense Fund was established earlier in 1965 and was soon followed by the Natural Resources Defense Council, the Earth Justice Foundation (formerly the Sierra Club Legal Defense Fund), the Conservation Law Foundation, and the Conservation Law Foundation of New England. The Sierra Club blossomed. Other established environmental organizations such as the National Audubon Society, the Wilderness Society, World Wildlife Federation, and the Izaak Walton League grew in membership. Defenders of Wildlife quickly emerged, while Greenpeace has been the most active internationally. The Nature Conservancy and Save the Redwoods League continued their policies of acquiring environmentally critical lands. Friends of the Earth sprang off from the Sierra Club. The National Parks Association renamed itself the National Parks Conservation Association. On the opposite side of the spectrum are organizations such as the Pacific Legal Foundation and the Mountain States Legal Foundation.

75 *See* Harold Gilliam, *Remembering Edgar Wayburn*, SIERRA (July–Aug. 2010),

Representative Burton invited Representatives to submit proposed additions to national parks, forests, marine sanctuaries, refuges, monuments, and seashores in their district.[76] He packaged them together in the Omnibus Parks Bill, signed by President Carter on November 10, 1978.[77] The Act transferred Mineral King to the National Park Service with a proviso banning downhill skiing in the area.[78]

The Johnson Administration in 1967 stripped the Sierra Club of its tax exemption because of its campaign against two proposed dams that would partly flood the Grand Canyon.[79] The tag line in the *New York Times* and *Washington Post* was "Should we also flood the Sistine Chapel so tourists can float nearer the ceiling?"[80] The IRS action ironically boosted the Club by turning it into an environmental martyr, rather than crushing it.[81]

C. Standing and Climate Change: *Massachusetts v. Environmental Protection Agency*[82]

The Supreme Court in a 1907 interstate pollution case held a state "in its capacity of quasi-sovereign" could sue for damages or abatement for interstate pollution.[83]

A century after *Georgia v. Tennessee Copper Co.* and forty-five years after *Sierra Club v. Morton,* the Court issued two significant holdings in *Massachusetts v. Environmental Protection Agency*.[84] First, it extended standing to Massachusetts, which has special standing as a state because of its "quasi-sovereign" status.[85]

The second holding has great importance in the current battle over climate change.[86] The Court held the EPA has jurisdiction under the Clean Air Act to regulate carbon dioxide

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http://www.sierraclub.org/sierra/201007/wayburn.aspx [http://perma.cc/2987-UF9J] (discussing the "park barrel" bills).

76 *See* STAFF OF SUBCOMM. ON NAT'L PARKS & INSULAR AFFS. OF THE H. COMM. ON INTERIOR & INSULAR AFFS., 95TH CONG., LEGISLATIVE HISTORY OF THE NATIONAL PARKS AND RECREATION ACT OF 1978 (1978) [http://perma.cc/JN2A-7YTB].

77 National Parks and Recreation Act of 1978, Pub. L. No. 95-625, § 314, 92 Stat. 3467.

78 *Id.*

79 *See* Bob Turner, *Sacrifice of a Natural Wonder America's Most Regretted Environmental Mistake*, TEHIPITE TOPICS, Winter 2017, at 11 [http://perma.cc/7TWY-SWSS].

80 *Id.*

81 The Sierra Club to this day eschews non-profit status.

82 *See generally* 549 U.S. 497 (2007).

83 Georgia v. Tenn. Copper Co., 206 U.S. 230, 236–37 (1907).

84 *See* 549 U.S. 497.

85 *See id.* at 520.

86 *See id.* at 525.

and other greenhouse gasses from auto exhausts and thus stationary sources, which include power plants, if found to endanger public health.[87] EPA thereby has the authority to impose substantial controls on greenhouse gas emissions from fixed sources—a major cause of global warming.

D. The *Chevron* Doctrine: *Chevron, U.S.A. v. Natural Resources Defense Council*[88]

Congress enacts statutes and creates agencies to implement the statutes.[89] The powers delegated to regulatory agencies are often extensive and the statutes vague.[90] Agencies thereby have to construe and apply the statutes through regulations and enforcement.[91] Courts have traditionally deferred to the expertise of the agencies in interpreting the statute.[92] A maxim of administrative law since the New Deal is that courts will defer to the discretion of administrative agencies, which possess the expertise which courts lack in the specific areas.[93]

Congress required permits for point sources of air pollution, but did not define point sources.[94] The narrow issue was whether a source could be viewed as a facility in its entirety or by individual components within the plant.[95] The agency's initial definition included any significant change or addition to a plant or facility, viewed as a single "bubble."[96] The definition was changed in 1981 with a new administration to a plant or factory in its entirety, such that if reductions elsewhere in the source resulted in no overall increase in emissions, then the polluter could avoid a "new-source" review.[97]

Chevron reformulated the doctrine with what is known as *Chevron* Deference.[98] First, the court should look to the intent of Congress: "If the intent of Congress is clear, that is the end of the matter; for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress."[99] The starting

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87 *See id.* at 528.
88 *See generally* 467 U.S. 837 (1984).
89 *See id.* at 843, 845.
90 *See id.* at 843.
91 *See id.* at 843–44.
92 *See id.* at 843.
93 *See id.*
94 *See id.* at 850–51.
95 *See id.* at 851.
96 *Id.*
97 *See id.* at 853.
98 *See generally id.*
99 *Id.* at 842–44 (finding that the agency's interpretation does not have to be the only

point should be the plain words of the statute.[100]

On the other hand, "if the statute is silent or ambiguous with respect to the specific issue, the question for the court is whether the agency's answer is based on a permissible construction of the statute."[101] Congress delegated authority to the agencies to fill gaps in the specific provisions of a statute.[102] A court is not to substitute its own construction of the statute for that of the agency.[103]

The *Chevron* holding became known as the *Chevron* two-step.[104] The first step is to determine if Congress "has directly spoken to the precise question at issue."[105] Then, the next step is to determine whether the agency made a permissible interpretation of the statute.[106] Agencies routinely argue *Chevron* protects their decisions even as to the extent of their jurisdiction, and usually succeed.

The *Chevron* Doctrine has become controversial in recent years as agencies stretch to justify their decisions.[107] They basically argue pursuant to *Chevron* that courts cannot second-guess their decisions—essentially going back to the years of non-reviewability before *Citizens to Preserve Overton Park v. Volpe*.[108]

IV. NEPA

The National Environmental Policy Act (NEPA), with its requirement of environmental impact statements on any major federal project significantly affecting the quality of the human environment, is one of America's greatest contributions to the global environment.[109] *Vermont Yankee* is not the first Supreme Court NEPA decision.[110] The Supreme Court's earlier decision in

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interpretation, but a reasonable construction).

100 *See id.*

101 *Id.* at 843.

102 *See id.* at 843–44.

103 *See id.* at 844.

104 *See* Valerie C. Brannon & Jared P. Cole, CONG. RSCH. SERV., R44954, CHEVRON *DEFERENCE*: *A PRIMER*, at 1–2 (2002).

105 *Id.* at 842.

106 *See id.* at 843–44. For a humorous look at the *Chevron* two-step by law students at NYU, see also Lewie Briggs, *The Chevron Two Step*, YOUTUBE (May 4, 2014), http://www.youtube.com/watch?v=uHKujqyktJc [http://perma.cc/6UT5-9ZJS].

107 *See, e.g.*, Eric Citron, *The Roots and Limits of Gorsuch's Views on Chevron Deference*, SCOTUSBLOG (Mar. 17, 2017, 11:26 AM), http://www.scotusblog.com/2017/03/roots-limits-gorsuchs-views-chevron-deference/ [http://perma.cc/9SJD-UKDH].

108 *See* Chevron, 467 U.S. 837; see also *Citizens to Pres. Overton Park, Inc.*, 401 U.S. 402.

109 The other is the creation of national parks.

110 435 U.S. 519 (1978).

Kleppe v. Sierra Club[111] held:

> 1) An EIS is not required until an agency has issued a report or recommendation on a major federal action;
>
> 2) The court's role is to ensure the agency took "a hard look" at the environmental consequences of a proposal, but not to substitute its judgment for that of the agency on the environmental consequences of the proposal; and
>
> 3) The only procedural requirements are those set forth in the plain words of the statute.[112]

Vermont Yankee[113] is a NEPA case involving two appeals by intervenors contesting the issuance of permits for the construction of nuclear power plants.[114] The Vermont Yankee half of the case involved the handling of nuclear waste.[115] The intervenors asserted that section 4 of the Administrative Procedure Act "merely establishes lower procedural bounds and that a court may routinely require more than the minimum when an agency's proposed rule addresses complex or technical factual issues or 'Issues of Great Public Import.'"[116]

The NRC's staff prepared a conclusory table to reflect the insignificant environmental effects of the fuel cycle.[117] The crux of the agency's substantive decision is that "the environmental effects of the uranium fuel cycle have been shown to be relatively insignificant . . . ."[118] The agency at the public hearing treated Dr. Frank Pittman, presenting the report, with great deference, whereas the intervenors were treated with open hostility.[119]

The D.C. Court of Appeals ordered the Atomic Energy Commission to adopt procedures for the intervenors.[120] The agency decided neither discovery nor cross examination would be

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111 *See* 427 U.S. 390 (1976).

112 *Id.* at 410 n.21 (citing Scenic Hudson Pres. Conf. v. Fed. Power Comm'n, 453 F.2d 463, 481 (2d Cir. 1971) and Nat. Res. Def. Council v. Morton, 458 F.2d 827, 838 (D.C. Cir. 1972)).

113 *See* Vt. Yankee Nuclear Power Corp. v. Nat. Res. Def. Council, Inc., 435 U.S. 519 (1978).

114 *Id.*

115 *See id.* at 538–39 (stating that the plan would produce over 100 pounds annually of radioactive waste, some of which would have to be isolated for 600 to hundreds of thousands of years).

116 *Id.* at 545.

117 *See id.* at 530.

118 *Id.* at 545.

119 *See generally id.*

120 *See* Nat. Res. Def. Council v. U.S. Nuclear Regul. Comm'n, 547 F.2d 633, 652–54 (D.C. Cir. 1976) (refraining from specifically requiring cross examination but implying it in the decision).

allowed.[121] Documents were made available to the intervenors, who would be given a reasonable time to present their arguments.[122]

The D.C. Court of Appeals was upset at the disparate treatment shown its staff versus the intervenors.[123] The court felt the agency's procedures were inadequate and ordered the case remanded, although it did not specify the procedures to be used on remand.[124]

The intervenors' premise was that "the problems involved are not merely technical, but involve basic philosophical issues concerning man's ability to make commitments which will require stable social structures for unprecedented periods."[125]

Judge Bazelon in his concurring opinion wrote:

> Decisions in areas touching the environment or medicine affect the lives and health of all. These interests, like the First Amendment, have 'always had a special claim to judicial protection.' Consequently, more precision may be required than the less rigorous development of scientific facts which may attend notice and comment procedures.[126]

The Court reaffirmed the Administrative Procedures Act: "Absent constitutional constraints or extremely compelling circumstances" the agencies are free to determine their own rules of procedure.[127] The Administrative Procedures Act sets the maximum procedural requirements.[128] Courts are not free to add to them.[129] Agencies can fashion their own rules of procedure but cannot be mandated by courts to do so.[130]

The Court therefore reaffirmed NEPA is a procedural statute, an environmental full disclosure statute.[131] The only procedural requirements of NEPA are those within the statute.[132] The agency's duty is to take a hard look at the environmental consequences.[133] The role of the court is not to second guess the agency's decision on the merits.[134]

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121 *Id.* at 643.
122 *See id.*
123 *Id.* at 652–53.
124 *See id.* at 653–54.
125 *Id.* at 652.
126 *Id.* at 657.
127 Vt. Yankee Nuclear Power Corp. v. Nat. Res. Defense Council, Inc., 435 U.S. 519, 543 (1978).
128 *See id.* at 524.
129 *See id.*
130 *See id.* at 543–45.
131 *See id.* at 558.
132 *See* Kleppe v. Sierra Club, 427 U.S. 390, 405–06 (1976).
133 *See id.* at 410 n.21.
134 *See id.* at 407.

The federal government still has not developed a site for disposal of high-level nuclear waste generated by commercial nuclear power plants.

The other case, *Consumers Power*, involved the extent to which the AEC had to consider energy conservation in its impact statements.[135] The NRC's Licensing Board rejected energy conservation as beyond their "province."[136] The agency viewed energy conservation as a novel concept and thus shifted the burden to the intervenors to present "clear and reasonably specific energy conservation contentions."[137] The Court of Appeals held the NRC had to undertake a "preliminary investigation of the proffered alterative sufficient to reach a rational judgment" in deciding whether to further pursue it.[138] The Commission's role is not to act like an umpire calling balls and strikes.[139]

The Supreme Court reversed, cautioning "[c]ommon sense also teaches us that the 'detailed statement of alternatives' cannot be found wanting simply because the agency failed to include every alternative device and thought conceivable by the mind of man."[140] The Court further held the "concept of alternatives must be bounded by some notion of feasibility" to avoid making the impact statement "an exercise in frivolous boilerplate."[141] The role of the courts is not to second guess or substitute its judgment for that of the agency.[142]

A long-standing split existed between the D.C. Circuit Court of Appeals and the Supreme Court on judicial review of nuclear energy.[143] The Court cautioned the lower courts that the desirability of nuclear energy is a legislative matter and not judicial:

> Nuclear energy may some day be a cheap, safe source of power or it may not. But Congress has made a choice to at least try nuclear energy, establishing a reasonable review process in which courts are to play only a limited role. . . . Time may prove wrong the decision to develop nuclear energy, but it is Congress or the States within their appropriate agencies which must eventually make that judgement.[144]

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135 *See* Aeschliman v. U.S. Nuclear Regul. Comm'n, 547 F.2d 622 (D.C. Cir. 1976).
136 *Id.* at 625.
137 *Id.* at 626.
138 *Id.* at 628.
139 *Id.* at 627.
140 Vt. Yankee Nuclear Power Corp. v. Nat. Res. Def. Council, Inc., 435 U.S. 519, 551 (1978).
141 *Id.*
142 *See id.* at 555.
143 *See generally* Kleppe v. Sierra Club, 427 U.S. 390; see also Vermont Yankee, 435 U.S. 519.
144 *Id.* at 557–58.

The D.C. Circuit again overturned the NRC decision on remand because it felt the agency had not considered the long-term consequences of storing and handling the nuclear wastes.[145] The Supreme Court again reversed the court of appeals, reemphasizing that NEPA is a procedural statute.[146] The court's role is "simply to ensure that the agency has adequately considered and disclosed the environmental impact of its actions."[147] The standard of review is "arbitrary or capricious."[148]

NEPA is one of America's great creations in environmental protection.[149] States and foreign countries have adopted their own versions of NEPA. NEPA, within the Supreme Court's constraints, plays a major role in informing the public on the environmental effects of federal action. It also serves as a method for opponents of a project to litigate and stall action on the adequacy of impact statements.[150]

A major problem with NEPA is that it has become a tool of delay by project opponents.[151] They seek relief contending a NEPA statement should have been prepared or, if prepared, is insufficient. Legal proceedings, and thus delay, ensues.

V. THE LIMITS OF TECHNOLOGY

Dupont's slogan for several decades was "Better Living Through Chemistry." Benjamin Braddock whispered in the Graduate: "One word: Plastics."[152] Faith in science and technology permeated society into the 1960s. Rachel Carson's *Silent Spring* triggered a reexamination of the faith in technology. DDT, leaded gas, and *Reserve Mining* paved the way for government regulation of toxic risk. The problem is that regulatory agencies have to engage in risk analysis with incomplete knowledge of the risks, especially long-term risks. Judges and juries have to decide cases when the toxic risks are

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145 *See* Nat. Res. Def. Council, Inc. v. U.S. Nuclear Regul. Comm'n, 685 F.2d 459, 477–80 (D.C. Cir. 1982).

146 Balt. Gas & Elec. Co. v. Nat. Res. Def. Council, Inc., 462 U.S. 87, 97–98 (1983).

147 *Id.* at 106–08.

148 *Id.* at 98.

149 The other is the creation of national parks with the creation of Yosemite National Park in 1872. Act of Mar. 1, 1872, ch. 24, § 1, 17 Stat. 32 (codified as amended at 16 U.S.C. §§ 21–40c).

150 *See generally* Denis Binder, *Cutting the Nimbian Knot: A Primer*, 40 DEPAUL L. REV. 1009 (1991).

151 *See generally id.* at 1009.

152 *The Graduate One Word Plastics*, YOUTUBE (Sept. 30, 2015), http://www.youtube.com/watch?v=eaCHH5D74Fs.

not fully known or often unknown.

The D.C. Circuit in *Industrial Union Department, AFL-CIO v. Hodgson*[153] recognized:

> [S]ome of the questions involved in the promulgation of these standards are on the frontiers of scientific knowledge, and consequently as to them insufficient data is presently available to make a fully informed factual determination. Decision making must in that circumstance depend to a greater extent upon policy judgments and less upon purely factual analysis. Thus, in addition to currently unresolved factual issues, the formulation of standards involves choices that by their nature require basic policy determinations rather than resolution of factual controversies. Judicial review of inherently legislative decisions of this sort is obviously an undertaking of different dimensions.[154]

Professor Rodgers in reviewing the disparate opinions in *Industrial Union Dep't. v. American Petroleum Inst.*[155] wrote the disagreements may reflect "the fact that we live in a time when values are in disarray. Institutions caught in the flux of technological and social change are in for a rough ride until and unless new grounds for consensus emerge."[156]

A. Dichlorodiphenyltrichloroethane ("DDT")

DDT was the miracle pesticide coming out of World War II. The chemical, first synthesized in 1874, seemed the answer to many problems. It killed the insects which spread malaria, typhus, and dengue fever.[157] It was used to delouse the returning soldiers at the end of the war.[158] DDT was then widely applied to civilian uses after the war, such as controlling boll weevils in the South.[159]

DDT is not known to be toxic to humans but is listed as a suspected carcinogen.[160] The soil half-life ranges from twenty-two

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153 499 F.2d 467 (D.C. Cir. 1974).

154 *Id.* at 474–75.

155 448 U.S. 607 (1980).

156 William H. Rodgers, Jr., *Judicial Review of Risk Assessments: The Role of Decision Theory in Unscrambling the Benzene Decision*, 11 ENV'T L. 301, 302 (1981).

157 *DDT Regulatory History: A Brief Survey (to 1975)*, EPA, https://archive.epa.gov/epa/aboutepa/ddt-regulatory-history-brief-survey-1975.html [http://perma.cc/MB5B-RK33] (Sept. 14, 2016).

158 *The US Army Used DDT to De-louse Soldiers*, APPALACHIAN HIST. (July 27, 2018), https://www.appalachianhistory.net/2018/07/army-used-ddt-for-de-lousing.html [http://perma.cc/3MSK-X7GB].

159 *DDT Regulatory History*, *supra* note 157.

160 AM. CANCER SOC'Y, *Known and Probable Human Carcinogens*, http://www.cancer.org/cancer/cancer-causes/general-info/known-and-probable-human-carcinogens.html [http://perma.cc/K4V5-HK92].

days to thirty years in the environment.[161] It is resistant to metabolism, which combined with its long half-life, allows DDT to build up in the food chain. Many insects developed resistance to DDT.[162]

Rachel Carson, a preeminent biologist,[163] noticed the relationship between DDT and the decline of raptors by disrupting their reproductive cycle. The chemical resulted in the thinning of their eggshells, resulting in their collapse as the mothers were nesting on them. The populations of eagles, hawks, falcons, condors, ospreys, and pelicans dropped as a result.

She documented the problem and then published *Silent Spring*[164] in 1962—one of the classic books of environmental protection. *Silent Spring* quickly became a national sensation. It alerted the American public to the dangers of toxins, especially toxic chemicals.

The first major issue before the newly established EPA was the fate of DDT. The EPA delayed in responding to a request to rescind the registration of DDT.[165] Judge Bazelon penned his famous line on the onset of the environmental era:

> We stand on the threshold of a new era in the history of the long and fruitful collaboration of administrative agencies and reviewing courts. For many years, courts have treated administrative policy decisions with great deference, confining judicial attention primarily to matters of procedure. On matters of substance, the courts regularly upheld agency action, with a nod in the direction of the "substantial evidence" test, and a bow to the mysteries of administrative expertise. . . .
>
> As a result of expanding doctrines of standing and reviewability, and new statutory causes of action, courts are increasingly asked to review administrative action that touches on fundamental personal interests in life, health, and liberty. These interests have always had a special claim to judicial protection, in comparison with the economic interests at stake in a ratemaking or licensing proceeding.[166]

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161 *DDT (General Fact Sheet)*, NAT'L PESTICIDE INFO. CTR., http://npic.orst.edu/factsheets/ddtgen.pdf [http://perma.cc/CN7H-ECSH] (last updated 1999).

162 *Id.*

163 Her other books include UNDER THE SEA-WIND (1941), THE SEA AROUND US (1951), THE EDGE OF THE SEA (1955), and THE SENSE OF WONDER (1965). She also extensively published essays and short articles.

164 CARSON, *supra* note 10 and accompanying text.

165 *See* Env't Def. Fund, Inc. v. Ruckelshaus, 439 F.2d 584 (D.C. Cir. 1971). The court viewed the silence on the request to suspend the DDT registration as a final decision, which was thereby reviewable. No adequate explanation supported the failure to act.

166 *Id.* at 597–98.

The EPA banned DDT in 1972,[167] followed, of course, by litigation. The Federal Insecticide, Fungicide, and Rodenticide Act (FIFRA) provides for the cancellation of misbranded pesticides.[168] Misbranding occurs if an insecticide "used as directed or in accordance with commonly recognized practice . . . shall be injurious to living man or other vertebrate animals."[169]

One claim against the EPA's DDT ban was that the agency lacked substantial evidence in the record.[170] Seven months of testimony produced inconsistent evidence, a not unusual result.[171] The court felt substantial evidence existed in the record to show the hazardous nature of DDT even if it was not proven beyond a reasonable doubt.[172] The Administrator found "DDT is hazardous because of its inherent properties: its persistence, mobility, and lipid solubility."[173] He concluded DDT posed "an unacceptable risk to man and his environment."[174] Inconsistent evidence might have justified a contrary conclusion, but was insufficient to vitiate the Administrator's decision.[175] The EPA followed up the DDT litigation by banning replacement pesticides.[176]

Two cases, one involving leaded gas and the other asbestos, proceeded through the judiciary in parallel tracks, wrestling with the legislative standard of "endanger."

B. Leaded Gas: *Ethyl Corp. v. Environmental Protection Agency*[177]

Early gasoline caused a knocking problem in cars. Tetraethyllead was found to be an effective anti-knock additive to gasoline as well as increasing the octane level in gas. However, the lead was emitted in auto exhausts, posing a substantial public health threat,[178] especially to children.

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167 The EPA technically cancelled the registration of all pesticides containing DDT.

168 7 U.S.C. § 135(a)(5) (current version at 7 U.S.C. § 136).

169 *Id.* § 135(z)(2)(g) (current version at 7 U.S.C. § 136).

170 The other claim was a violation of NEPA. Env't Def. Fund, Inc. v. Env't Prot. Agency, 489 F.2d 1247, 1250 (D.C. Cir. 1973).

171 *Id.* at 1252.

172 *Id.*

173 *Id.*

174 *Id.*

175 *Id.* at 1252–53.

176 The EPA followed up the DDT litigation by subsequently suspending the registration of the aldrin and dieldrin pesticides. Env't Def. Fund, Inc. v. Env't Prot. Agency, 510 F.2d 1292 (D.C. Cir. 1975). *See also* Env't Def. Fund, Inc. v. Env't Prot. Agency, 465 F.2d 528 (D.C. Cir. 1972).

177 541 F.2d 1 (D.C. Cir. 1976).

178 Lead at high exposure levels can be fatal, cause anemia, severe intestinal cramps, paralysis of nerves, and fatigue. Extensive litigation over lead paint and its risks to children has resulted. *See, e.g.*, State v. Lead Indus. Ass'n, Inc., 951 A.2d 428 (R.I. 2008).

The EPA promulgated a schedule for phasing out lead from gasoline. The Clean Air Act authorized the EPA to regulate gasoline additives that "endanger the public health or welfare,"[179] but did not define "endanger." The EPA relied on theoretical, epidemiological, and clinical tests to establish the risks of lead in the atmosphere, especially near highways and homes with lead paint.[180]

Judge J. Skelly Wright started the court's decision with prescient words:

> Man's ability to alter his environment has developed far more rapidly than his ability to foresee with certainty the effects of his alterations. It is only recently that we have begun to appreciate the danger posed by unregulated modification of the world around us, and have created watchdog agencies whose task it is to warn us, and protect us, when technological 'advances' present dangers unappreciated—or unrevealed—by their supporters. Such agencies, unequipped with crystal balls and unable to read the future, are nonetheless charged with evaluating the effects of unprecedented environmental modifications, often made on a massive scale. Necessarily, they must deal with predictions and uncertainty, with developing evidence, with conflicting evidence, and, sometimes, with little or no evidence at all.[181]

The lead manufacturers argued for a "high quantum of factual proof, proof of actual harm rather than of a 'significant risk of harm.'"[182] They asserted the regulation has to be premised on "factual proof of actual harm."[183]

The court of appeals disagreed, looking to both case law and the dictionary.[184] The word "endanger" entails less than actual harm; "endanger" is a precautionary standard; "will endanger" presents a "significant risk of harm."[185] It means harm is threatened.[186] The court followed the reasoning of *Reserve Mining* that "the magnitude of risk sufficient to justify regulation is inversely proportionate to the harm to be avoided."[187] Danger can be decided by "assessment of risks as well as by proof of facts."[188] The alternative approach, that of the lead manufacturers, would

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179 541 F.2d at 7 (citing 42 U.S.C. § 1857f–6c(1)(A)).
180 *Id.* at 44.
181 *Id.* at 6.
182 *Id.* at 12.
183 *Id.*
184 *Id.* at 13.
185 *Id.*
186 *Id.*
187 *Id.* at 19 (citing Rsrv. Mining Co. v. Env't Prot. Agency, 514 F.2d 492, 528–29 (8th Cir. 1975)).
188 *Id.* at 24.

mean the agencies would have to wait for actual harm, to be reactive rather than preventative.[189]

The opinion further addresses the demand for a high degree of proof to justify a regulation, or ban:

> Where a statute is precautionary in nature, the evidence difficult to come by, uncertain, or conflicting because it is on the frontiers of scientific knowledge, the regulations designed to protect the public health, and the decision that of an expert administrator, we will not demand rigorous step-by-step proof of cause and effect. Such proof may be impossible to obtain if the precautionary purpose of the statute is to be served.[190]

Judge Wright reaffirmed the standard of judicial review, the yet to be named *Chevron* Doctrine, by following the earlier DDT case:

> In the case at bar our task is made somewhat simpler than the agency's by adhering conscientiously to the proper scope of judicial review of administrative action, i.e., we as a court are confronted with a problem in administrative law, not in chemistry, biology, medicine, or ecology. It is the administrative agency which has been called upon to hear and evaluate testimony in all scientific fields relevant to its ultimate question of permission or prohibition of the sale and use of DDT. The EPA Administrator had an opportunity to make a careful study of the record of seven months of public hearings and the summaries of evidence prepared for him, heard oral argument, and now has arrived at a decision to ban most uses of DDT. It is his decision which we must review; we are not to make the same decision ourselves.[191]

C. *Reserve Mining* Cases

The Eighth Circuit asked: "[W]hat manner of judicial cognizance may be taken of the unknown[?]"[192]

Two steel companies formed a subsidiary, Reserve Mining, to process Minnesota taconite into iron ore. Sixty-seven thousand tons daily of tailings were discharged into Lake Superior and the atmosphere.[193] *Reserve Mining* would normally be a pollution issue. No harm had yet been shown to public health and any

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189 *Id.* at 25.

190 *Id.* at 28.

191 *Id.* at 37 n.77 (quoting Env't Def. Fund, Inc. v. Env't Prot. Agency (Coahoma), 489 F.2d 1247, 1252 (D.C. Cir. 1973)).

192 Rsrv. Mining Co. v. United States, 498 F.2d 1073, 1084 (8th Cir. 1974).

193 Thomas R. Huffman, *Exploring the Legacy of Reserve Mining: What Does the Longest Environmental Trial in History Tell Us About the Meaning of American Environmentalism?*, 12 J. POL'Y HIST. 339, 340–41 (2000).

health danger was not imminent.[194] However, asbestos was found in the air and water discharges, creating a toxic health risk.[195] The critical issue for the Court of Appeals was if an injunction should be issued in light of the uncertainties of the risk. The district court issued a preliminary injunction based on the public health risks of breathing and drinking asbestos fibers.[196]

Reserve Mining is a pioneering case in using epidemiology, occupational health, and oncology.[197] By 1970 asbestos was a known carcinogen with a rising death toll from mesothelioma, lung cancer, and asbestosis. The known health risks were from inhaling asbestos, compounded by smoking. The evidence of an imminent health hazard was speculative and conjectural. Dr. Arnold Brown, a court appointed expert, opined "no adverse health consequences could be scientifically predicted on the basis of existing medical knowledge,"[198] but "the presence of a known, human carcinogen . . . is in my view cause for concern, and if there are means of removing that human carcinogen from the environment, that should then be done."[199] Studies have established that airborne asbestos are a health risk, but the evidence is lacking on asbestos fibers entering the digestive tract.[200] The extent to which the ingestion of asbestos fibers poses a health risk is unknown, but Dr. Brown testified the possibility of an increased risk of future cancer cannot be ignored.[201]

The court balanced the public interests and issued an injunction, recognizing "[A] risk may be assessed from suspected, but not completely substantiated, relationship between facts, from trend among facts, from theoretical projections from imperfect data, or from probative preliminary data not yet certifiable as 'fact.'"[202] The court recognized the threat did not require an immediate shutdown of the plant,[203] affording Reserve Mining a reasonable opportunity and time to abate the pollution and threat to public health.[204]

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194 Rsrv. Mining Co. v. Env't Prot. Agency, 514 F.2d 492, 500 (8th Cir. 1975).
195 *Id.* at 501.
196 United States v. Rsrv. Mining Co., 380 F. Supp. 11 (D. Minn. 1974).
197 Huffman, *supra* note 193, at 347.
198 514 F.2d at 506.
199 *Id.* at 513.
200 *Id.* at 514.
201 *Id.* at 517.
202 *Id.* at 529 (quoting Ethyl Corp. v. Env't Prot. Agency, 541 F.2d 1, 28 (D.C. Cir. 1975)).
203 *Id.* at 507.
204 *Id.* at 537.

The court though in an earlier opinion recognized: "[W]e are a court of law, governed by rules of proof, and unknowns may not be substituted for proof of a demonstrable hazard to the public health."[205]

The dilemma for the court was that proof did not exist showing asbestos in water is harmful to humans:

> In the absence of proof of a reasonable risk of imminent or actual harm, a legal standard requiring immediate cessation of industrial operations will cause unnecessary economic loss, including unemployment, and, in a case such as this, jeopardize a continuing domestic source of critical metals without conferring adequate countervailing benefits.[206]

The court recognized the discharges into the air and water posed "a potential threat to the public health."[207] The court thereby held the discharges posed a danger to public health. It mandated filtration of drinking water for the affected communities.

The judges looked to the recent appellate decision in the lead gas case, quoting Judge Wright:

> The meaning of "endanger" is, I hope, beyond dispute. Case law and dictionary definition agree that endanger means something less than actual harm. When one is endangered, harm is threatened; no actual injury need ever occur. . . . 'Endanger,' . . . is not a standard prone to factual proof alone. Danger is a risk, and so can only be decided by assessment of risks. [A] risk may be assessed from suspected, but not completely substantiated, relationships between facts, from trends among facts, from theoretical projections from imperfect data, or from probative preliminary data not yet certifiable as 'fact.'[208]

They further wrote Congress used the word "'endangering' in a precautionary or preventative sense, and, therefore, evidence of

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205 Rsrv. Mining Co. v. United States, 498 F.2d 1073, 1084 (8th Cir. 1974).

206 514 F.2d at 537. *See also* Bradley v. Am. Smelting & Refin. Co., 709 P.2d 782, 791 (Wash. 1985).

207 514 F.2d at 500.

208 *Id.* at 529. The judges disposed of the air pollution claims by finding a violation of Minnesota's air pollution rules, thereby constituting a public nuisance. *Id.* at 524. A significant side issue in *Reserve Mining* is that the appellate court removed District Judge Miles Lord from the case for overt bias against Reserve Mining and disregard of earlier holdings by the appellate court. Rsrv. Mining Co. v. Lord, 529 F.2d 181, 185 (8th Cir. 1976). The court felt "Judge Lord seems to have shed the robe of the judge and to have assumed the mantle of the advocate." *Id.* For a history of the irascible Judge Miles Lord, see ROBERTA WALBURN, MILES LORD: THE MAVERICK JUDGE WHO BROUGHT CORPORATE AMERICA TO JUSTICE (2017). For general discussions of *Reserve Mining*, see THOMAS F. BASTOW, "THIS VAST POLLUTION . . ." (1986), and FRANK D. SCHAUMBURG, JUDGMENT RESERVED: A LANDMARK ENVIRONMENTAL CASE (1976).

potential harm as well as actual harm comes within the purview of that term."[209]

Reserve Mining proceeded in 1980 to dispose of the tailings on land ponds five miles from the lake.[210] Clarity has returned to Lake Superior.

The effect of these trifecta cases is that agencies can take a prophylactic approach to toxic risk analysis, short of a zero-tolerance standard.[211] The word "endangering" is to be construed as "precautionary" or "preventative."[212] Actual proof of harm is not therefore a prerequisite for judicial action.

D. *Edwards v. New York Times* and the First Amendment

The DDT controversy also gave rise to a critical First Amendment decision on the right of the media to cover controversial issues. The debate over the fate of DDT was highly contentious.

The National Audubon Society (NAS) conducts an annual Christmas Bird Count, followed by publishing an annual report. Spotters, often referred to as "birders," go out annually at the same location to count birds by species. The raptor count had been rising seemingly despite the growing presence of pesticides in the environment. The preface to the 1971 report explained the apparent discrepancy was because the annual count has more and better trained counters, resulting in a more accurate count. It continued: "Any time you hear a 'scientist' say the opposite, you are in the presence of someone who is being paid to lie, or is parroting something he knows little about."[213] DDT supporters asserted a ban was "deliberately genocidal."[214]

The NAS provided five names to the *New York Times* reporter, who was able to contact three of the five. They denied the accusations with one calling it "almost libelous."[215]

The *Times* printed the story including the denials. The scientists sued for defamation. The Second Circuit upheld the *Times* on First Amendment grounds. The judges held the article was newsworthy. The court recognized the right of the media to

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209 514 F.2d at 528.

210 Huffman, *supra* note 193, at 342.

211 *See* Indus. Union Dep't, AFL-CIO v. Am. Petrol. Inst., 448 U.S. 607 (1980) (essentially a zero-tolerance level for benzene in the workplace).

212 514 F.2d at 528.

213 Edwards v. Nat'l Audubon Soc'y, Inc., 556 F.2d 113, 117 (2d Cir. 1977).

214 *Id.* at 116.

215 *Id.* at 117.

cover and report on controversies. The media has a privilege of neutral reportage.

> Succinctly stated, when a responsible, prominent organization like the National Audubon Society makes serious charges against a public figure, the First Amendment protects the accurate and disinterested reporting of those charges, regardless of the reporter's private views regarding their validity.[216]

The court further held that the denials by the named scientists did not constitute constitutional malice, the standard established in *New York Times v. Sullivan*.[217] The *Times* reported both the accusation and the denials.

The First Amendment protections extended to the media also protect project opponents. Developers were prone to bringing lawsuits against opponents, hoping to chill their opposition.[218] Professors Pring and Canan of the University of Denver Law School labeled these lawsuits "SLAPP" actions (Strategic Litigation Against Public Participants).[219]

California and other states have enacted anti-SLAPP statutes to ban these lawsuits.[220] In addition, if the public participants win the original SLAPP suit, they can then bring abuse of process and malicious prosecution suits against the original plaintiffs.

VI. THE ENDANGERED SPECIES ACT (ESA): *TENNESSEE VALLEY AUTHORITY V. HILL*[221]

The Tellico Dam was ninety-five percent complete on the Little Tennessee River in Tennessee when a small, endangered species, the Snail Darter, was discovered downstream of the

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216 *Id.* at 120. The Audubon case and the privilege of neutral reporting is the subject of an article from the St. John's Law Review Symposium, Celebrating the Centennial of the Second Circuit Court of Appeals. Floyd Abrams, *The First Amendment in the Second Circuit: Reflections on* Edwards v. National Audubon Society, Inc., *the Past and the Future*, 65 ST. JOHN'S L. REV. 731 (1991).

217 556 F.2d at 120–21.

218 *See, e.g.*, Note, *Counterclaim and Countersuit Harassment of Private Environmental Plaintiffs: The Problem, Its Implications, and Proposed Solutions*, 74 MICH. L. REV. 106 (1975); ExxonMobil Pipeline Co. v. Coleman, 512 S.W.3d 895 (Tex. 2017) (determining application of the Texas Citizens Participation Act).

219 Penelope Canan & George W. Pring, *Studying Strategic Lawsuits Against Public Participation: Mixing Quantitative and Qualitative Approaches*, 22 L. & SOC'Y REV. 385 (1988); GEORGE W. PRING & PENELOPE CANAN, SLAPPS: GETTING SUED FOR SPEAKING OUT (1996).

220 *See, e.g.*, CAL. CIV. PROC. CODE §§ 425.16–425.17 (West 2020).

221 437 U.S. 153 (1978).

dam.[222] The dam's completion had been held up by NEPA litigation with the injunction about to be lifted.[223]

The ESA, like many of the federal environmental statutes, contains a citizen suit provision,[224] which allows private citizens to sue to enforce environmental statutes.[225] Section 7 of the statute provides:

> Each Federal agency shall, in consultation with and with the assistance of the Secretary, insure that any action authorized, funded, or carried out by such agency . . . is not likely to jeopardize the continued existence of any endangered species or threatened species or result in the destruction or adverse modification of habitat of such species which is determined by the Secretary . . . to be critical . . . .[226]

The statute thereby protects not only the species, but also its critical habitat. Destroying the critical habitat of a species can decimate a species indirectly rather than directly. Section 9 extends the Act's protections to private parties, prohibiting any person from taking any endangered or threatened species.[227]

Chief Justice Burger[228] wrote the 6-3 decision upholding the ESA and the appellate court decision granting a permanent injunction against the dam.[229] He wrote the ESA is "the most comprehensive legislation for the preservation of endangered species ever enacted by any nation[,]"[230] and "[t]he plain intent of

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222 *See* ZYGMUNT J.B. PLATER, THE SNAIL DARTER AND THE DAM: HOW PORK-BARREL POLITICS ENDANGERED A LITTLE FISH AND KILLED A RIVER 1 (2013) (providing context and a comprehensive history of the Tellico Dam saga as the lead attorney for the plaintiffs).

223 *See* Env't Def. Fund v. Tenn. Valley Auth., 371 F. Supp. 1004, 1015 (E.D. Tenn. 1973), *aff'd* 492 F.2d 466, 468 (6th Cir. 1974).

224 16 U.S.C.A. § 1540(g)(1) (West 2020).

225 For a discussion of citizen suits, see generally Adam Babich, *Citizen Suits: The Teeth in Public Participation*, 25 ENV'T L. REP. NEWS & ANALYSIS 10141, 10141 (1995); Jeffrey G. Miller & Brooke S. Dorner, *The Constitutionality of Citizen Suit Provisions in Federal Environmental Statutes*, 27 J. ENV'T L. & LITIG. 401, 401 (2012).

226 16 U.S.C.A. § 1536(a)(2) (West 2020); *see also* 16 U.S.C.A. § 1532(6) (West 2020) ("The term 'endangered species' means any species which is in danger of extinction throughout all or a significant portion of its range other than a species of the Class Insecta determined by the Secretary to constitute a pest whose protection under the provisions of this chapter would present an overwhelming and overriding risk to man.").

227 *See* 16 U.S.C.A § 1538(a)(1)(B) (West 2020); *see also* 16 U.S.C.A. § 1532(19) (West 2020) ("The term 'take' means to harass, harm, pursue, hunt, shoot, wound, kill, trap, capture, or collect, or to attempt to engage in any such conduct.").

228 The story is that the Chief Justice was opposed to the statute. However, he changed positions to write the strong, majority opinion when he realized the Court was going to uphold the statute, hoping to draw a legislative backl*ed Species Act Lessons Over 30 Years, and the Legacy of the Snail Darter, a Small Fish in a Pork Barrel*, 34 ENV'T L. 289, 304 n.35 (2004); PLATER, *supra* note 222, at 267.

229 *See* Tenn. Valley Auth. v. Hill, 437 U.S. 153, 193–95 (1978).

230 *Id.* at 180.

Congress in enacting this statute was to halt and reverse the trend toward species extinction, whatever the cost."[231]

The Chief Justice recognized:

> One would be hard pressed to find a statutory provision whose terms were any plainer than those in § 7 of the Endangered Species Act. Its very words affirmatively command all federal agencies "to *insure* that actions *authorized, funded*, or *carried out* by them do not *jeopardize* the continued existence" of an endangered species or "*result* in the destruction or modification of habitat of such species . . . ."[232]

He continued by asserting that the "language admits of no exception[,]"[233] and "that Congress intended endangered species to be afforded the highest of priorities."[234] Chief Justice Burger further recognized that Congress placed an "incalculable" value on endangered species.[235]

The Supreme Court in *Tennessee Valley Authority* turned a sleeper statute into a great source of environmental protection. The ESA lacks the usual statutory license, permit, and variance provisions with one limited exception.[236] Injunctive relief is almost automatic under the statute when endangered species are threatened on public or private lands.[237] The usual equitable requirement of balancing the equities, including a cost-benefit analysis, is inapplicable because "Congress viewed the value of endangered species as 'incalculable.'"[238]

Congress responded to the decision by creating the seven-member ESA Committee, commonly nicknamed the "God Committee" or "God Squad."[239] A majority of five members is necessary to exempt an action from the ESA.[240] The God Committee unanimously reaffirmed the

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231 *Id.* at 184.

232 *Id.* at 173.

233 *Id.*

234 *Id.* at 174.

235 *Id.* at 187.

236 *See* 16 U.S.C.A. § 1539(a)(1)(B) (West 2020) (codifying Congress' 1982 amendment to the Endangered Species Act to allow a permit for a "taking otherwise prohibited . . . if such taking is incidental to, and not the purpose of, the carrying out of an otherwise lawful activity").

237 *See* Weinberger v. Romero-Barcelo, 456 U.S. 305, 313–14 (1982).

238 *See* 437 U.S. at 187–88.

239 The God Committee consists of the Secretaries of Agriculture, Army, and Interior, the Administrators of the Environmental Protection Agency and National Oceanic and Atmospheric Agency, the Chair of the Council of Economic Advisors, and an elected official from the affected state. *See* 16 U.S.C.A. § 1536(e)(3) (West 2020).

240 *See* 16 U.S.C.A. § 1536(h)(1) (West 2020). The conditions specified in the statute are: i) no reasonable alternative to the agency's action; ii) the benefits of the proposal

decision in favor of the Snail Darter, thereby standing against completion of the dam.[241]

The Tennessee delegation in Congress subsequently attached a rider to a budget bill. The rider required the completion and operation of the dam, which opened on November 29, 1979.[242] The Snail Darter survived elsewhere, but the completion of the Tellico Dam effectively resulted in the end of the era of big dams.[243] The ESA received a broad mandate from the Supreme Court.[244]

VII. THE PUBLIC TRUST DOCTRINE

The public trust doctrine harkens back to the Justinian Code: "By the law of nature these things are common to mankind—the air, running water, the sea, and consequently the shores of the sea."[245] The Justinian Code was a compilation of existing Roman legal principles. The public trust section reflects a preexisting history.[246] Both civil law and common law jurisdictions recognize the public trust doctrine.

The Supreme Court in *Illinois Central Railroad Co. v. Illinois*[247] recognized the public trust doctrine in U.S. law.[248] The public trust doctrine then mostly fell into the background, although California recognized it over the years. In 1869, the Illinois legislature granted 1,000 acres of submerged lands of the Chicago waterfront, namely the bed of Lake Michigan, to the

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clearly outweigh the benefits of any alternative course of action consistent with the conservation of species or its critical habitat; iii) the action is of the public interest and is of regional or national significance; and iv) neither the federal agency nor the external applicant made irreversible commitments of resources. 16 U.S.C.A. § 1536(h)(1)(A) (West 2020).

241 *See* PLATER, *supra* note 222, at 5.

242 *See id.* at 341.

243 *See* Dan Tarlock, *Hydro Law and the Future of Hydroelectric Power Generation in the United States,* 65 VAND. L. REV. 1723, 1763 n.196 (2012) (referring to the completion of the Seven Oaks Dam on the Santa Ana River as the major exception to provide flood protection in Orange, Riverside, and San Bernardino Counties in California in response to the river's history of severe flooding).

244 *But see* J.B. Ruhl, *The Endangered Species Act's Fall from Grace in the Supreme Court*, 36 HARV. ENV'T L. REV. 487, 490 (2012) (positing that the Supreme Court, in subsequent opinions, retreated somewhat from the lofty levels of *TVA v. Hill* by placing restrictions on standing and imposing additional conditions on recovery).

245 J. INST. 2.1.1.

246 One major situation giving rise to the doctrine dealt with villa owners and their costal estates. The villa owners sought to extend their properties into the seas with large fishponds, preventing local fishermen-citizens from fishing. *See* Bruce W. Frier, *The Roman Origins of the Public Trust Doctrine*, 32 J. ROMAN ARCHAEOLOGY 641, 643–44 (2019).

247 146 U.S. 387 (1892).

248 *See id.* at 435–37.

Illinois Central Railroad.[249] It revoked the grant just four years later.[250] The Supreme Court held the state holds the lands in trust for the people for the purposes of the public trust.[251] Small grants can be made, but not an "abdication of the general control of the state over lands under the navigable waters."[252]

Professor Joseph Sax published in 1970 his seminal article *The Public Trust Doctrine in Natural Resource Law: Effective Judicial Intervention*,[253] positing the public trust doctrine as a critical principle of environmental law. His thesis, after an extensive review of the history of the doctrine, was "to encourage public agencies to engage in creative water management that serves the overall public interest."[254]

He looked at the suspicious path of the Illinois legislation that transferred the waterfront to the railroad, as well as similar transactions elsewhere in America,[255] to posit this premise: "When a state holds a resource which is available for the free use of the general public, a court will look with considerable skepticism upon *any* governmental conduct which is calculated *either* to reallocate that resource to more restricted uses *or* to subject public uses to the self-interest of private parties."[256]

The traditional protections of the public trust doctrine are fishing, commerce, and navigation measured from the medium low water mark and the median high water mark (the wet sand area). The California Supreme Court extended the public trust doctrine to include changing public needs, such as the preservation of lands in their natural state, open space, and environments for food and habitat for birds and marine life.[257]

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249 *See id.* at 448–54.

250 *See id.* at 449.

251 *See id.* at 463–64.

252 *Id.* at 452–53.

253 Joseph L. Sax, *The Public Trust Doctrine in Natural Resource Law: Effective Judicial Intervention*, 68 MICH. L. REV. 471 (1970). It is one of the classic environmental law articles.

254 David Aladjem, *The Public Trust Doctrine: New Frontiers for Sustainable Water Resources Management*, NAT'L RES. & ENV'T, Summer 2010, at 17 (citing to Sax, *supra* note 253).

255 *See* Sax, *supra* note 253, at 547. A different perspective on the Illinois Central transaction is in Joseph D. Kearney & Thomas W. Merrill, *The Origins of the American Public Trust Doctrine: What Really Happened in Illinois Central*, 71 U. CHI. L. REV. 799 (2004).

256 Sax, *supra* note 253, at 490.

257 *See* Marks v. Whitney, 491 P.2d 374, 380 (Cal. 1971); *see also* Wilbour v. Gallagher, 462 P.2d 232, 239 (Wash. 1969) (indicating public trust includes rights of fishing, boating, swimming, water skiing, and other related recreational uses).

The West was settled for resource exploitation, be it mining for gold, silver, and lead, farming, ranching, forestry, or fishing. Water development in the West was essential since much of the West, especially outside the coastal areas, is dry. The need was to utilize the West's scarce water resources. Water Law is a matter of state law. The western states, led by California[258] and Colorado,[259] adopted the prior appropriation system of water rights rather than the riparian system of England and the East.

California, a state of constant population growth since the days of the 49ers, was as culpable as elsewhere of destroying wetlands. For example, the San Francisco Bay shrunk by a third, in the century leading up to the creation of the San Francisco Bay Conservation and Development Commission.[260] Corruption was widespread in the dispersal of public lands.[261]

Americans leveled hills, drained, filled and channeled wetlands, bridged, tunneled, dammed, diverted rivers, clear cut the forests, mined the nation's lands in the first 260 years of the country's existence. California was no exception beginning with the Gold Miners of 1849, who used hydraulic mining to level hills in the search for gold.

The growing pueblo of Los Angeles developed its existing water supply, and then under the leadership of William Mulholland diverted the Owens River to the San Fernando Valley in 1913. Owens Valley was a rich agricultural area. The city surreptitiously bought up the water rights to the valley. In the debates leading up to the diversion, Mulholland said: "If you don't get the water, you won't need it."[262] He said when the gates were opened: "There it is, take it."[263]

The Owens Valley diversion epitomized the West's efforts to bring water to the people rather than the people to the water by

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258 *See* Irwin v. Phillips, 5 Cal. 140, 11–15 (1855).

259 *See* Yunker v. Nichols, 1 Colo. 551, 553–54 (1872); Coffin v. Left Hand Ditch Co., 6 Colo. 443, 446 (1882).

260 *See* S.F. BAY CONSERVATION & DEV. COMM'N, 2018 ANN. REP. 5 (2019), http://bcdc.ca.gov/reports/2018AnnualReport.pdf [http://perma.cc/AU2J-43F2].
About 35 miles of Bay habitat have been restored since creation of the BCDC in 1965. *Id.* Both Oakland and San Francisco International Airports are on filled-in land of the Bay.

261 Professor Sax postulates that much of the public trust litigation in the United States developed as a reaction to legislative largesse with the handling of the public domain. *See* Sax, *supra* note 253, at 490–91 n.62.

262 DAVID HALBERSTAM, THE POWERS THAT BE 115 (2000).

263 Amy Pyle, *'There It Is. Take It …' and for 75 Years, the City Has*, L.A. TIMES (Nov. 18, 1988), http://www.latimes.com/archives/la-xpm-1988-11-18-me-614-story.html [http://perma.cc/2LY9-ECHW].

reshaping the natural environment.[264] Los Angeles took it, grew, and outgrew the Owens Valley water. It went another 90 miles up the Sierra Nevada Mountains to Mono Lake, diverting four of the five tributaries of Mono Lake into the Los Angeles Aqueduct.[265]

A classic example of the Mid-Nineteenth Century environmental disregard was the Los Angeles Department of Water Policy's proposed diversion of waters from Mono Lake to its existing Owens Valley diversion.[266] California's Water Board decision said:

> [I]t is indeed unfortunate that the City's proposed development will result in decreasing the aesthetic advantages of Mono Basin but there is apparently nothing that this office can do to prevent it False This office . . . has no alternative but to dismiss all protests based upon the possible lowering of the water level in Mono Lake and the effect that the diversion of water from these streams may have upon the aesthetic and recreational use of the Basin.[267]

The environmental consequences on the fertile Owens Valley were devastating; the Valley was often turned into a windblown, dusty desert. The environmental effects on Mono Lake were equally devastating. The Lake had shrunk by a third from its-pre-diversion level of 85 square miles to 60.3 square miles in 1979 while its surface level dropped 43 feet.[268] The Lake has a high salt concentration which supports the brine shrimp population which feed nesting and migratory birds.[269] The islands in the Lake provided the breeding grounds for 95% of the California Gull population.[270] The lake's level continuously dropped, exposing the gull population on the disappearing islands to coyotes.[271]

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264 Another example is San Francisco's diversion of water from the Tuolumne River in the Sierra Nevada Mountains to supply water to San Francisco and other Bay Area communities.

265 The history of Los Angeles' struggles for water to serve a burgeoning population are well-documented. *See* LES STANDIFORD, WATER TO THE ANGELS: WILLIAM MULHOLLAND, HIS MONUMENTAL AQUEDUCT, AND THE RISE OF LOS ANGELES (1st ed. 2015); WILLIAM DEVERELL & TOM SITTON, WATER AND LOS ANGELES: A TALE OF THREE RIVERS, 1900–1941 (2016); CATHERINE MULHOLLAND, WILLIAM MULHOLLAND AND THE RISE OF LOS ANGELES (2000). For a broader analysis of the dry West's struggles for water, see NORRIS HUNDLEY JR., WATER AND THE WEST (1975) and the classic MARC REISNER, CADILLAC DESERT: THE AMERICAN WEST AND ITS DISAPPEARING WATER (1993).

266 Professor Ryan has written extensively on the Mono Lake litigation. *See* Erin Ryan, *The Public Trust Doctrine, Private Water Allocation, and Mono Lake: The Historic Saga of "National Audubon Society v. Superior Court*," 45 ENV'T L. 561 (2015).

267 Nat'l Audubon Soc'y v. Super. Ct. of Alpine Cty., 658 P.2d 709, 714 (Cal. 1983) (citation omitted).

268 *See id.*

269 *Id.* at 715.

270 *Id.* at 716.

271 *See id.*

The conflict between diversion and the public trust doctrine came to a head in the California Supreme Court decision in *National Audubon Society v. Superior Court*[272] echoing Professor Sax's thesis. The California Supreme Court held:

> [T]he public trust is more than an affirmation of state power to use public property for public purposes. It is an affirmation of the duty of the state to protect the people's common heritage of streams, lakes, marshlands and tidelands, surrendering that right of protection only in rare cases when the abandonment of that right is consistent with the purposes of the trust.[273]

The California Supreme held the public trust doctrine protects navigable waters from harm caused by diversion of non-navigable tributaries.[274] No vested right exists to the waters protected by the public trust.[275]

The result is that the state "retains continuing supervisory control over its navigable waters and the lands beneath those waters."[276] The state can thereby reconsider prior decisions. The holding therefore is that some body of the state has to reconsider the allocation of the Mono Lake waters.[277]

The Mono Lake case changed both the settled expectations of the Los Angeles Department of Water and Power, which had been diverting Owens Valley and Mono Lake waters for decades pursuant to permits issued by the state, and permit holders throughout the West. The California Water Resources Control Board in 1993 ordered minimum stream flows restored and imposed a minimum water level for Mono Lake.[278] Los Angeles and the environmentalists reached a full agreement on the diversions in 2013.[279]

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272 *See id.* at 712.

273 *Id.* at 724. For a look back at the Mono Lake case, see Craig Anthony (Tony) Arnold, *Working Out an Environmental Ethic: Anniversary Lessons from Mono Lake*, 4 WYO. L. REV. 1 (2004).

274 *See Nat'l Audubon Soc'y*, 658 P.2d at 721.

275 See *id.* at 729.

276 *Id.* at 727.

277 *See id.* at 728–29.

278 *See* Louis Sahagun, *L.A., Conservationists Reach Agreement to Repair Mono Lake Damage*, L.A. TIMES (Aug. 23, 2013, 12:00 AM), http://www.latimes.com/local/la-xpm-2013-aug-23-la-me-mono-20130824-story.html#:~:text=Ending%20decades%20of%20bitter%20disputes,World%20War%20II%2Dera%20aqueduct [http://perma.cc/EMQ9-3TDS].

279 *Id.*

The Audubon case effectively opened and reopened water law in the West to instream flow protecting environmental values, habitat protection and fish flows.

The Justinian Code and the public trust doctrine became the basis of *Juliana v. United States*,[280] which could result in revolutionary changes in United States environmental Law. Nineteen minors aged 8 to 19 filed suit in 2015 against the United States seeking injunctive relief against the federal government's contributions to global warming.[281] They advanced three different theories for relief: 1) a constitutional right exists to a clean, healthy environment; 2) just as the Justinian Code led to the public trust doctrine over water, so too should it create an atmospheric trust over the air;[282] and 3) the public trust doctrine applies to the federal government as well as state governments.[283] The District Court granted relief on all three theories,[284] but the Ninth Circuit Court of Appeals denied standing to the plaintiffs, thereby dismissing the case.[285]

VIII. MINING

A. Hydraulic Mining

Gold was discovered on January 24, 1848 at Sutter's Mill in California. A gold rush ensued with the 49ers coming from around the world. The early miners panned for gold—a laborious, inefficient method of gold mining.[286]

The miners soon discovered high pressure hoses could rip the soil off hills, being funneled into sluices where the gold would drop to the bottom. The environmental consequences of hydraulic mining were catastrophic. Trees were stripped off the hills to

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280 947 F.3d 1159 (9th Cir. 2020).

281 *See* Juliana v. United States, 217 F. Supp. 3d 1224, 1233 (D. Or. 2016), *rev'd*, 947 F.3d 1159 (9th Cir. 2020).

282 For a discussion of the Justinian Code's background of the Atmospheric Trust argument, see Erin Ryan, *From Mono Lake to the Atmospheric Trust: Navigating the Public and Private Interests in Public Trust Resource Commons*, 10 GEO. WASH. J. ENERGY & ENV'T L. 39 (2019); J.B. Ruhl & Thomas A.J. McGinn, *The Roman Public Trust Doctrine: What Was It, and Does It Support an Atmospheric Trust?*, 47 ECOLOGY L. Q. 117 (2020).

283 *See Juliana*, 217 F. Supp. at 1233.

284 *Id.* at 1250, 1253, 1259.

285 *See* Juliana v. United States, 947 F.3d 1159, 1174–75 (2020).

286 For a history of the gold mining techniques in California, see Snowy Range Reflections Staff, *Mining Techniques of the Sierra Nevada and Gold Country*, 2 J. SIERRA NEV. HIST. & BIOGRAPHY (2009), https://www.sierracollege.edu/ejournals/jsnhb/v2n1/miningtechniques.html [http://perma.cc/55TA-WDD4].

facilitate mining. Hills were leveled, rivers were narrowed, navigation was impaired, and farmland was buried. Flooding intensified as streams were blocked or clogged. Erosion was intensified. Fish populations declined.

Aggrieved farmers sued the largest hydraulic mining company.[287] The federal judge issued an injunction after two years of considering the case, holding that the process constitutes a public and private nuisance.[288] This early environmental victory, the first in the United States, is little known today.

B. Strip Mining (Surface Mining)[289]

Coal fueled the industrial revolution and continues to generate electricity and heat through much of the world despite the global commitment to reducing carbon emissions. Underground mining was historically the source of coal. The fuel is dirty and the consequences on Appalachia environmentally disastrous.[290] Coal production started shifting to surface mining, also known as strip mining, about a half century ago.

Unreclaimed strip mining is an environmental disaster, leaving a moon-like landscape.[291] John Prine, a folk singer, wrote the song *Paradise* about a coal company's strip mine in Paradise, Kentucky.[292] In response, President Ford twice vetoed a surface mining reclamation act.[293] President Carter finally signed the Surface Mining Control and Reclamation Act (SMCRA) in 1977.[294] Severe restrictions are contained in the statute, including protection of alluvial valleys, permits, reclamation, and the power of the Secretary of the Interior to designate areas as

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287 *See* The Debris Case. Woodruff v. N. Bloomfield Gravel Mining Co., 16 F. 25, 26 (D. Cal. 1883).

288 *See id.* at 27–28.

289 Surface mining can be referred to as open cut mining or strip mining. I prefer to use "strip mining" because the practice strips the surface off the land.

290 *See* HENRY CAUDILL, NIGHT COMES TO THE CUMBERLANDS (1962).

291 Thousands of miles of Appalachian streams are contaminated with acid waters. Water supplies are imperiled. Recreation and industrial uses are curtailed while vegetation and fish life imperiled. *See* Denis Binder*, A Novel Approach to Reasonable Regulation of Strip Mining*, 34 U. PITT. L. REV. 339, 343–45 (1973). For a discussion of the environmental impacts of strip mining in the western states, see Denis Binder*, Strip Mining, The West and the Nation*, 12 LAND & WATER L. REV. 1, 20–21 (1977).

292 JOHN PRINE, *Paradise*, *on* JOHN PRINE (Atlantic Records 1971).

293 S. 425 received a pocket veto by President Ford. *See* 120 CONG. REC. 41996–97 (1974). H.R. 25 was vetoed the next year. *See Veto of the Surface Mining Control and Reclamation Act of 1975, Message from the President of the United States*, 94 CONG. H. NO. 94–160 (May 20, 1975).

294 Surface Mining and Control Reclamation Act of 1977, Pub. L. No. 95–87, 91 Stat. 445 (1977) (codified at 30 U.S.C. §§ 1201–1328).

unsuitable for surface mining, if the mining operation could adversely affect fragile or historical lands in a manner that could cause substantial damage to important historic, cultural, scientific, and aesthetic values to national systems.[295] The land is to be restored to its "approximate original contour."[296]

A coal miners association claimed the statute was unconstitutional for violating the tenth Amendment. The Supreme Court upheld the statute in *Hodel v. Virginia Surface Mining & Reclamation Association, Inc.,*[297] under the Tenth Amendment as an example of cooperative federalism. The federal government defers primary enforcement to states if the states agree and meet the federal requirements.[298] The result was a comprehensive state and national regulation of strip mining, substantially reducing the environmental degradation it caused. The statute covers mining, operations, cleanup and restoration.[299] The Court also reiterated its past decisions holding that the Commerce Clause can displace states' exercises of their police powers.[300]

SMCRA is an example of the statutory model of cooperative federalism, which is characteristic of several environmental statutes. The federal government is prepared to unilaterally regulate an environmental problem, but shares regulation and enforcement with states as long as they meet conditions prescribed by Congress. The states can do the primary regulation and enforcement, but the federal agency has oversight responsibilities.

The Court recognized a narrow test for judging the constitutionality of a federal regulatory program affecting interstate commerce. The test is simple: does a rational basis exist for the Congressional action?[301] The Commerce Clause is a grant of plenary power to Congress.[302]

The regulatory program had several abuses in practice, including outright violations.[303] A statutory exception subject to substantial violation was the two-acre exception intended to

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295 *See* 30 U.S.C.A. § 1265 (Westlaw through P.L. 116–252).
296 *Id.* at § 1265(b)(3).
297 452 U.S. 264, 289 (1981).
298 *See* 30 U.S.C.A § 1253 (Westlaw through P.L. 116–252).
299 *Id.*
300 *See Hodel*, 452 U.S. at 292–93.
301 *Id.* at 276.
302 *Id.*
303 *See* Lily Whiteman, *Recent Efforts to Stop Abuse of SMCRA: Have They Gone Far Enough,* 20 ENV'T L. 167, 169–70 (1990).

protect small "mom and pop" operations. One ploy was the "string of pearls" scheme, whereby a series of parallel pits were mined on a seam.[304] Congress abolished the two acre exception in 1987.[305]

A more recent problem is mountain top mining whereby coal miners chop off the top of mountains to mine the coal.[306] Augers used to drill into hills; now they are demolished from the top.[307] Mountain top mining devastates forests, fills stream with debris, and kills off native species.[308]

Only decades later did the country move away from fossil fuels, especially coal, for electricity production; this resulted in a substantial reduction in both surface and underground coal mining.

IX. INJUNCTIVE RELIEF

Equity developed in England when the strict common law rules could not provide relief to deserving plaintiffs. Injunctive relief is the primary, but not exclusive equitable remedy. The normal remedy under the Administrative Procedures Act is judicial review and reversal, but injunctions are an alternative remedy for ongoing operations.

Equity, which started out as a flexible remedy, has developed its own rules. The normal requirements for injunctive relief are 1) An inadequate remedy at law; 2) Irreparable injury to plaintiff if the injunction is denied; 3) Balancing of the equites; and 4) the public interest. Injunctive relief is discretionary.

The *Restatement (Second) of Torts* section 936 lists six factors to be considered in balancing the equities:

> Sec. 936. Factors in Determining Appropriateness of Injunction.
>
> 1) The appropriateness of the remedy of injunction against a tort depends upon a comparative appraisal of all the factors in the case, including the following primary factors:
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> a) the nature of the interest to be protected,
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> b) the relative adequacy to the plaintiff of injunction and of other

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304 *Id*. at 171–72.

305 *See* Act to Amend the Surface Mining Control and Reclamation Act of 1977, Pub. L. No. 100–34, § 201, 101 Stat. 300 (1987).

306 *See e.g.*, John McQuaid, *Mining the Mountains*, SMITHSONIAN MAG. (Jan. 2009), https://www.smithsonianmag.com/science-nature/mining-the-mountains-130454620/ [http://perma.cc/9NVF-RD9W].

307 *Id.*

308 *Id.*

> remedies,
>
> c) any unreasonable delay by the plaintiff in bringing suit,
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> d) any related misconduct on the part of plaintiff,
>
> e) the relative hardship likely to result to defendant if an injunction is granted and to the plaintiff if it is denied,
>
> f) the interests of third persons and of the public, and
>
> g) the practicability of framing and enforcing the order or judgment.[309]

The question arose regarding whether environmental laws preempted traditional equitable balancing, with the argument being that the strong public policy of environmental protection should control the balancing. For example, the Supreme Court in *TVA v. Hill* did not allow a balancing of the equities in enforcing the Endangered species Act.[310]

For example, the Navy used Vieques Island off Puerto Rico for weapons training for decades.[311] A lawsuit was filed alleging the Navy's ongoing shelling operations violated the Clean Water Act for discharging munitions into navigable waters without a permit.[312] The district court found a violation of the CWA and required the Navy to seek a permit, but denied issuance on an injunctive.[313] The court of appeals reversed, reasoning the Clean Water Act removed equitable discretion,[314] thus requiring immediate injunctive relief for the violations.[315]

The Supreme Court reversed the appellate tribunal,[316] holding that equitable discretion remained under the Clean Water Act. The traditional balancing of the equities remains, but with a specific caveat from the Court—courts of equity, in exercising their discretion, "should pay particular regard for the public consequences in employing the extraordinary remedy of injunction."[317] The Court held that the basis for equitable relief is "irreparable injury and the inadequacy of legal remedies."[318]

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309 RESTATEMENT (SECOND) OF TORTS § 936 (AM. L. INST. 1977). The injunction sections of the Restatement (3rd) of Torts have not been finalized at the time this article was written.

310 Tenn. Valley Auth. v. Hill, 437 U.S. 153, 187–88 (1978).

311 *See* Romero-Barcelo v. Brown, 478 F. Supp. 646, 655 (D. P.R. 1979).

312 *See id.* at 663.

313 *See id.* at 664, 708.

314 *See* Romero-Barcelo v. Brown, 643 F. 2d 835, 861–62 (1st Cir. 1981).

315 *See id.*

316 Weinberger v. Romero-Barcelo, 456 U.S. 305, 307 (1982).

317 *Id*. at 312.

318 *Id*.

The Court distinguished *TVA v. Hill* by noting the Endangered Species Act left no discretion.[319] Congress made it "abundantly clear that the balance has been struck in favor of affording endangered species the highest of priorities."[320]

A quarter century later, the Court reaffirmed *Romer-Barcelo* in another Navy training program, this time sonar-training, emphasizing that any harm to the plaintiffs is offset by the public interest. The Court further recognized the public interest of national security. The Court saw "no basis for jeopardizing national security, as the present injunction does."[321]

The effect of Weinberger and its progeny is a reaffirmation of the basic equity premise that equitable relief is discretionary. The public interest remains a major factor in balancing the equities.

X. THE CONSTITUTIONAL DIMENSIONS

A. Commerce Clause: *City of Philadelphia v. New Jersey*[322]

The thirteen American colonies entered into the Articles of Confederation upon achieving independence from England in the Treaty of Paris. The Articles failed for several reasons, one of which was restrictions existed on commerce between the states. The Constitution replaced the Articles on March 4, 1789.

One of the major changes was to place Congress in control of commerce between the states, displacing the individual states. The Commerce Clause thereby became a major source of power for the federal government, as well as a restraint on the states (the "negative commerce clause").

The federal government is a government of enumerated powers, not plenary powers. The Commerce Clause is the primary source of regulatory power.[323] The Clause empowers Congress "to regulate commerce with foreign Nations, and among the several States, and with Indian Tribes."[324] The regulation of commerce pursuant to the Commerce Clause is limited to a sufficient nexus between the proscribed act and interstate

319 *Id.* at 331.
320 Tenn. Valley Auth. v. Hill, 437 U.S. 153, 194 (1978).
321 Winter v. Nat'l Res. Def. Council, Inc., 555 U.S. 7, 32–33 (2008).
322 437 U.S. 617 (1978).
323 *Id.*
324 U.S. CONST. art. I, § 8.

commerce.[325] Other sources of power are the property, spending, and taxation clauses.[326]

The Commerce Clause significantly serves not only as a grant of power to Congress, but also as a restriction on state powers.[327] A primary goal of the Commerce Clause is to break down barriers to the free flow of commerce.[328] State and local governments thereby lack the power to restrict the free flow of commerce between the states.[329]

The natural inclination of states and local governments is to obtain the benefits of commerce but place the burdens on others. *Philadelphia v. New Jersey*[330] is a prime example of this reality. New Jersey was concerned about exhausting the capacity of its landfills.[331] It thereby banned the importation of out-of-state solid or liquid waste (trash) except when the waste had economic value.[332] New Jersey's statute was an act of economic protectionism.[333]

The Supreme Court threw out the New Jersey act as a restriction on the free flow of commerce.[334] All items in interstate commerce, including trash, are entitled to protection under the Commerce Clause.[335] The key is discrimination based on origin, even for trash. The purpose of protecting the state "may not be accomplished by discriminating against articles of commerce coming from outside the [s]tate unless there is some reason, apart from their origin, to treat them differently."[336] The critical passage in the case is:

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325 *See, e.g.*, United States v. Lopez, 514 U.S. 549, 561 (1995); United States v. Morrison, 529 U.S. 598, 613 (2000).

326 A case that combines issues of the Commerce, Property, Spending, and Taxation Clauses is *New York v. United States*, 505 U.S. 144 (1992).

327 *See* 437 U.S. at 622–23.

328 *See id.* at 623.

329 *Id.*

330 *Id.* at 628.

331 *Id.* at 625.

332 New Jersey allowed the importation of garbage to be fed to swine, any separated waste material intended for a recycling or reclamation facility, municipal solid waste to be processed into secondary materials, and pesticides, hazardous waste, chemical waste, bulk liquid, and bulk semi-liquid to be treated, processed or recovered. *Id.* at 618–19, 619 n.2 (citing N.J. STAT. ANN. § 13-1I-10 (West Supp. 1978)).

333 *Id.* at 628–29.

334 *Id.* at 629.

335 *Id.* at 622.

336 *Id.* at 626–27. Apparently New York and New Jersey trash are basically identical in content. *Id.* at 629. New Jersey was allowing New Jersey trash to be deposited in the state's landfill, but not New York trash. *Id.* New Jersey was thus discriminating based on the state of origin. *Id.*

> [W]here simple economic protectionism is effected by state legislation, a virtually *per se* rule of invalidity has been erected. The clearest example of such legislation is a law that overtly blocks the flow of interstate commerce at a State's borders. But where other legislative objectives are credibly advanced and there is no patent discrimination against interstate trade, the Court has adopted a much more flexible approach, the general contours of which were outlined in *Pike v. Bruce Church, Inc* . . . .[337]

The Supreme Court further held a state had no right to give its residents a preferred right of access over access to natural resources within the state.[338]

Philadelphia v. New Jersey is the basis for striking down a number of restrictions on commerce, including reciprocity requirements,[339] bans, taxation, preference with in-state products, such as electricity, anti-exportation clauses,[340] bans on products transported through the state, and even voter approval requirements.[341]

B. Spending Clause[342]

An alternative enumerated source of power for Congressional regulation is the Spending Clause: "The Congress shall have Power . . . to pay the Debts and provide for the common Defence and general Welfare of the United States . . . ."[343] Congress can attach conditions to the receipt of federal funds.[344] Congress thereby uses money as a means of inducing states to take actions they might otherwise oppose. For example, the Supreme Court held in *South Dakota v. Dole*[345] Congress could condition the receipt of federal highway funds

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337 *Id.* at 624 (citing Pike v. Bruce Church, Inc., 397 U.S. 137, 142 (1970), which laid out these markers: "Where the statute regulates even-handedly to effectuate a legitimate local public interest, and its effects on interstate commerce are only incidental, it will be upheld unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits. If a legitimate local purpose is found, then the question becomes one of degree. And the extent of the burden that will be tolerated will of course depend on the nature of the local interest involved, and on whether it could be promoted as well with a lesser impact on interstate activities.").

338 *Id.* at 627.

339 *See* Hardage v. Atkins, 619 F.2d 871, 872–73 (10th Cir. 1980).

340 *See* Sporhase v. Nebraska *ex rel.* Douglas, 458 U.S. 941, 953, 960 (1982).

341 *See* Stablex Corp. v. Town of Hooksett, 456 A.2d 94, 101 (N.H. 1982).

342 A symposium on the Spending Clause can be found at *Spending Clause Symposium*, 4 CHAP. L. REV. 1 (2001), with articles by Professors Richard A. Epstein, John C. Eastman, Erwin Chemerinsky, Earl M. Maltz, Bradley A. Smith, Denis Binder, Celestine Richards McConville, and Lynn A. Baker.

343 U.S. CONST. art. I, § 8, cl. 1.

344 *See* South Dakota v. Dole, 483 U.S. 203, 211–12 (1987).

345 *Id.*

upon states raising the minimum drinking age to 21.[346]

Certain limitations apply though to government's power under the Spending Clause:

1) Spending must be in pursuit of the general welfare;

2) The intent to attach conditions must be articulated and unambiguous;

3) The conditions must be reasonably related to the articulated grant; and

4) The conditions cannot be barred by other Constitutional provisions.[347]

The Ninth Circuit opinion in *Nevada v. Skinner*[348] provides an example of the Spending Clause in action. Gas was very inexpensive through the 1960's. Detroit's response was to build large, heavy gas guzzling vehicles. Two Arab oil embargoes in the 1970's shot up the price of gas and focused attention on energy conservation.[349]

A substantial way to conserve gas is to drive slower. Congress attached a maximum speed limit of 55 miles per hour (MPH) (the double nickel) to the receipt of federal highway funds.[350] The 55 MPH was unpopular in the vast open space of the West. Nevada sued, claiming the potential loss of 95% of federal highway funds was so coercive as to deprive it of any choice in setting its speed limits.[351] The argument is that the state had no practical alternative but to comply because of the potential loss of 95% of its highway funding.[352] Nevada was looking to the words of the 1937 case of *Steward Machine Co. v. Davis*:[353] "Our decisions have recognized that in some circumstances the financial inducement offered by Congress

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346 The federal government provides 95% of the funding for interstate and primary road construction. *See id*.

347 Nevada v. Skinner, 884 F.2d 445, 447 (9th Cir. 1989), *cert. denied,* 493 U.S. 1070 (1990). The Supreme Court subsequently reaffirmed that a condition attached to the receipt of federal funds must bear "some relationship" to the funding's purpose. New York v. United States, 505 U.S. 144, 167 (1992).

348 884 F.2d 445. Nevada played fast and loose with standing and the federal funding. The Nevada statute raised the speed limit to 70 MPH, but included a self-executing provision whereby the state's speed limit would be lowered to the national speed limit if federal officials threatened to cut off funding. *Id.* at 446.

349 *Id.* at 451.

350 *See id.* Congress during the Reagan Administration raised the national speed limit to 65 MPH.

351 *See id.* Montana and Nevada lacked speed limits on sparsely populated rural areas prior to Congress' adoption of the 55 MPH national speed limit.

352 *Id.* at 448.

353 301 U.S. 548 (1937).

might be so coercive as to pass the point at which 'pressure turns into compulsion.'"[354]

The appellate court held the difficulty of assessing a state's financial capabilities made the coercion theory "highly suspect as a method for resolving disputes between federal and state governments."[355] Congress could have constitutionally imposed the national speed limit pursuant to the Commerce Clause. Hence it could not constitute unconstitutional coercion under the Spending Clause.[356]

C. Property Clause: *Kleppe v. New Mexico*[357]

The federal government owns 28% of the nation's land,[358] especially concentrated in the western states.[359] The issue is if the federal government is a landowner subject to state or local regulation or if the federal government possesses independent sovereignty over its lands. The Property Clause provides "[t]he Congress shall have Power to dispose of and make all needful Rules and Regulations respecting the Territory or other Property belonging to the United States . . . ."[360]

Wild horses and burros roam the West. Ranchers abhor them because they compete with cattle for fodder. New Mexico enacted a statute allowing the seizure of wild horses and burros, as was the history in the West. Congress enacted the Wild Free-Roaming Horses and Burros Act, which protected the animals both on federal lands and also if they roam onto private lands.[361]

Burros wandered onto a rancher's federal grazing lands.[362] He notified the New Mexico Livestock Board, which then rounded up and auctioned off nineteen burros.[363] New Mexico argued the federal government only possessed power to control the animals if they were moving in interstate commerce or

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354 *Skinner,* 884 F.2d 445, 447 (citing to *Steward Machine*, 301 U.S. at 590).

355 *Id.* at 448. The legal irony is that the mandatory maximum 55 MPH could easily have been upheld under the Commerce Clause.

356 *Id.* at 449.

357 426 U.S. 529 (1976).

358 CONG. RSCH. SERV., R42346, FEDERAL LAND OWNERSHIP: OVERVIEW AND DATA 1 (2020).

359 45.9% of the land in the contiguous eleven western states is owned by the federal government while 60.9% of Alaska's land is federally owned. *Id.* at 19.

360 U.S. CONST. art. IV., § 3, cl. 2.

361 Wild Free-Roaming Horses and Burros Act of 1971, Pub. L. No. 92-195, 85 Stat. 649 (1971) (codified at 16 U.S.C. §§ 1331–40). For a critique of the statute, see George Santini, Comment*, Good Intentions Gone "Estray"—The Wild, Free-Roaming Horse and Burro Act*, 16 LAND & WATER L. REV. 525 (1981).

362 Kleppe v. New Mexico, 426 U.S. 529, 533 (1976).

363 *Id.* at 533–34.

damaging the federal lands.[364] Otherwise, the federal government would have to obtain the state's consent.[365]

The Supreme Court in *Kleppe v. New Mexico*[366] held Congress acts as both as a proprietor and as a legislature pursuant to the Property Clause.[367] Congress has "complete power" over public property "entrusted to it."[368] Significantly, state and local governments are precluded from regulating the federal lands absent Congressional consent.[369]

The effect of *Kleppe* is that Congress can determine the development or preservation of 28% of the nation's land. The federal government is an owner, operator, proprietor, lessor, licensor, and regulator. The expansive interpretation of the Property Clause allows the federal government not only to regulate things on the federal domain,[370] but also activities passing through the federal domain.[371]

The Court had previously held Congress has absolute power under the Property Clause for "particular public property entrusted to it."[372] The Supreme Court in *Kleppe* held the absolute power Congress has over public lands includes the power to regulate and protect the land's wildlife.[373]

The significance of *Kleppe* is that much of the (rural) west have different views of the public lands than the federal government. They view the federal government as an absentee landlord out of touch with the needs of the people. They want to develop, drill, mine, log, graze, consume the water, otherwise utilize the land, and tax the federal lands.[374] The use of the nation's forests is an ongoing controversy. Should they be seen as a resource for logging or for recreation? A famous letter from Bernard DeVoto explains the dichotomy:

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364 *Id.* The federal government arguably then only had the powers to make incidental rules regarding the use of federal property and to protect federal property. *Id.* at 536.

365 *Id.* at 541.

366 426 U.S. 529 (1976).

367 *Id.* at 540.

368 *Id.*

369 *See id.*

370 Motor boats on rivers, snowmobiles in the national parks, or ATV's and motorcycles in the desert.

371 *See* Nat'l Ass'n of Prop. Owners v. United States, 499 F. Supp. 1223 (D. Minn. 1980), *aff'd*, State of Minnesota v. Block, 660 F.2d 1240 (8th Cir. 1981) (including motor boats and snowmobiles in Boundary Waters Canoe Area Wilderness).

372 United States v. City and County of San Francisco, 310 U.S. 16, 30 (1940).

373 *Kleppe*, 426 U.S. at 541.

374 *See, e.g.*, United States v. Nye County Nevada, 938 F.2d 1040, 1041 (9th Cir. 1991).

> You are certainly right when you say that "us natives" can do what you like with your scenery. But the National Parks and Monuments happen not to be your scenery. They are our scenery. They do not belong to Colorado or the West, they belong to the people of the United States, including the miserable unfortunates who have to live east of the Allegheny hillocks.[375]

This viewpoint periodically expressed itself in movements such as the Sagebrush Rebellion[376] or the Catron County Supremacy Movement.[377] These attempts to assert local control ran afoul of the Property Clause and *Kleppe v. New Mexico*.

Activities the federal government has regulated, restricted, and sometimes banned on federal lands include fishing,[378] ATV's, motor boats,[379] canoes,[380] dog roaming, cattle grazing,[381] prairie dogs on federal lands,[382] beach bonfires,[383] houseboats,[384] snowmobiles,[385] and pesticides."[386]

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375 BERNARD DEVOTO, *Letter from Bernard DeVoto to the Editor of the Denver Post* (Aug. 1, 1950), *in* THE LETTERS OF BERNARD DEVOTO 362, 363 (Wallace Stegner ed., 1975).

376 The Sagebrush Rebellion from the late 1970's to the early 1980's unsuccessfully attempted to force the divestiture of federal lands. A district court rejected Nevada's claim that the Federal Land Policy and Management Act (FLPMA) violated Nevada's 10th Amendment and the Equal Footing Clause. State of Nevada *ex rel.* Nev. State Bd. of Agric. v. United States, 512 F. Supp. 166, 168 (D. Nev. 1981). In general, see FEDERAL LAND OWNERSHIP, *supra* note 358, at 19; A. Costandina Titus, *The Nevada "Sagebrush Rebellion" Act: A Question of Constitutionality*, 23 ARIZ. L. REV. 263, 263 (1981) and Richard D. Clayton, Note, *The Sagebrush Rebellion: Who Should Control the Public Lands?,* 1980 UTAH L. REV. 505, 509.

377 Some counties claimed the federal control of public land was unconstitutional, title belonged in the states, and the counties could thereby control land use on these lands. *See* Elizabeth M. Osenbaugh & Nancy K. Stoner, *The County Supremacy Movement*, 28 URB. LAW. 497, 497 (1996).

378 Commercial fishing in Golden Gate National Recreation Area. San Francisco Herring Ass'n v. U.S. Dep't of the Interior, 946 F.3d 564, 567–68 (9th Cir. 2019).

379 *See* Friends of the Boundary Waters Wilderness v. Bosworth, 437 F.3d 815, 820 (8th Cir. 2006). The federal government in the Boundary Waters Canoe Area Wilderness even applied its restrictions on motor boats and snowmobiles pursuant to the Property Clause to lands it did not own in the BWCAW. *See* State of Minnesota v. Block, 660 F.2d 1240, 1253 (8th Cir. 1981). The case of *Sturgeon v. Frost*, 136 S. Ct. 1061 (2016) may seem contrary, but it interpreted specific statutes applicable to Alaska.

380 *See* Free Enter. Canoe Renters Ass'n of Mo. v. Watt, 549 F. Supp. 252, 263 (E.D. Mo. 1982) (involving commercial renting of canoes within the boundaries of the Ozark National Scenic Riverways).

381 *See* Barton v. United States, 609 F.2d 977, 979 (10th Cir. 1979).

382 *See* People for the Ethical Treatment of Prop. Owners v. U.S. Fish & Wildlife Serv., 852 F.3d 990, 994 n.4 (10th Cir. 2017).

383 *See, e.g.*, *Ocean Beach Fire Program*, NPS.GOV (June 4, 2018), https://www.nps.gov/goga/learn/management/obfireprogram.htm [http://perma.cc/9T3X-RYBM] (including fore pots and a no-burn season from November 1–February 28/29). As teenagers and college students, we would go down to Ocean Beach, gather driftwood, and start a bonfire anywhere on the dry sand any day of the year.

384 *See* Great Am. Houseboat Co. v. United States, 780 F.2d 741, 745 (9th Cir. 1986) (involving houseboats on Lake Shasta).

D. The Takings Clause

The Fifth Amendment, which has been incorporated into the 14th Amendment and thus applicable to the states,[387] provides: "No person shall . . . be deprived of . . . property, without due process of law; nor shall private property be taken for public use, without just compensation."[388] A taking is unconstitutional and thus subject to reasonable compensation, but a reasonable regulation pursuant to police power is constitutional.[389] A dividing line between a taking and a reasonable regulation remains unsettled.

A judge, seven decades ago, recognized that attempting distinctions between a taking and a reasonable exercise of the police power enmeshes one in a "sophistic Miltonian Serbonian Bog."[390] In a classic article, Professor Dunham characterized the cases as a "crazy-quilt pattern."[391]

The Supreme Court has not drawn a bright line between a reasonable exercise of the police power and a taking, admitting it could not develop a fine line for distinguishing between the two.[392] As stated in *Penn Central Transportation Co. v. City of New York:* "[T]his Court, quite simply, has been unable to develop any 'set formula' for determining when 'justice and fairness' require that economic injuries caused by public action be compensated by the government, rather than remain disproportionately concentrated on a few persons."[393] Indeed,

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385 *See e.g.*, Fund for Animals v. Norton, 390 F. Supp. 2d 12, 14 (D.D.C. 2005) (involving snowmobiles in Yellowstone and Grand Teton National Parks—one of roughly a score of cases involving Yellowstone and snowmobiles).

386 *See* United States v. Moore, 640 F. Supp. 164, 167 (S.D. W.Va. 1986) (spraying of pesticides to eliminate black flies within the New River Gorge National River).

387 *See* Chicago, B. & Q. R. Co. v. City of Chicago, 166 U.S. 226, 234 (1897).

388 U.S. CONST. amend. V.

389 A workable definition of the police power appears in the venerable case of *Lawton v. Steele*, 152 U.S. 133, 136 (1894):

> The extent and limits of . . . the 'police power' have been a fruitful subject of discussion in the appellate courts of nearly every State in the Union. It is universally conceded to include everything essential to the public safety, health, and morals, and to justify the destruction or abatement, by summary proceedings, of whatever may be regarded as a public nuisance. . . . Beyond this . . . the state may interfere whereover the public interests demand it, and in this particular a large discretion is necessarily vested in the legislature to determine, not only what the interests of the public require, but what measures are necessary for the protection of such interests.

390 Brazos River Auth. v. City of Graham, 354 S.W.2d 99, 105 (Tex. 1961).

391 Allison Dunham, *Griggs v. Allegheny County in Perspective: Thirty Years of Supreme Court Expropriation Law*, 1962 SUP. CT. REV. 63, 63.

392 *See* Penn Cent. Transp. Co. v. City of New York, 438 U.S. 104, 149–50 (1978).

393 *Id.* at 124.

"The question of what constitutes a 'taking' for purposes of the Fifth Amendment has proved to be a problem of considerable difficulty."[394]

The Court has certainly fulfilled this expectation in a series of subsequent takings and wetlands cases. Decisions do not always resolve the issue at hand. Each new Supreme Court decision initially seems to clarify the issue, but often increases confusion, complexity, and exceptions to exceptions. Even clear statements of principles have exceptions.[395] The reality is that no clear definition exists, thus, no clear rules exist.[396]

A common tool of land use planning is to require developers to "dedicate" land, facilities, or money to offset the community costs of the development. The costs could include infrastructure improvements, schools, police and fire stations, park and recreation facilities, and even land to be preserved as open space. The question arises if government goes too far in imposing conditions.

Nollan v. California Coastal Commission[397] involved the California Coastal Commission conditioning a permit to tear down an existing building on a small beachfront lot upon dedication of a public access, lateral easement along the beach.[398] The Supreme Court held the requirement was unconstitutional; an essential nexus must exist between the purported goal and the restriction/condition.[399] The Coastal Commission argued the shoreline development would interfere with visual access to the beach, but the condition of lateral access was unrelated to this goal.[400]

Chief Justice Rehnquist wrote in *Dolan v. City of Tigard*,[401] "We see no reason why the Takings Clause of the Fifth Amendment, as much a part of the Bill of Rights as the First Amendment or Fourth Amendment, should be relegated to the

394 *Id.* at 123.

395 For exception, a physical invasion, no matter how slight, is usually a takings. *See* Loretto v. Teleprompter Manhattan CATV Corp., 458 U.S. 419, 441 (1982); *but cf.* Preseault v. I.C.C., 494 U.S. 1, 17 (1990). *See also* Amalgamated Food Emp. Union Local 590 v. Logan Valley Plaza, Inc., 391 U.S. 308, 325 (1968) (addressing the judicial roller coaster for shopping center owners); Lloyd Corp., Ltd. v. Tanner, 407 U.S. 551, 567–569 (1972); Hudgens v. N.L.R.B., 424 U.S. 507, 508 (1976); PruneYard Shopping Ctr. v. Robins, 447 U.S. 74, 82–83 (1980).

396 One clear rule is that if the public trust doctrine applies, then no takings issue arises since the property owner is not deprived of a property right.

397 483 U.S. 825 (1987).

398 *Id.* at 827–29.

399 *Id.* at 837.

400 *Id.* at 838.

401 512 U.S. 374 (1994).

status of a poor relation in these comparable circumstances."[402]

Dolan, a plumbing and electric supply wholesaler in Tigard, Oregon, a town of 30,000, wished to expand his building from 9,700 square feet on 1.67 acres to 17,600 square feet and pave a 39-space parking lot.[403] The lot backed up to Fanno Creek, a floodplain unusable for commercial development.[404] The Municipal Plan for the Central Business District required 15% for open space and landscaping.[405] The city demanded Dolan dedicate the floodplain and a 15' strip above it for a pedestrian/bike path.[406] The two dedications would equal 10% and count towards the 15% open space requirement.[407]

The Court recognized preventing flooding has a nexus to the dedication.[408] An asphalt parking lot further increases runoff from an impervious surface. Thus, there was a nexus, a relationship, between the dedication and the purpose of the restrictions.[409]

However, the burden rested on the city to show the required dedication is related in both nature and extent to the impact of the proposed development. The city faced several factual problems in the case. First, the public greenway was unrelated to flood control.[410] Second, the city would deny the basic property rights of owners to exclude.[411] The city didn't meet its burden of proof of showing a reasonable relationship between the trail and the dedication.[412]

Nollan held an essential nexus must exist between a condition the government is seeking to regulate and the measures implemented that affect public property. *Dolan* followed up by imposing a test of rough proportionality, which does not require precision.[413] The standard also needs individualized determination.[414] Some effort must be made to quantify the findings.[415]

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402 *Id.* at 392.
403 *See id.*
404 *Id.* at 379.
405 *Id.* at 380.
406 *Id.*
407 *Id.*
408 *Id.* at 383.
409 *Id.* at 386–87.
410 *Id.* at 393.
411 *Id.*
412 *Id.* at 395.
413 *Id.* at 391.
414 *Id.*
415 *Id.*

For example, the city said the dedications "could" offset, but that is not equivalent to "will" or "likely to." The City had not shown the additional number of vehicle and bicycle trips, generated but the expansion, was reasonably related to the required dedication.

The Court held the government cannot require a person to give up a constitutional right in exchange for a discretionary benefit when the property sought has little or no benefit to the government.[416]

XI. FEDERALISM: ILLINOIS V. CITY OF MILWAUKEE TRILOGY

Justice Holmes wrote in the 1907 interstate pollution case of *State of Georgia. v. Tennessee Copper Co.*:[417]

> It is a fair and reasonable demand on the part of a sovereign that the air over its territory should not be polluted on a great scale by sulphurous acid gas, that the forests on its mountains, be they better or worse, and whatever domestic destruction they have suffered, should not be further destroyed or threatened by the acts of persons beyond its control, that the crops and orchards on its hills should not be endangered from the same source.[418]

The case became the basis for a federal common law of interstate pollution.

Environmental Law in the early years was a Tabula Rasa. Courts wrestled with fundamental questions, one of which was allocating jurisdiction between federal and state courts. Many contamination cases involve common law nuisance claims.

In *Illinois v. City of Milwaukee, Wis.*, [419] the Supreme Court not only held that federal law governs interstate water pollution, but also that federal common law could resolve the dispute. Justice Douglas wrote, "When we deal with air and water in their ambient or interstate aspects, there is a federal common law[.] . . ."[420] The decision had the potential to open up the federal court houses to a flood of nuisance suits.

However, the Court held nine years later in City of Milwaukee v. Illinois (Milwaukee II) that federal common law is displaced when Congress speaks directly on the matter; then it

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416 *Id.* at 396.

417 206 U.S. 230 (1907).

418 *Id.* at 238.

419 406 U.S. 91, 93 (1972). Illinois sued four Wisconsin cities and two sewerage commissions for discharging sewage in lake Michigan. *See also* Ohio v. Wyandotte Chemicals Corp., 401 U.S. 493 (1971).

420 *See* Illinois v. City of Milwaukee, Wis., 406 U.S. 91, 103 (1972).

occupies the field.[421] The opinion left open the question of whether state common law could apply.[422] The Court subsequently held the law of the source state would apply to an interstate water pollution case, but the case could be brought in the state where the harm occurred.[423]

The *City of Milwaukee* decision was the predecessor 30 years later to *American Electric Power Co., Inc. v. Connecticut*.[424] Several states, New York City and three private land trusts sued the federal Tennessee Valley Authority and four private utilities for emitting carbon dioxide from their fossil fuel plants.[425] Carbon dioxide is a greenhouse gas. The large atmospheric emissions of carbon dioxide contributed to global warming. Plaintiffs sought abatement.[426] The Clean Air Act and EPA actions were sufficient under the City of Milwaukee rule to displace federal jurisdiction on a federal common law public nuisance theory. The door is left open under diversity jurisdiction for a private public nuisance lawsuit in federal court.[427]

The practical effect of the *Illinois v. Milwaukee* litigation is that the federal courts are closed to state common law or statutory pollution lawsuits absent a federal violation or complete diversity of citizenship.

XII. CONCLUSION

We never really know at the unveiling of a new discipline or revolution where it will lead. Will Environmental Law just be, as the 1978 appellants argued in *City of Philadelphia v. New Jersey*, "outwardly cloaked in the currently fashionable garb of environmental protection[?]"[428] Or, would Environmental Law become a compelling, or even determinative, component of public policy? A half-century allows us a look-back to study its evolution.

The ethos has changed: Storm King Mountain, Tellico Dam, Overton Park and the Cross Florida Barge Canal mark the end of the post-World War II infrastructure era as well as 360 years of

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421 *See* City of Milwaukee v. Illinois & Michigan, 451 U.S. 304, 310–11 (1981).
422 *See id.* at 340.
423 *See* Int'l Paper Co. v. Ouellette, 479 U.S. 481, 497 (1987).
424 564 U.S. 410 (2011).
425 *Id.* at 415.
426 *Id.* at 424.
427 *See* Juliana v. United States, 947 F.3d 1159, 1165 (9th Cir. 2020) (pending in the federal courts including private common law nuisance and public trust claims in addition to constitutional claims).
428 437 U.S. 617, 625–26 (1978).

America's emphasis on development to the transition to the Age of the Environment. The full realization of the change in paradigms wasn't immediately realized. These formative battles are, at best, footnotes and perhaps a few perfunctory citations, to today's students and young practitioners. My generation is fast disappearing from environmental law. I have tried over the past decade to paint a picture of the beginnings and thus its legacy.

America's environment has substantially improved over the past half century. The air and waters are cleaner.[429] The Great Lakes are clean. The Rogue River is again naturally beautiful as it flows through Oregon. The Cuyahoga River no longer catches on fire as it flows through Cleveland. The western forests are still standing.

The fabric of environmental law developed in the early days. Many of the cases may seem prosaic, taken for granted,[430] but were considered revolutionary at the time, such as with the more recent *Massachusetts v. EPA*. Today's litigation remains dependent on standing, reviewability, and administrative discretion.

Some early developments, such as NEPA and the Endangered Species Act, quickly grew from "sleeper statutes" into broad statutes cutting across the environmental spectrum. NEPA became a global model. The significance of cases, such as *Sierra Club v. Morton*, was quickly recognized. A few cases established both legal precedence and resolved environmental issues.

Environmental protection is an on-going challenge. Old problems may be resolved. New problems will always emerge. Pollution, even under permits, will contaminate the air and water. Recycling remains a practical issue because of economics.

Environmental Law is dynamic. It overlapped from the beginning Land Use Planning, Administrative Law, Constitutional Law, Energy Law, Property Law and Torts like Venn Diagrams. It is as amazing today as 50 years ago. It is always changing and expanding as the environmental problems evolve and new ones emerge, such as Climate Change, Environmental Justice, and plastics.

However, the pillars supporting Environmental Law remain solid. Even when an environmental problem, such as hydraulic mining, is seemingly resolved over a century ago, the legacy

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429 As an asthmatic I could not have lived in Orange County during the 1960's or 1970's, but do so today as part of the greater Los Angeles Plain.

430 A look at the three Ruhl-Salzman environmental surveys discussed in footnotes 16–17 show a consistent movement to newer cases except for four cases from four to five decades ago.

continues as with the abandoned mines in Colorado. Air and water pollution, and toxic hazards will persist. The parameters of controlling them were established in the early days of the Environmental Era.

The answer to the first set of questions is oblivious. Environmental Law is a critical component of public policy decision making.

Environmental Law seems rock-hard today. Yet, the questions I ask today are: 1) Is Environmental Law now firmly engrained into critical public policy decisions; or 2) Has it reached its apogee?

The Environmental Age is entering its sixth decade. A reaction is highly foreseeable at some point. The Trump Administration has reversed several existing policies[431] and is seeking to revise the CEQ guidelines on NEPA statements.[432] These changes will run through a gauntlet of litigation with uncertain results.

I think of my 2013 conclusion in Looking Back to the Future: The Curmudgeon's Guide to the Future of Environmental Law: "The changes have been dramatic, but it is unwise to ignore the polices, statutes, and mores of the preceding 360 years as they continue to define much of our future, particularly in times of economic adversity and resource scarcities, such as energy. To the extent that environmental protection does not provide our basic needs, it may fail economic and political reality."[433]

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431 For a list of the changes, see Nadja Popovich, Livia Albeck-Ripka & Kendra Pierre-Louis, *The Trump Administration Is Reversing More Than 100 Environmental Rules. Here's the Full List*, N.Y. TIMES (Nov. 10, 2020), http://www.nytimes.com/interactive/2020/climate/trump-environment-rollbacks.html?searchResultPosition=1 [http://perma.cc/K5M6-CKSE].

432 A discussion of the proposed NEPA changes is found at: James M. McElfish, Jr., *What Did CEQ Do?*, ELI (Sept. 14, 2020), http://www.eli.org/vibrant-environment-blog/what-did-ceq-do [http://perma.cc/5K8Z-F36U].

433 Denis Binder, *Looking Back to the Future: The Curmudgeon's Guide to the Future of Environmental Law*, 46 AKRON L. REV. 993, 1016 (2013).

Is Owning Stock an Abnormally Dangerous Activity? Shareholder Limited Liability in Tort

Daniel P. Schley, CFA∗

Academics have contested the merits of shareholder limited liability for decades.[1] As part of this discussion, some of limited liability's critics cite tort law to conclude that corporate law erroneously shields shareholders from personal liability.[2] They contend that tort law would not so egregiously allow shareholders to externalize costs onto tort victims who have no control over the type of legal entity that injures them.[3] But tort law does not follow this logic. It does not examine the type of the defendant merely to search for the deepest pockets to find liability.[4] Moreover, corporate officers and directors—not shareholders—control the ability for the corporation to pay its debts as they come due (corporate capitalization).[5]

Given these academic conclusions' inconsistency with tort law and corporate governance, this Article reconsiders whether shareholders would benefit from limited liability in tort and finds that tort law, like the current corporate law regime, would uphold shareholder limited liability. Shareholders would not be strictly liable for corporate torts. Rather, they would only be liable to the extent they failed to use reasonable care. This Article reaches this conclusion by examining a well-known Judge Richard Posner decision which emphasized that strict liability for abnormally dangerous activities is only relevant to activities, not

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1 *See, e.g.*, Paddy Ireland, Limited Liability, Shareholder Rights and the Problem of Corporate Irresponsibility, 34 CAMBRIDGE J. OF ECON. 837 (2010); Stephanie Blankenburg et al., Limited Liability and the Modern Corporation in Theory and in Practice, 34 CAMBRIDGE J. OF ECON. 821 (2010).

2 *See* discussion *infra* Part II.

3 *See* discussion *infra* Part II.

4 *See* discussion *infra* Part III.

5 *See* discussion *infra* Parts II, IV.

substances.[6] With respect to shareholder personal liability for corporate torts, the relevant activity is corporate capitalization, not the shareholder contribution of equity capital and related limited control rights (the substance). Because a corporation's officers and directors can prevent undercapitalization through the use of due care, negligence—not strict liability—is the appropriate regime for shareholder personal liability.[7] Corporate law understands this intuition by only allowing such liability through the use of piercing the corporate veil, which resembles negligence. Though tort law's conclusions regarding shareholder liability align with corporate law, tort law independently still provides a valuable insight into understanding the hazy doctrine of piercing the corporate veil and corporate purpose more generally. This Article ends with some recommendations for further research.

I. INTRODUCTION

The proper scope of the corporation remains a vigorous debate. Often at its crux is shareholder limited liability. Numerous academics note with suspicion this unique aspect of corporate law which allows shareholders to avoid personal liability to a corporation's creditors.[8] Generally only liable up to their paid-in-capital, though able to reap potentially unlimited gains, shareholders purportedly push corporations to take on excessive risk.[9] These risks are not merely financial (in the form of excess leverage), but even *legal*: if a corporation breaks the law, it is only the corporation—not the shareholders—that pays the penalty or fine.[10] These perverse incentives, coupled with the prevailing belief under shareholder primacy theory that corporate managers have the sole obligation to maximize shareholder profits,[11] have led some scholars to conclude that the corporation is best described in human terms as a psychopath— irresponsible, manipulative, asocial, and unable to feel remorse.[12] Others conclude corporate limited liability

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6 Ind. Harbor Belt R.R. Co. v. Am. Cyanamid Co., 916 F.2d 1174 (7th Cir. 1990).

7 This Article assumes that there has been no election under applicable law for shareholder management of the corporation. See, e.g., DEL. CODE ANN. tit. 8 § 351 (West 2020).

8 *See, e.g.*, David Ciepley, *Beyond Public and Private: Toward a Political Theory of the Corporation*, 107 AM. POL. SCI. REV. 139, 148 (2013).

9 *See* Nina A. Mendelson, *A Control-Based Approach to Shareholder Liability for Corporate Torts*, 102 COLUM. L. REV. 1203, 1247 (2002).

10 *See* Ciepley, *supra* note 8, at 148.

11 *See, e.g.*, Dodge v. Ford Motor Co., 170 N.W. 668, 684 (Mich. 1919).

12 *See* JOEL BAKAN, THE CORPORATION: THE PATHOLOGICAL PURSUIT OF PROFIT AND POWER 56–57 (2004).

is merely a historical accident, which tort law would not tolerate.[13] Academics claim the defects of the corporation create real consequences for the economy at large and undermine economic growth.[14] With the rise of the shareholder primacy theory, limited liability now poses an even greater risk as corporate management own more stock and stock options.[15] In the eyes of such critics, limited liability is simply a mistake which should be eliminated.[16]

Other academics strenuously contest these conclusions about the corporation and shareholder limited liability.[17] Judge Frank H. Easterbrook and Professor Daniel R. Fischel, for example, defend limited liability noting that it decreases the need to monitor investments and other shareholders, promotes free transfer of shares, allows for market pricing and diversification, and optimizes investment decisions.[18]

So, should shareholders retain limited liability? Or should they instead be unlimitedly personally liable for corporate torts? Would eliminating limited liability deter the purported corporate incentive to externalize costs by encouraging shareholders to monitor corporate activities more closely? Or are shareholders, despite their limited control rights, just too powerless and anonymous to influence managerial decisions?

One need not look further than to the absence of examples of corporations failing to compensate their tort victims to reach the conclusion that limited liability is a phantom problem.[19] Where are all of the uncompensated tort victims if limited liability creates such inexorable danger? The reality is that shareholders are largely unable to use the corporation to externalize costs onto creditors. Other corporate stakeholders, like insurers,

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13 *See* Henry Hansmann & Reinier Kraakman, *Toward Unlimited Shareholder Liability for Corporate Torts*, 100 YALE L.J. 1879 (1991) [hereinafter *Toward Unlimited Shareholder Liability for Corporate Torts*]; Henry Hansmann & Reinier Kraakman, *The Essential Role of Organizational Law*, 110 YALE L.J. 387, 431–32 (2000) [hereinafter *The Essential Role of Organizational Law*].

14 *See The Essential Role of Organizational Law*, *supra* note 13.

15 *See* Ciepley, *supra* note 8, at 148; s*ee also* William Lazonick, *Profits Without Prosperity*, HARV. BUS. REV., Sept. 2014, at 3, 4–5.

16 *See Toward Unlimited Shareholder Liability for Corporate Torts*, *supra* note 13, at 1880.

17 *See, e.g.*, Jesse M. Fried & Charles C.Y. Wang, *Short-Termism and Capital Flows* (Eur. Corp. Governance Inst., Working Paper No. 342/2017, 2018), http://ssrn.com/abstract_id=2895161.

18 Frank H. Easterbrook & Daniel R. Fischel, *Limited Liability and the Corporation*, 52 U. CHI. L. REV. 89, 94–96 (1985).

19 *See* Joseph A. Grundfest, *The Limited Future of Unlimited Liability: A Capital Markets Perspective*, 102 YALE L.J. 387, 421 (1992) ("[T]he evidence is hardly overwhelming that limited liability causes a significant increase in a corporation's willingness to engage in risky behavior.").

debtholders and officers and directors, have incentives aligned with any potential tort creditor (that is, a contingent creditor) and are successfully able to police the corporation to such contingent creditor's benefit. This is exactly why share prices in California did not increase after the introduction of limited liability.[20] If cost externalization were possible, those share prices would have increased.

Though concerns about limited liability may only exist in the ivory tower, most critiques of shareholder personal liability have relied on the practical difficulties of shareholder personal liability.[21] None, however, has focused on the theoretical—the truth that tort law actually supports the current corporate law limited liability regime.

Tort law would not hold shareholders personally liable for corporate torts. This becomes obvious when analogizing personal shareholder liability to tort law's strict liability for abnormally hazardous activities. Such strict liability attaches only to activities, not substances. The relevant activity for shareholder personal liability is corporate capitalization, not the contribution of equity capital and limited associated shareholder control rights. A corporation's officers and directors, not its shareholders, control corporate capitalization. Because when officers and directors use due care, corporations are almost certainly able to pay debts—including contingent debts like compensation to potential tort creditors—as they come due, a shareholder would not be strictly liable for corporate torts. A shareholder only becomes liable to the extent he or she controls corporate capitalization and then fails to use reasonable care in doing so. As this Article explains in detail, that is merely to say that a shareholder only faces personal liability when courts pierce the corporate veil—the current corporate law regime.

This Article reaches these conclusions by analyzing whether shareholders would be personally liable in tort law instead of corporate law. Part II discusses recent developments in academic understanding of the corporation and how they should affect the interpretation of prior academic work. Part III introduces strict liability, discusses its relevance to shareholders, and analogizes a well-known strict liability case to the question of shareholder liability for corporate torts. Part IV compares this Article's findings to the current state of corporate law for shareholder

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20 *See* Mark I. Weinstein, *Limited Liability in California 1928–31: It's the Lawyers*, 7 AM. L. & ECON. REV. 439, 440 (2005).

21 See generally Grundfest, *supra* note 19.

liability for corporate torts. Part V reconsiders corporate purpose in light of tort law. In conclusion, Part VI provides some final remarks and suggestions of further relevant research.

II. SHAREHOLDER PERSONAL LIABILITY IN TORT TO THE CORPORATION'S TORT CREDITORS

The most prominent argument for imposing shareholder personal liability for corporate torts proposes liability based on two justifications. One centers around the fact that it is inefficient and unfair as a matter of policy for tort victims to have no control over the type of legal entity that harms. The other supports shareholder liability for corporate torts given their ownership of the corporation and control of its capitalization. These justifications, however, are misguided. First, tortious liability depends not merely on finding the deepest pockets—because a corporation may or may not have the requisite capital—but, rather, on providing proper incentives to control outcomes. Moreover, shareholders neither truly own the corporation nor sufficiently control corporate capitalization to justify their personal liability for corporate acts.

A. The Prominent Argument in Tort Favoring Shareholder Personal Liability

Professors Henry Hansmann and Reinier Kraakman provide a prominent argument for shareholder personal liability.[22] They even posture that corporate limited liability likely is a vestige of a historical accident in the development of corporate law.[23] They argue that it is simply too crude a check. Instead, they advance the theory that, under tort law, shareholders should be personally liable because they are in the best position to avoid and insure against costs.[24]

Their principal rationale is that tort law would find shareholder limited liability inefficient.[25] Limited liability allows shareholders to externalize costs onto society.[26] Unlike corporate contract creditors, a corporation's tort creditors are unable, *ex ante*, to negotiate for shareholder limited liability.[27] Shareholders take advantage of this putative loophole by undercapitalizing.[28]

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22 *The Essential Role of Organizational Law*, *supra* note 13, at 431.

23 *Id.*

24 *See Toward Unlimited Shareholder Liability for Corporate Torts*, *supra* note 13, at 1918.

25 *See The Essential Role of Organizational Law*, *supra* note 13, at 431.

26 *Id.*

27 *Id.*

28 *Id.*

In doing so, shareholders not only leave tort creditors uncompensated when the corporation is insolvent, but also succeed in shielding their own personal assets from those creditors.[29] Involuntary creditors are therefore defenseless.[30] Because these involuntary creditors have no control over the type of legal entity that injures them, Hansmann and Kraakman note that it is inefficient, not to mention unfair, to allow the amount a tort victim recovers to depend merely upon the legal form of the organization responsible for their injury.[31] Shareholders benefitting, for instance, "from intentional dumping of toxic wastes, from marketing hazardous products without warnings, or from exposing employees without their knowledge and consent to working conditions known by the firm to pose substantial health risks, should not be able to avoid the resulting costs simply by limiting the capitalization of their firm."[32] Abolishing limited liability would, in their view, force shareholders to face full liability for potential tort losses. Share prices and the cost of equity would decrease and increase, respectively, to account for such liability.[33]

Hansmann and Kraakman suggest replacing shareholder limited liability with a *pro rata* personal liability regime.[34] They caution that, in abolishing limited liability, courts would still need to determine which costs are efficiently and equitably borne by a corporation and its shareholders but note that shareholders would, in at least certain circumstances, be in the best position to avoid and insure against cost.[35] In those situations, the authors submit that shareholders should be personally liable for corporate torts.[36]

The academic literature critiquing Hansmann and Kraakman's proposal have done so largely on practical grounds.[37] Professor Joseph A. Grundfest, for example, contends that capital market participants are sufficiently agile to arbitrage away personal liability for equity ownership.[38] In Grundfest's view, shareholders would first rearrange themselves so that personal

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29 *Id.* at 393–94.

30 *Id.*

31 *See The Essential Role of Organizational Law*, *supra* note 13, at 431–32.

32 *Toward Unlimited Shareholder Liability for Corporate Torts*, *supra* note 13, at 1917.

33 *See id.* at 1907.

34 *See id.* at 1917–19.

35 *See id.*

36 *See id.*

37 *See, e.g.*, Grundfest, *supra* note 19, at 388 n.3; Janet Cooper Alexander, *Unlimited Shareholder Liability Through a Procedural Lens*, 106 HARV. L. REV. 387, 387 (1992).

38 *See id.* at 390.

assets would be unreachable under a proportionate personal liability regime.[39] Shareholders with personal wealth would only purchase shares of companies with little risk of personal asset exposure.[40] Only persons with little or no personal assets or, more likely, little to no asset exposure, would purchase the equity of riskier firms.[41] Furthermore, were proportionate personal liability implemented at the state level, constitutional limitations on personal jurisdiction would not allow jurisdiction over passive shareholders.[42] Even a statute at the federal level would face problems obtaining personal jurisdiction over foreign defendants given the principles of international comity.[43]

Constitutional problems are compounded by the logistics of collection. Domestic shareholders not party to the original action would attempt to relitigate.[44] The value of shares owned by many shareholders is less than the costs to proceed with an action against them.[45] Enforcing a judgment against a foreign shareholder—or even *identifying* that shareholder—could be impossible.[46] Individuals with personal assets seeking exposure to "riskier" equities could also avoid owning shares altogether through derivatives, which would achieve returns similar to those attained through ownership of traditional shares with limited liability.[47]

Corporations themselves would respond adversely to proportionate personal liability. They would issue less equity in favor of debt and equity-like instruments, like convertible bonds and warrants—all of which lack proportionate personal liability of shares.[48] Intermediaries like investment banks could create structured products to allow the ultimate beneficiaries equity like returns without the concomitant proportionate liability.[49] No amount of regulation would adequately prevent all of these parties from ultimately protecting the shareholder-like party from personal proportionate liability.[50]

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39 *See id.* at 387.
40 *See id.*
41 *See id.*
42 *See id.* at 395.
43 *See id.* at 397.
44 *Id.*
45 *Id.*
46 *Id.* at 398.
47 *Id.* at 402.
48 *Id.* at 409.
49 *Id.* at 408.
50 *Id.* at 416.

Though these critiques merit their own consideration, they do not consider Hansmann and Kraakman's underlying theoretical claim that tort law would not allow shareholder limited liability.[51] This Article considers Hansmann and Kraakman's assumptions about both the corporation and tort law with respect to shareholder limited liability.

B. The Prominent Basis in Tort Favoring Shareholder Personal Liability Relies on Flawed Assumptions about both Tort Law and the Corporation

Hansmann and Kraakman's argument that tort law fails to explain limited liability relies on questionable assumptions about both tort law and the corporation. First, the Restatement of Torts prefers allocative rather than distributive liability.[52] In other words, whether a defendant should be liable in tort—and under which liability regime—should depend on which regime will most effectively control outcomes, not who has the deepest pockets.[53] In determining shareholder personal liability for corporate torts, however, Hansmann and Kraakman argue in favor of liability based on the latter.[54] They contend as a matter of policy that shareholders ought to be personally liable merely because the tort plaintiff has no control over the wealth of the tortfeasor corporation.[55] Indeed, they extrapolate from their position that the amount of damages for shareholder liability should depend on the structure of the particular corporate defendant; shareholders who are corporate parents of a wholly-owned subsidiary should bear greater costs for the subsidiary's torts than shareholders who are natural persons.[56] These rationales are inconsistent with tort doctrine. Tort liability, and the extent of damages for such liability, is not simply based on whether the defendant's shareholders are artificial or natural persons—who could, in theory, be equally as wealthy and equally as culpable.[57]

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51 *See generally, Toward Unlimited Shareholder Liability for Corporate Torts*, *supra* note 13.

52 *See, e.g.*, Ind. Harbor Belt R.R. Co. v. Am. Cyanamid Co., 916 F.2d 1174, 1181 (7th Cir. 1990).

53 *Id.* at 1181–82.

54 *See Toward Unlimited Shareholder Liability for Corporate Torts*, *supra* note 13, at 1916–17.

55 *Id.*

56 *See Toward Unlimited Shareholder Liability for Corporate Torts*, supra note 13, at 1917.

57 *Cf.* Easterbrook & Fischel, *supra* note 18, at 110–11 (arguing courts may be more likely to pierce the veil when the shareholder is a parent corporation of a corporate subsidiary, but only because such a corporate shareholder is more likely to attempt to externalize costs, not because such a corporate shareholder is wealthier than a natural shareholder).

Indeed, judgment-proof natural persons often leave victims uncompensated, yet tort law does not strain to find some nexus to a wealthier party. Rather, as even Hansmann and Kraakman admit, liability should be based on the action in question and which actors are in the best position to avoid the relevant accidents.[58] Hansmann and Kraakman offer no argument for why shareholders are corporate actors in the best position to avoid accidents.

They likely fail to do so because they reach their conclusions based on two related yet problematic theories of the corporation, which incorrectly describe the shareholder's relationship with the corporation. Under Property ("Principal/Agent") Theory, corporations are merely aggregations of shareholders' property.[59] Shareholders are therefore owners of the corporation and principals for whom the corporate officers and directors serve as agents.[60] This statement, however, is more applicable to a partnership where partners function as the sole owners and central contracting parties of the partnership.[61] A modern business corporation, however, meaningfully departs from this construct for two reasons. First, corporate assets and liabilities belong not to shareholders, but to the corporation as a distinct entity. Second, shareholders are not principals to whom the directors owe duties as agents.[62]

Shareholders are not owners because they merely own corporate stock—a contractual obligation between the shareholder and the corporation.[63] This contractual obligation entitles shareholders to own neither the corporation nor its assets.[64] For example, owning Apple shares does not entitle a shareholder to take iPads from an Apple store.[65] The corporation itself, rather, owns itself and its assets. A shareholder's rights with respect to a corporation are therefore not dissimilar to other parties in contract with the corporation, such as debtholders.[66]

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58 *Toward Unlimited Shareholder Liability for Corporate Torts*, *supra* note 13, at 1916.

59 LYNN STOUT, *The Economic Nature of The Corporation*, *in* THE OXFORD HANDBOOK OF LAW AND ECONOMICS 337, 345 (Francesco Parisi ed., 2017).

60 *Id.* at 345.

61 David Ciepley, *Member Corporations, Property Corporations, and Constitutional Rights*, 11 LAW & ETHICS OF HUM. RTS. 31, 43 (2017).

62 *Id.*

63 *Id.* at 45.

64 *Id.*

65 LYNN STOUT, THE SHAREHOLDER VALUE MYTH 37 (2012).

66 *Id.* at 37–38.

Shareholders are also not principals to whom the directors owe duties as their agents.[67] A principal must "exist[] prior to, and independent of, the hiring of the agent."[68] In a corporation, however, it is only *after* the firm's incorporator appoints a board of directors to act on the corporation's behalf that the corporation has the power and ability to issue stock to shareholders.[69] Only the corporation and its board exist prior to the alleged principal —the shareholders.[70] Moreover, although shareholders have certain limited rights (to vote on certain corporate matters, sue the corporation, and sell shares), they do not control the corporation's behavior, a key component of agency.[71] To the contrary, the board of directors controls corporate actions.[72]

Hansmann and Kraakman, however, in the vein of Property Theory, treat shareholders as owners and principals of the corporation, and the corporate directors as the shareholders' agents.[73] They note the identical concern that both owners and shareholders may use the corporate form to limit their personal liability.[74] One can only harmonize these statements by arguing that they are in fact, identical—that shareholders are the owners of the corporation. Moreover, their argument suggests shareholder control such that they would, in fact, be principals. They contend that shareholders—not the corporation through its officers and directors—control the corporation's capitalization.[75] Only by ignoring the role of corporate directors are they able to conclude that corporations themselves should have no liability at all if shareholders have insufficient control over corporate managers of the corporation.[76] The board of directors and officers control corporate capitalization, not shareholders.[77] Shareholders

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67 *Id.* at 42.

68 *Id.*

69 *Id.*

70 *Id.*

71 *Id.*; *see* RESTATEMENT (THIRD) OF AGENCY § 3.04 (AM. L. INST. 2006).

72 ARTHUR R. PINTO & DOUGLAS M. BRANSON, UNDERSTANDING CORPORATE LAW 114 (4th ed., 2013).

73 *See The Essential Role of Organizational Law*, *supra* note 13, at 429.

74 *Compare The Essential Role of Organizational Law, supra* note 13, at 431 ("[O]rganizational law is essential to shield owners of an organization from personal liability."), *with Toward Unlimited Shareholder Liability for Corporate Torts, supra* note 13, at 1917 ("Shareholders . . . should not be able to avoid . . . costs simply by limiting the capitalization of their firm.").

75 *See Toward Unlimited Shareholder Liability for Corporate Torts, supra* note 13, at 1919.

76 *Id.* at 1908.

77 It is true that, subsequent to the issuance of shares, shareholders must normally vote on changes to a corporation's bylaws. *See* DEL. CODE ANN. tit. 8, § 109(a) (West 2020). The bylaws include the number of authorized shares a corporation may issue. *See* § 109(b) (Westlaw). One could argue that shareholders could derivatively control corporate

do not decide when to issue (or buy back) equity or debt, issue dividends, when and how to insure for contingent liabilities, or manage the corporation's working capital.[78] These actions fall exclusively within the purview of the corporation's board of directors and its management.[79] Only if one views the shareholder as a principal, can one suggest actual shareholder control of corporate assets—this is simply not the case in the corporation.[80] Finally, Hansmann and Kraakman's remedies also suggest a belief in shareholders as principals.[81] For example, they argue in favor of shareholder personal liability based on the corporation's management's awareness that a plaintiff will file a tort claim against the corporation.[82] Such vicarious liability ought only be imputed to the employee's principal, which is the corporation itself, not the shareholder.

A second theory on which Hansmann and Kraakman may rely is Aggregate Theory, which treats the corporation as an aggregation of natural persons.[83] Under this view, corporations are merely "composed" of human beings: "a form of organization used by human beings to achieve desired ends."[84] Aggregate Theory, similar to Property Theory, crucially fails to distinguish

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capitalization by rejecting a corporation's request for an increase in the number of authorized shares so that the corporation could raise equity to provide for adequate corporate capitalization. Such shareholder "control" of capitalization, however, is better described as within the vein of *ultra vires* (that is, notice to shareholders of the scope of the corporation) as opposed to actual control of corporate capitalization. *See* PINTO, *supra* note 72. Indeed, several examples show how such alleged corporate control is illusory. First, articles of incorporation may permit directors to adopt, amend, or repeal bylaws without shareholder approval. *See* § 141 (Westlaw). Second, the corporation (through the board of directors) does not need shareholder approval to purchase insurance (such as a credit default swap) which could achieve results similar to an equity issuance. *See id*. Finally, a corporation's board of directors does not require shareholder approval of a reverse stock split. *See* U.S. SEC. & EXCH. COMM'N, *Reverse Stock Splits*, (Aug. 16, 2020, 1:24 PM), https://www.investor.gov/introduction-investing/investing-basics/glossary/reverse-stock-splits [http://perma.cc/XDT2-PS4V]. A reverse stock split would reduce the number of shares outstanding, thereby allowing the corporation to issue sufficient equity for adequate capitalization. *See id*. Despite shareholders' limited control rights, corporate capitalization ultimately remains in hands of the board of directors, not shareholders.

78 *See* DEL. CODE ANN. tit. 8, §§ 141(c), 351 (West 2020).

79 *Id.* § 141(c).

80 True, such statements may not apply to controlling shareholders, who may derivatively control a corporation and as such are subject to fiduciary duties. *See* Iman Anabtawi & Lynn Stout, *Fiduciary Duties For Activist Shareholders*, 60 STAN. L. REV. 1255, 1269–70 (2008). I discuss strict liability for controlling shareholders in a subsequent section.

81 *See Toward Unlimited Shareholder Liability for Corporate Torts*, *supra* note 13, at 1897.

82 *See id.*

83 *See* STOUT, *supra* note 59, at 344–45.

84 Burwell v. Hobby Lobby Stores, Inc., 573 U.S. 682, 706 (2014).

the corporate form, with its separate personality, from partnerships or proprietorships.[85]

In the vein of Aggregate Theory, Hansmann and Kraakman treat the shareholders and the corporation as identical. They note separate yet equivalent concerns that shareholders, corporations, and owners should not be able to use limited liability to externalize costs.[86] These statements, when viewed together, ignore that the corporation is an entity distinct from its shareholders. Consider, for example, Hansmann and Kraakman's concern regarding a corporation's ability to limit its liability.[87] They do not suggest apprehension that a corporation can limit liability through the creation of a subsidiary.[88] Rather, they express a concern that a corporation can limit its liabilities through its own incorporation.[89] Corporations cannot limit liability differently than any natural person. Because a corporation owns itself and is its own principal, it will be vicariously liable for its agents' actions in tort.[90] Hansmann and Kraakman can only argue such corporate use of limited liability by treating the shareholder and corporation as identical.

Although Hansmann and Kraakman's basis for shareholder personal liability may be flawed, this does not necessarily indicate that their conclusions are wrong. Tort law may still suggest shareholder personal liability for corporate torts. The relevant question, as even Hansmann and Kraakman acknowledge, is whether shareholders have enough control over corporate managers to have a significant effect on the probability

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85 *See* STOUT, *supra* note 59, at 345.

86 *Compare The Essential Role of Organizational Law*, *supra* note 13, at 431 ("[O]rganizational law is essential to shield *owners* of an organization from personal liability.") (emphasis added), *with Toward Unlimited Shareholder Liability for Corporate Torts*, *supra* note 13, at 1917 ("*Shareholders* . . . should not be able to avoid . . . costs simply by limiting the capitalization of their firm.") (emphasis added), *and Toward Unlimited Shareholder Liability for Corporate Torts*, *supra* note 13, at 1919 ("[A]llowing *corporations* to avoid tort liability through the simple device of limited liability seems . . . highly suspect.") (emphasis added).

87 *See Toward Unlimited Shareholder Liability for Corporate Torts*, *supra* note 13, at 1919.

88 *See id.*

89 *Id.* ("We do not want to exaggerate our faith in tort law as a means of controlling behavior. It is a very rough and costly mechanism. But it usefully discourages the most severe forms of opportunistic cost externalization. Moreover, if any class of actors is likely to respond rationally to the deterrence incentives created by tort law, it is corporations and their shareholders. Similarly, if tort law is to have any role in shifting risks to low-cost insurers, then using it to shift risks to the equity market makes sense. *Consequently, allowing corporations to avoid tort liability through the simple device of limited liability seems, at the very least, highly suspect*.") (emphasis added).

90 RESTATEMENT (THIRD) OF AGENCY §§ 2.04, 3.04 (AM. L. INST. 2006).

that the corporation will commit a tort.[91] Although shareholders are neither principals nor owners of the corporation, and are distinct from the corporation itself, they do retain some control through their capacity to vote, sue, and sell shares.[92] What amount of control, if any, should render them liable in tort for corporate malfeasance?

III. RECONSIDERING SHAREHOLDER LIMITED LIABILITY IN TORT: INTUITION AND APPLICABILITY OF STRICT LIABILITY AND ABNORMALLY DANGEROUS ACTIVITIES

A. Strict Liability Provides an Appropriate Intuition for Shareholder Personal Liability for Corporate Torts

To answer the question of how tort law would deal with shareholder liability for corporate torts, we must first consider which relevant accident control regime—strict liability or negligence—would apply. Strict liability finds liability regardless of the tortfeasor's use of due care.[93] As such, it is meant to control care and activity levels, whereas negligence—the typical liability regime in tort—controls only care levels.[94] Care level refers to the level of care one can adopt when engaging in an activity, such as driving at a reasonable speed with reasonable caution.[95] Activity level, on the other hand, refers to the extent someone engages in an activity *at all*, such as how often one drives a car.[96] Although negligence and strict liability have the same effect on care levels—both incent an actor to take additional precaution to the extent that it is less than the expected costs of an accident—only a strict liability regime encourages an actor not to engage in the activity at all.[97]

Professor George Fletcher argues that strict liability rules should apply when an actor exposes another to non-reciprocal risks: an asymmetry where an actor's conduct endangers another, but the latter's conduct does not endanger the former.[98]

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91 *See Toward Unlimited Shareholder Liability for Corporate Torts*, *supra* note 13, at 1907–08.

92 *See generally*, Robert B. Thompson, *Preemption and Federalism in Corporate Governance: Protecting Shareholder Rights to Vote, Sell, and Sue*, 62 L. & CONTEMP. PROBS. 215, 216–17 (1999).

93 *See Liability*, BLACK'S LAW DICTIONARY (11th ed. 2019).

94 Keith N. Hylton, *Property Rules, Liability Rules, and Immunity: An Application to Cyberspace*, 87 B.U. L. REV. 1, 10 (2007).

95 *Id.*

96 *Id.*

97 *Id.* at 10–11.

98 *Cf.* PINTO, *supra* note 72, at 250.

Strict liability is alternatively, though similarly, described through a ratio test where the "costs externalized by an activity, even when conducted with reasonable care, substantially exceed the benefits externalized by that activity."[99] For example, two motorists driving past each other present one another with approximately equal risks. This is not the case, however, when a motorist drives past a blasting site and blasts shatter the motorist's window. The use of explosives presents the motorist with a non-reciprocal risk (and costs externalized far greater than benefits externalized), for which the defendant in charge of the blasting site ought to be strictly liable. Strict liability therefore incentivizes blasters not only to consider using proper care in blasting but also to decide where to blast (i.e., away from cars), and to explore the feasibility of using safer substitutes (like a wrecking ball).[100]

Strict liability offers an appropriate analogy to limited liability. First, by focusing on the activity level, it addresses academics' concern that incorporation permits shareholders to externalize too many costs onto society in relation to benefits. Strict liability would hold shareholders liable despite their exercise of reasonable care, thereby discouraging owning stock in a way that mere negligence cannot: incenting shareholders to consider other organizational forms where capital providers are personally liable (i.e., partnerships and proprietorships), or proceed as shareholders (with personal liability) at their own peril.[101]

Second, limited liability presents a non-reciprocal risk. Those persons with whom the corporation comes into contact (including both voluntary and involuntary creditors) are likely natural persons, with an assumed basic level of economic worth and earning capacity. The corporation, on the other hand, is by definition artificial and can easily exist without any such basic assumptions. The corporation could be a shell—completely worthless. Robert Monks aptly noted, "[t]he great problem of having corporate citizens is that they aren't like the rest of us."[102] "As Baron Thurlow in England is supposed to have said, 'they have no soul to save, and they have no body to incarcerate.'"[103] Perhaps this is Hansmann and Kraakman's actual concern

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99 Hylton, *supra* note 94, at 12.

100 *See* Ind. Harbor Belt R.R. Co. v. Am. Cyanamid Co., 916 F.2d 1174, 1177 (7th Cir. 1990); *see also* Hylton, *supra* note 94, at 12.

101 JOHN L. DIAMOND ET AL., UNDERSTANDING TORTS 249 (5th ed. 2013).

102 THE CORPORATION (Big Picture Media Corp. 2003).

103 *Id.*

regarding the corporate form: not that a corporation may be impecunious per se (because, judgment-proof natural persons similarly may leave uncompensated tort victims), but rather that their artificiality makes them (and their ownership of assets) distinctly unlike natural persons. Strict liability would address this non-reciprocal risk to society.

Third, strict liability still retains a proximate cause analysis.[104] Proximate cause is an additional limitation on a defendant's culpability which requires that the defendant be liable only if their conduct is not only the actual cause of the plaintiff's injury, but is also the cause as a matter of policy.[105] Proximate cause attempts to delimit a defendant's liability to the kind of harm the possibility of which makes the activity abnormally dangerous.[106] For example, in a famous strict liability case, a blasting operator who used reasonable care was not strictly liable to a plaintiff mink rancher whose mother mink trampled its kittens upon the vibrations resulting from the blasting.[107] Proximate cause precluded liability given that the plaintiff's mink ranching was an extraordinary and unusual use of his land.[108]

Conventional proximate cause analysis is consistent with shareholder personal liability. Even Hansmann and Kraakman would limit shareholder liability for corporate torts to tort damages that the corporation's assets cannot cover.[109] Inability to pay tort creditors due to corporate undercapitalization is exactly the type of harm that makes the corporate form dangerous. Specifically, the corporation and its shareholders would use limited liability to externalize costs onto others.

One particular Restatement form of strict liability—liability for abnormally dangerous activities—provides an intuitive framework for owning stock.[110] Although liability for abnormally

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104 *See* RESTATEMENT (SECOND) OF TORTS § 519(2) (AM. LAW INST. 1977).

105 DIAMOND ET AL., *supra* note 101, at 267.

106 RESTATEMENT (SECOND) OF TORTS § 519(2) (AM. LAW INST. 1977).

107 Foster v. Preston Mill Co., 268 P.2d 645, 646 (Wash. 1954).

108 *Id.* at 648.

109 *See Toward Unlimited Shareholder Liability for Corporate Torts*, *supra* note 13, at 1891–92.

110 *See* RESTATEMENT (SECOND) OF TORTS §§ 519–20 (AM. LAW. INST. 1977). True, one could argue that one should analyze shareholder strict liability under an analogy to the possession of livestock under the Restatement. How different, after all, is a psychopath from a wild animal? *Cf id.* § 504. My argument that owning stock is not an abnormally dangerous activity, however, would also—just as forcefully—indicate that owning stock under an analogy to livestock is not an activity for which a shareholder is strictly liable. Possessors of livestock are notably not strictly liable if the damages are "brought about by the . . . reckless or negligent conduct of a third person." *Id.* § 504(3)(c). A corporation's

dangerous activities attaches to ownership of tangible property or physical activity,[111] Hansmann and Kraakman argue that "limited liability encourages excessive entry and aggregate overinvestment in unusually hazardous industries"[112]—the exact same types of activities to which strict liability often attaches. Moreover, it is not unthinkable that a court could consider applying theories of strict liability to the ownership of intangible assets—academics have analyzed the possible application of tort doctrine, including strict liability, to such intangible ventures as the provision of Internet services.[113] Given these similarities, would shareholders be liable under this Restatement test? Should owning stock be considered an abnormally dangerous activity (or sufficiently analogous to it)?[114]

B. Is Owning Stock an Abnormally Dangerous Activity? Introducing the Restatement and *Indiana Harbor Belt*

Given the seeming compatibility between theories of strict liability and owning stock, it is worth exploring whether merely owning stock is sufficiently analogous to be considered an abnormally dangerous activity. The Restatement (Second) of Torts (Sections 519–20) gives a guideline for determining whether an activity is abnormally dangerous[115]:

> One who carries on an abnormally dangerous activity is subject to liability for harm to the person, land or chattels of another resulting from the activity, although he has exercised the utmost care to prevent the harm. . . .
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> . . . .
>
> . . . In determining whether an activity is abnormally dangerous, the following factors are to be considered:

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officers and directors are such third persons.

111 *See id.* § 520 cmt. f (noting that an activity must create a danger of physical harm in order to be abnormally dangerous).

112 *Toward Unlimited Shareholder Liability for Corporate Torts*, *supra* note 13, at 1883.

113 *See*, *e.g.*, Hylton, *supra* note 94, at 16, 28 (analogizing digital code to physical property in order to apply tort doctrine, including strict liability, to Internet-borne injuries).

114 Arguably shareholding's creation of physical harm is too derivative or too intangible to consider it an abnormally dangerous activity. *See* RESTATEMENT (SECOND) OF TORTS § 520 cmt. f (AM. LAW INST. 1977). However, as will become apparent, strict liability for abnormally dangerous activities crucially relies on a distinction between substances and activities. Such a distinction provides a strong analogy to the question of holding shareholders strictly liable for corporate torts and the conclusion that a negligence regime would apply.

115 *See id.* §§ 519–520.

> (a) existence of a high degree of risk of some harm to the person, land or chattels of others;
>
> (b) likelihood that the harm that results from it will be great;
>
> (c) inability to eliminate the risk by the exercise of reasonable care;
>
> (d) extent to which the activity is not a matter of common usage;
>
> (e) inappropriateness of the activity to the place where it is carried on; and
>
> (f) extent to which its value to the community is outweighed by its dangerous attributes.[116]

The Section 520 factors on their face seem to offer mixed guidance.[117] Some support the proposition that owning stock is abnormally dangerous.[118] With regard to factor (c), shareholders (in such capacity) generally cannot eliminate the risk of undercapitalization by the exercise of reasonable care given that the board of directors and other delegated managerial officers control corporate activities, including decisions concerning corporate capitalization.[119] Regarding factors (a) and (b), as mentioned, incorporation incentivizes investment in unusually hazardous industries which are inherently risky and potentially expose the corporation to massive tort liability for physical harm.[120] Moreover (although perhaps not an issue of locality), under factor (e), through analogy, incorporation is clearly not always the appropriate legal entity through which a business firm should conduct its activities.[121] In certain circumstances, such as when a corporation may be undercapitalized,[122] a partnership or proprietorship is clearly preferable in order to limit cost externalization.

Two factors are also unclear. Consider whether corporations are of common usage under factor (d). The Restatement comment on 'common usage' distinguishes between "automobiles [which] have come into such general use that their operation is a matter of common usage," and "the operation of a tank or any other motor vehicle of such size and weight as to be unusually difficult

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116 *Id.*

117 *See id.*

118 *See id.*

119 RESTATEMENT (SECOND) OF TORTS § 520(c).

120 *See* RESTATEMENT (SECOND) OF TORTS § 520(a–b); *see also The Essential Role of Organizational Law*, *supra* note 13, at 423, 431–32.

121 RESTATEMENT (SECOND) OF TORTS § 520(e).

122 A corporation is undercapitalized when it fails "in good faith [to] put at the risk of the business unincumbered [sic] capital reasonably adequate for its prospective liabilities." HENRY WINTHROP BALLANTINE, BALLANTINE ON CORPORATIONS 303 (rev. ed. 1946).

to control safely, or to be likely to damage the ground over which it is driven," which is "abnormally dangerous."[123] Should corporations be considered cars or tanks? One the one hand, if the corporation in fact behaves irresponsibility toward society at large, is it not akin to a tank on the road? On the other, corporations are ubiquitous—undercapitalized corporations arguably less so. Finally, with regards to factor (f), as discussed in the introduction, it is unclear whether incorporation (and therefore limited liability) provides the community more value than the danger it presents. The Section 520 factors on their face are either indeterminate or favor strict liability. Moreover, Section 519 requires that the defendant be in control of the alleged abnormally dangerous activity.[124] Do shareholders, through their limited control rights, have sufficient control over the corporation to be held strictly liable for corporate activity?

Indiana Harbor Belt Railroad Company v. American Cyanamid Co., a well-known strict liability case decided by Judge Richard Posner, helps shed light on both the Section 520 factors and Section 519 control.[125] In *Indiana Harbor Belt*, a chemical manufacturer, American Cyanamid Company ("Cyanamid"), leased a railroad tank car, filled it with a hazardous chemical (acrylonitrile), and shipped it.[126] A Missouri Pacific Railroad train picked up the car.[127] Later, at a small switching line within the Chicago metropolitan area, the switching line employees noticed fluid gushing from the bottom outlet of the car. [128] The Department of Environmental Protection subsequently ordered the switching line to take decontamination measures.[129] The switching line sued Cyanamid for the costs of those measures.[130]

The plaintiff argued that the transportation of acrylonitrile in bulk through the Chicago metropolitan area was an abnormally dangerous activity for which the manufacturer should be held strictly liable.[131] The plaintiff argued that the defendant, as an ordinary manufacturer and passive shipper of hazardous materials, should be incented through strict liability to explore alternative shipping routes through less populated

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123 RESTATEMENT (SECOND) OF TORTS § 520 cmt. i (AM. LAW INST. 1977).

124 *See* RESTATEMENT (SECOND) OF TORTS § 519.

125 Ind. Harbor Belt R.R. Co. v. Am. Cyanamid Co., 916 F.2d 1174 (7th Cir. 1990).

126 *Id.* at 1175 (describing acrylonitrile as "flammable at temperatures above 30 degrees Fahrenheit, highly toxic, and possibly carcinogenic.").

127 *Id.*

128 *Id.*

129 *Id.*

130 *Id.*

131 *Id.* at 1181.

areas.[132] According to the plaintiff's argument, introducing a hazardous chemical into a stream of commerce passing through the Chicago metropolitan area was enough to hold the manufacturer strictly liable.[133]

Judge Posner rejected this argument and, in doing so, elaborated on the Section 520 factors, in particular Section 520(c) (the inability to eliminate the risk by the exercise of reasonable care).[134] In his view, *someone* could have prevented the accident through the use of reasonable care:

> No one suggests . . . that the leak in this case was caused by the *inherent* properties of acrylonitrile. It was caused by carelessness—whether that of the [railroad tank car lessor] in failing to maintain or inspect the car properly, or that of Cyanamid in failing to maintain or inspect it, or that of the Missouri Pacific when it had custody of the car, or that of the switching line itself in failing to notice the ruptured lid, or some combination of these possible failures of care. Accidents that are due to a lack of care can be prevented by taking care; and when a lack of care can . . . be shown in court, such accidents are adequately deterred by the threat of liability for negligence.[135]

Judge Posner held that because proper care of tank cars made the danger of an acrylonitrile spill negligible, there was no compelling reason to move to a regime of strict liability.[136]

Judge Posner also helps us understand the bounds of Section 519 control. Throughout his opinion, Judge Posner emphasized that the relevant activity for determining liability was not the mere manufacture of a dangerous chemical, but rather its transportation.[137] To this end, he contrasted the defendant Cyanamid, the manufacturer-shipper, with the acrylonitrile carrier.[138] Although manufacturer-shippers can, in theory, designate in the bill of lading a route of shipment, shippers cannot be expected to become "students of railroading in order to lay out the safest route by which to ship their goods."[139] They, as manufacturer-shipper, were not the relevant controlling actor best suited to determine whether to reroute hazardous chemicals. That actor was the chemical carrier:

> [U]ltrahazardousness or abnormal dangerousness is, in the contemplation of the law at least, a property not of substances, but of

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132 *Id.*
133 *Id.* at 1175–80.
134 *Id.* at 1179.
135 *Id.*
136 *See id.*
137 *See id.* at 1181.
138 *Id.* at 1180.
139 *Id.*

> activities: not of acrylonitrile, but of the transportation of acrylonitrile by rail through populated areas. Natural gas is both flammable and poisonous, but the operation of a natural gas well is not an ultrahazardous activity. . . . [T]he manufacturer of a product is not considered to be engaged in an abnormally dangerous activity merely because the product becomes dangerous when it is handled or used in some way after it leaves his premises, even if the danger is foreseeable. . . . The relevant activity is transportation, not manufacturing and shipping.[140]

For these reasons, the manufacturer-shipper was held to be not strictly liable.[141]

Judge Posner went on to express skepticism that the imposition of strict liability would have actually changed the aggregate expected accident costs.[142] Even putting aside that rerouting would be prohibitively expensive—because new tracks would be needed to avoid metropolitan areas—it would require longer journeys over poorer quality tracks.[143] Though the cost of each individual accident may decrease, the probability of an accident may very well increase.[144]

Judge Posner did, in dicta, note that he could not exclude liability for the *Indiana Harbor Belt* defendant in certain hypothetical scenarios.[145] Were there a less hazardous chemical substitute (non-existent in this case), a manufacturer could be strictly liable for shipment.[146] Such an argument—relying on the inherent properties of acrylonitrile—would encourage the defendant to relocate the shipment or, more likely, reduce its scale by substitution.[147] This would be especially true in a jurisdiction that accepts the Restatement Section 521 view that because common carriers cannot refuse service to a shipper of a lawful commodity, they are exempt from strict liability for the carriage of abnormally dangerous materials.[148] Because of this exemption, the manufacturer is in a stronger relative position to consider whether to reroute its dangerous materials.[149] Moreover, Cyanamid's active participation in the chemical shipment by leasing and filling the tank car and contracting with the tank car

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140 *Id.* at 1181 (citations omitted).
141 *See id.*
142 *See id.* at 1179.
143 *See id.* at 1180.
144 *See id.*
145 *See id.* at 1178.
146 *See id.* at 1181.
147 *See id.*
148 *Id.* at 1180.
149 *See id.*

lessee to maintain the tank car indicates that the shipper was sufficiently engaged in the relevant activity of transportation.[150] At the same time, however, Judge Posner noted this active participation may not necessarily indicate that strict liability ought to apply: active participation "imposed upon [Cyanamid] a duty of due care and by doing so brought into play a threat of negligence liability that, for all we know, may provide an adequate regime of accident control in the transportation of this particular chemical."[151]

C. Is Owning Stock an Abnormally Dangerous Activity? Applying the Restatement and *Indiana Harbor Belt*

Indiana Harbor Belt provides valuable insight into whether owning stock is an abnormally dangerous activity. First, *Indiana Harbor Belt* makes clear that factor 520(c) (inability to eliminate the risk by the exercise of reasonable care) refers not just to any individual actor, but rather to that actor in the context of others.[152] In the context of the corporation, there normally *are* actors who can, through the use of reasonable care, mitigate the threat of cost externalization. Those actors are not the corporation's shareholders, but rather its officers and directors. Officers and directors control corporate activities and, most relevant to shareholder personal liability, corporate capitalization.[153] Like the carriers in control of a manufacturer's dangerous chemicals, officers and directors control shareholders' capital. When officers and directors use proper care, the risk that a corporation undercapitalizes and thereby leaves its tort creditors uncompensated becomes negligible.

Judge Posner's comments on adequate control under Section 519 of the Restatement also shed light on the relevant activity necessary for the imposition of strict liability.[154] Just as the manufacture of a volatile chemical merely constitutes the substance and its transportation the relevant activity, in the case of a corporation, stock ownership is the substance and corporate capitalization the activity. The relevant activity in the context of shareholder limited liability is not whether shareholders have provided (manufactured) the substance (capital) to the

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150 *Id.* at 1181. Because the district court and plaintiff's counsel ignored any distinction between a passive and active shipper and merely argued liability based on being the former, the court considered the distinction waived. *Id.*

151 *Id.*

152 *See id.* at 1177; *see also* RESTATEMENT (SECOND) OF TORTS § 520.

153 *See* DEL. CODE ANN. tit. 8 §§ 141–142 (West 2020).

154 Ind. Harbor Belt R.R. Co. v. Am. Cyanamid Co., 916 F.2d 1177 (7th Cir. 1990).

corporation, but rather how the corporation has decided to deploy capital (including any shareholder capital contribution). Though the manufacturer-shipper has some limited and derivative control over shipment of its chemicals, it ultimately entrusts the carrier to transport those chemicals in a specific manner. Shareholders in such capacity almost identically have limited control rights over their capital contribution but entrust their capital with the corporation's officers and directors with the hope that they will deploy it and obtain an acceptable return on such capital.[155] Even though it may be *foreseeable* that corporate officers and directors would deploy shareholder capital in a way that is dangerous (e.g., by undercapitalizing and externalizing costs onto third parties), shareholders in such capacity do not sufficiently engage in the activity to be strictly liable. Recall that even the decision whether to incorporate a firm (as opposed to creating a partnership) is in the hands of the board of directors, not shareholders.[156] A corporation must be in existence before its shareholders are created.[157] Shareholders are simply the manufacturer-shippers; corporate officers and directors are the carriers.[158]

Judge Posner's concern that strict liability is not applicable to the activity of transportation because it would not result in the desired lowering of expected accident costs rings true here as well.[159] Judge Posner noted that rerouting would increase the length of the journey over poorer track.[160] Just as rerouting would increase the length of the journey, shareholder personal liability would increase the cost of capital for projects.[161] Because raising capital would become more difficult, corporations would be incentivized to attempt identical projects with less capital (i.e., undercapitalize). Just as rerouting may lead to the use of poorer tracks[162], shareholder personal liability may lead to the contribution of inferior capital. Because debtholders retain limited liability, debt would become more favorable than equity, leading to excessive corporate leverage. Relatedly, an adverse selection problem may arise: poorer investors with fewer personal assets to lose will be more likely to invest as shareholders. So even if shareholders are personally liable, they

155 *See generally* DEL. CODE ANN. tit. 8, ch. 1 (West 2020).
156 STOUT, *supra* note 65, at 42.
157 *Id.*
158 *Indiana Harbor Belt*, 916 F.2d at 1177–78.
159 *Id.*
160 *Id.* at 1180.
161 *Id.*
162 *Id.*

may not ultimately have the personal capital available to satisfy tort creditors. Ultimately, it is unlikely that there will be fewer uncompensated tort victims with the imposition of shareholder personal liability.[163]

Although Judge Posner does list in dicta some factors that may have made Cyanamid (the manufacturer-shipper) more likely to be held strictly liable[164], they are not relevant to stock ownership. For example, he mentions the difference between an active and passive shipper.[165] One could argue that controlling or activist shareholders should in this vein be strictly liable given that they have adequate control over the corporation and thereby become more like a chemical carrier. Again, the key question is whether negligence liability would prove an adequate regime of accident control. Ultimately, the corporation's officers and directors still may use due care so as to make such accidents (that is, undercapitalization resulting in the externalization of costs) negligible. Judge Posner also mentions the possibility of strict liability if there were a less dangerous substitute for acrylonitrile and if the carriers were not held strictly liable for carrying lawful goods.[166] Given that capital is fungible and that a corporation may reject certain capital in exchange for shares, an argument for shareholder strict liability based on the availability of less dangerous substitutes is not meaningfully applicable.[167] The clear conclusion from the Restatement and *Indiana Harbor Belt* is that shareholders in tort are not strictly liable when corporations undercapitalize.[168] Negligence—the use of

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163 *See generally* Grundfest, *supra* note 19, *passim* (explaining that the imposition of personal liability onto shareholders is easily circumvented and will not have the intended effect of increasing the corporation's duty of care).

164 *See* 916 F.2d at 1180.

165 *Id.* at 1181.

166 *Id.* at 1180.

167 A situation where a shareholder could theoretically be strictly liable for his capital contribution would be if he had contributed not cash, but rather some sort of other asset with such illiquidity or volatility that it was ultimately worthless in the hands of the corporation directly leading to a corporation's undercapitalization. Consider, for example, an exotic derivative product with an active market before the financial crisis which after the crisis became worthless. True, holding such shareholders strictly liable may not be a feasible method of accident avoidance given that directors perhaps breach their duty of care by accepting such capital. Were directors, however, like common carriers—required to accept any type of legal capital for stock—there would be a strong argument for such shareholder strict liability in this limited hypothetical situation. Shareholders could easily avoid the accident (by contributing a liquid, low volatility asset like cash) and the corporation could not (by refusing to accept such capital contribution).

168 *See generally* Ind. Harbor Belt R.R. Co. v. Am. Cyanamid Co., 916 F.2d 1177 (7th Cir. 1990)*;* RESTATEMENT (SECOND) OF TORTS §§ 519-520.

reasonable care—provides a sufficient regime under which to prevent corporate undercapitalization.

IV. CORPORATE LAW COMPARED

How does corporate law's treatment of shareholder liability differ from the treatment under tort law? Under corporate law, shareholders are generally not personally liable to a corporation's creditors beyond their capital investment in the corporation.[169] This privilege, however, is not absolute.[170] Shareholders may become personally liable for a corporation's liabilities (including to tort creditors) under the equitable doctrine of piercing the corporate veil.[171] Though piercing the corporate veil is a poorly understood and hazy doctrine,[172] creditors successfully do so in certain limited circumstances. First, in all instances, the shareholders exert a high degree of control over the corporation.[173] Second, in the context of a tort claim, courts examine two general categories to determine liability: respect for corporate formalities and corporate capitalization.[174] Courts generally require finding both to pierce the corporate veil.[175]

Corporate formalities, in turn, may be grouped into legal, economic, and operational formalities.[176] Legal formalities include whether to issue stock certificates, hold meetings, elect officers, and document loans and other transactions.[177] Economic formalities refer to whether shareholders intermix their personal affairs with the corporation, such as failing to maintain a separate bank account for the corporation.[178] Operational formalities refer to whether the corporation and shareholder share offices, employees, or otherwise seem to operate identically.[179] To avoid undercapitalization and denial of separate entity privileges, "shareholders should in good faith put at the

169 *See, e.g*, Model Bus. Corp. Act § 6.22(b) (1985).

170 *See generally,* Robert B. Thompson, *Piercing the Corporate Veil: An Empirical Study*, 76 CORNELL L. REV. 1036 (1991).

171 *Id.* at 1036.

172 *Id.* at 1036–37.

173 *See* Kinney Shoe Corp. v. Polan, 939 F.2d 209, 212 (4th Cir. 1991).

174 *See id.* When the creditor is a contract creditor, courts often ask whether the debtor misled the contract creditor regarding the corporation's capitalization. *See* Easterbrook & Fischel, *supra* note 18, at 112.

175 *See Kinney Shoe Corp.*, 939 F.2d at 212.

176 *See id.* at 211–12 (grouping the factors identified in *Laya v. Erin Homes, Inc.* into three overarching categories).

177 *See id.*

178 *See id.*

179 *See id.* at 211.

risk of the business unincumbered [sic] capital reasonably adequate for its prospective liabilities."[180]

Analysis of tort law's treatment of limited liability sheds light on the hazy doctrine of piercing the corporate veil. The elements present in piercing the corporate veil perform the same function as those of tortious negligence. In order for a plaintiff to recover in a negligence action, he must establish (1) that the defendant owed the plaintiff a duty, (2) that the defendant breached this duty by failing to use reasonable care, (3) which was the cause-in-fact and proximate cause of (4) plaintiff's losses, or damages.[181] When a shareholder fails to respect corporate formalities and controls the corporation , he *personally* has assumed a duty of care to corporate creditors both actual (i.e., in contract) and contingent (i.e., in tort).[182] When a shareholder further undercapitalizes his corporation, thereby leaving a corporate creditor uncompensated, he breaches this duty by failing to use reasonable care. Such undercapitalization (a properly capitalized corporation would have been able to compensate reasonably the creditor)—the cause-in-fact and proximate cause of the plaintiff's loss—results in shareholder personal liability to the plaintiff creditor for the resulting damages.

True, under this framework, reasonable capitalization would still, at times, leave tort creditors uncompensated. But other corporate creditors (such as debtholders) are frequently left uncompensated. Though contract creditors were able, *ex ante*, to negotiate and price corporate risk, there is no fundamental difference in the price of risk (i.e., the risk of externalized costs) when one negotiates for actual financial debt as compared to appropriately insuring for contingent debt including debt owed to any potential tort creditor. Insurance performs the same *ex ante* function of risk pricing as the contract negotiation. Moreover, tort creditors of non-corporate natural persons are also, at times, ultimately uncompensated. The negligence regime merely forces a corporation—an artificial person—to mimic a natural one. A properly capitalized corporation faces no greater threat to society of externalizing costs than any other natural person. There is therefore no additional need in tort to force on the corporation's shareholders the task of providing the corporation with additional insurance beyond what the corporation reasonably requires.

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180 BALLANTINE, *supra* note 122, at 303.

181 DIAMOND ET AL, *supra* note 101, at 45.

182 Iman Anabtawi & Lynn Stout, *Fiduciary Duties for Activist Shareholders*, 60 STAN. L. REV. 1255, 1269 (2008).

One could argue that when a plaintiff successfully pierces the corporate veil, he normally may pierce the veil as to all shareholders, those more innocent and culpable alike.[183] This, in turn, indicates that hypothetically innocent shareholders are strictly liable for corporate torts and corporate undercapitalization.[184] As an example of a relatively innocent shareholder who would have been held liable, some point to *Minton v. Cavaney*.[185] In that case, two promoters created a corporation to lease a swimming pool but never capitalized it (it never had any assets) and failed to respect corporate formalities, such as issuing stock.[186] Cavaney, an attorney, assisted the two promoters in a temporary capacity as secretary, treasurer, and director of the corporation, likely as an accommodation to his client.[187] When a victim drowned in the pool, her survivors, after winning a judgment against the corporation, sued Cavaney's estate.[188] Although reversed on other grounds, the court would have found Cavaney personally liable, noting that he was to receive one-third of the shares to be issued and that Cavaney kept corporate records in his office.[189]

There are two problems with relying on *Minton* to conclude that innocent shareholders are "strictly liable" for corporate torts. First, when piercing the corporate veil, courts have normally not held truly passive shareholders personally liable.[190] Second, to the extent that relatively innocent shareholders are liable, such liability is within the vein of *Res Ipsa Loquitur*, a negligence claim, not strict liability. Normally, a plaintiff bears the burden of proving each element of a negligence cause of action by a preponderance of the evidence.[191] However, the doctrine of *Res Ipsa Loquitur* allows a plaintiff in limited situations to use circumstantial evidence to establish a defendant's unreasonable conduct.[192] It allows a jury to infer from that circumstantial conduct that a defendant acted unreasonably without any other proof.[193] The circumstantial evidence is crucial to plaintiffs who otherwise would be unable to make specific allegations about

183 PINTO, *supra* note 72, at 58–59.
184 *See id.*
185 *See id.* at 59.
186 Minton v. Cavaney, 56 Cal. 2d 576, 578–79 (1961).
187 *Id.* at 578.
188 *Id.*
189 *Id.* at 580.
190 *See* PINTO, *supra* note 72, at 59–60.
191 DIAMOND ET AL., *supra* note 101, at 73.
192 *Id.*
193 *Id.*

defendant malfeasance.[194] Under the Restatement (Third) of Torts, *Res Ipsa Loquitur* allows the factfinder to "infer that the defendant has been negligent when the accident causing the plaintiff's harm is a type of accident that ordinarily happens as a result of the negligence of a class of actors of which the defendant is the relevant member."[195] Put slightly differently, *Res Ipsa Loquitur* requires that the harm-causing event was probably due to negligence, and that the defendant was probably the culpable party.

The defendant's suggested liability in *Minton* arose in such a way. The harm—the corporation's failure to satisfy a tort creditor's judgment (i.e., undercapitalization)—was due to the board of directors' negligence (failure to use reasonable care in capitalizing the corporation).[196] Moreover, the defendant was probably a culpable party.[197] Judge Roger Traynor noted that "evidence that Cavaney was to receive one-third of the shares to be issued supports an inference that he was an equitable owner, and the evidence that for a time the records of the corporation were kept in Cavaney's office supports an inference that he actively participated in the conduct of the business."[198] The Defendant in *Minton* simply would have been unable to overcome these inferences (i.e., his burden): the defendant's relationship with the promoters and the corporation itself was enough to establish the inference that he had sufficient control (that is, the act was probably negligence) over the corporation to be personally liable to its creditors (that is, he was probably the culpable party).

Indeed, this is exactly a distinction Judge Posner discusses in *Indiana Harbor Belt* to highlight the difference between strict liability and negligence.[199] In *Indiana Harbor Belt*, Judge Posner contrasts *Siegler*, where the court imposed strict liability on a transporter of hazardous materials. There, a gasoline truck blew up, obliterating Plaintiff's decedent and decedent's car. The explosion destroyed the evidence necessary to establish whether the accident had been due to negligence.[200] Though the *Siegler* Plaintiff could have tried to base his claim in negligence through

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194 *Id.*

195 RESTATEMENT (THIRD) OF TORTS: LIAB. FOR PHYSICAL & EMOTIONAL HARM § 17 (AM. L. INST. 2010).

196 Minton v. Cavaney, 56 Cal. 2d 576, 578, 580 (1961).

197 *Id.* at 580.

198 *Id.* (emphasis added) (citation omitted).

199 *See* Ind. Harbor Belt R.R. Co. v. Am. Cyanamid Co., 916 F. 2d 1174, 1179–80 (7th Cir. 1990).

200 *Id.*

the doctrine of *Res Ipsa Loquitur*, the *Siegler* court turned to strict liability instead of *Res Ipsa Loquitur* because even if the defendant truck driver used all due care, a gasoline truck might well blow up without negligence on the part of the driver.[201] In such a case, a plaintiff would be unable to invoke *Res Ipsa Loquitur*. The Plaintiff switching lines in *Indiana Harbor Belt* did not show such a danger.[202]

Similarly, corporate undercapitalization does not present involuntary creditors with a risk that they could not otherwise prove fault without a strict liability regime. Though corporations may seem at times to "blow up," there is always an evidentiary record (or lack thereof) to show whether a shareholder respected corporate formalities and adequately capitalized the corporation. The piercing the corporate veil regime again follows this logic.

Res Ipsa Loquitur also helps illustrate the scope of piercing the corporate veil. Piercing only occurs within close corporations or within corporate groups, not public companies.[203] As the number of shareholders increase, the less likely it becomes that a court will pierce.[204] This is because, as *Res Ipsa Loquitur* suggests, with an increasing number of shareholders, it becomes more difficult for a tort plaintiff to suggest that the negligent conduct was probably tied to the particular shareholder defendant. Corporate law follows the logic tort law suggests: Shareholders are not strictly liable for corporate undercapitalization. They only become liable to the extent that they assume certain duties through the failure to respect corporate formalities and corporate control and then breach such duties by failing to use reasonable care in capitalizing the corporation.

V. CORPORATE PURPOSE RECONSIDERED

As discussed, the choice of regime between negligence and strict liability is one of comparison between externalized costs and benefits. When an activity externalizes more costs, strict liability ought to apply. When an activity externalizes more benefits, a negligence regime ought to apply.[205] The idea that shareholders ought not be strictly liable for corporate undercapitalization therefore implies that incorporation externalizes more benefits than costs.

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201 *Id.*
202 *Id.* at 1179–80.
203 *See* Thompson, *supra* note 170, at 1039.
204 *Id.*
205 *See* Hylton, *supra* note 94, at 14.

What is that externalized benefit? Shareholder provision of capital to corporations allows for the facilitation of optimal investment decisions.[206] Under Modern Portfolio Theory, investors can minimize risk through diversification. This minimization, in turn, allows corporations a lower cost of capital because a corporation's officers and directors need not consider non-systematic risk in making decisions. In a world of unlimited or strict shareholder liability, projects with a positive net present value ("NPV") i.e., those that would benefit society would be rejected because the value of shares would be based not merely on the present value of the corporation's expected future cash flows, but also something irrelevant to the investment decision: shareholder wealth. Piercing the corporate veil—a negligence regime—allows society to undertake NPV positive projects because incorporation allows a project to separate itself from its capital investors and stand on its own merits.[207]

Piercing the corporate veil, however, teaches that although corporations do externalize benefits to society, they still invite shareholder opportunism (that is, externalized costs) when certain shareholders attempt to use the corporate form to artificially limit liabilities to creditors. For this reason, in order for shareholders to truly limit their liability, they must follow corporate formalities and, if acting as a corporate officer and/or director, adequately capitalize the corporation. These actions not only allow the corporation to stand on its own merits, but also relieve the shareholder from a personal duty to corporate creditors. This is because such actions force the corporation to internalize the costs that it would otherwise externalize onto its creditors.

This is why—perhaps ironically—shareholders are only able to limit their liability when there is no *ex ante* value to limited liability. This is the case in a properly functioning corporation. True, *shareholders* may have an incentive to externalize these costs. Other corporate actors, however, have incentives not only *contra* the shareholders but also aligned with contingent (tort) creditors. Those actors typically mute any shareholder incentive to externalize costs. For example, because unsecured debtholders have a claim *pari passu* with a tort creditor, in exchange for debt capital, a debtholder will demand from the borrower and its subsidiaries an affirmative covenant to maintain reasonable

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206 *See* Easterbrook & Fischel, *supra* note 18, at 97.

207 Corp. Fin. Inst., *Modern Portfolio Theory (MPT)*, https://corporatefinanceinstitute.com/resources/knowledge/trading-investing/modern-portfolio-theory-mpt/ [http://perma.cc/YE36-L2X5] (last visited Mar. 10, 2021).

insurance.[208] This covenant is ubiquitous with the possible exception of investment-grade borrowers with multi-billion dollar market capitalizations—enough to cover potential losses arising from a corporate tort.[209] Without this covenant, the debtholder faces the material risk that a tort creditor's claim will dilute his or her own. Corporate officers and directors—who not only have a substantial human capital investment in the corporation but also may face personal liability for their action (or inaction)—will also push the corporation to adequately insure so as to protect their human capital investment and personal assets. Even if putatively improperly incentivized by ownership of stock and stock options, risk aversion will lead Corporate Officers and Directors to D&O insurance.[210] In turn, those insurers will increase their premiums in order to account for the costs of bad corporate governance. [211] As such, corporate actors are generally able to force the corporation to internalize otherwise externalized costs.[212]

Piercing the corporate veil is needed when the corporation is not properly functioning—specifically, when other corporate actors are unable to prevent shareholders from successfully attempting to extract value from limited liability.[213] To best understand when piercing the corporate veil applies, consider the relationship between shareholders and actual corporate creditors (namely debtholders), whose relationship can best be explained in terms of option theory. Both shareholders and debtholders have purchased a right to a corporation's future profits and concomitantly made agreements with each other. Debtholders have sold a call option (the right to purchase any increase in a corporation's value) on future profits to shareholders. Shareholders, meanwhile, have bought a put option from debtholders (that is, they have purchased the right to sell the corporation to debtholders). Shareholders pay for this put option

208 *See* MICHAEL BELLUCCI & JEROME MCCLUSKEY, THE LSTA'S COMPLETE CREDIT AGREEMENT GUIDE 339–40 (McGraw-Hill Educ. 2d ed. 2017).

209 *See id.*

210 *See* Lawrence J. Trautman & Kara Altenbaumer-Price, *D&O Insurance: A Primer* 1 AM. U. BUS. L. REV. 337, at 337, 366 (2011-2012).

211 *Id.*

212 *Id.* at 366. Perhaps the existence of more corporate actors—whose self-interest works to police contingent creditor claims—explains why tort creditors are less successful than contract creditors in piercing the corporate veil. *See* Thompson, *supra* note 170, at 1039–40, 1058–59.

213 Other corporate actors are unable to do so only in close corporations or within corporate groups—those places where courts exclusively pierce the corporate veil. *See* Thompson, *supra* note 170, at 1038–39.

through the terms of the corporate debt, including, but not limited to, the debt's interest rate, covenants, and tenor.

In the case of a tort creditor, piercing the corporate veil similarly prohibits shareholders from using the corporate form to obtain a free (or discounted) put option from contingent creditors (including potential tort creditors) with whom the corporation cannot negotiate *ex ante*.[214] It forces the corporation to internalize the risks it poses to tort creditors through some sort of insurance: either through contracting with a third-party insurer or through self-insurance (i.e., additional equity capital). This insurance performs the identical function as the *ex ante* negotiated purchase of a put option, in effect turning those involuntary creditors into voluntary creditors.[215] This is exactly why share prices of California corporations did not meaningfully change with the introduction of limited liability: corporations had already internalized costs so as to make the value of shareholder indemnity for corporate torts negligible.[216]

This understanding, in turn, helps us understand the extent of the NPV analysis discussed previously in the context of piercing the corporate veil. The NPV analysis ought to be performed not at the level of shareholder returns, but rather at the level of the corporate whole. Shareholders cannot use the corporate form to shield themselves artificially from liability to creditors. Said slightly differently, shareholders only risk losing limited liability by attempting to use the corporate form to make an otherwise negative NPV project into a positive one through the externalization of costs onto creditors. Such an action would without the doctrine of piercing the corporate veil (and unlike the California firms previously mentioned) result in an artificially higher share price through the externalization of costs onto others. Piercing the corporate veil allows creditors to make an enterprise stand on its own merits, which in turn requires those culpable shareholders to bear the realized costs of negative NPV projects.[217]

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214 *See* David K. Millon, *Piercing the Corporate Veil, Financial Responsibility, and Limits of Limited Liability*, 56 EMORY L. J. 1305, 1324 (2007).

215 *See* Easterbrook & Fischel, *supra* note 18, at 107–09.

216 *See* Weinstein, *supra* note 20, at 440.

217 This conclusion is analogous to the widely-adopted "Independent Investor" test which determines the eligibility of employee salary deductions under 26 U.S.C. § 162(a)(1). 26 U.S.C.A. § 162(a)(1) (West). Given that employee salaries are deductible but shareholders dividends are not, one who is both a shareholder and employee (usually in a closely-held company) may attempt to disguise a shareholder dividend as an employee salary in order to avoid incurring tax liability. The "Independent Investor" test guides the deductibility of employee-shareholder salaries by asking whether an independent third-party shareholder would accept the corporate stock's rate of return given the employee's

For this reason, in order for shareholders to avail themselves fully of limited liability, the corporation's NPV analysis must consider and adequately discount the costs not only of actual creditors, such as debtholders or trade creditors, but also *contingent* creditors, which include any potential tort creditor. Firms internalizing those risks (through more expensive insurance) will be less incented to engage in excessively risky activity. Moreover, by internalizing such risk, the corporation no longer imposes the risk of cost externalization onto involuntary creditors made possible by corporate undercapitalization.

Finally, this understanding of NPV, which requires that corporations consider not merely their shareholders, but also other corporate stakeholders in investment decisions, supports and augments another theory of the corporation.[218] According to stakeholder welfare theory, in calculating social benefits from corporate activity, the corporation should not focus merely on benefits to equity investors, but rather on other stakeholders like employees, customers, suppliers, and the community.[219] A corporation must, in considering a NPV analysis at the *corporate* level, look to maximize *corporate* welfare because each of these stakeholders is ultimately either an actual or contingent creditor. The corporation and its shareholders are free to maximize profits, but only to the extent that the corporation reasonably considers and mitigates the risks the corporate form presents to all stakeholders through undercapitalization.

VI. CONCLUSION

In this Article, I have argued that tort law would treat shareholder personal liability under a negligence regime and not strict liability, and that a negligence regime closely resembles the current corporate law regime. There are several important conclusions to draw from this argument, namely, that both advocates and critics of shareholder strict liability may be disappointed under a regime of strict shareholder personal liability. Advocates of limited liability may be disappointed by

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deducted salary. *See* Exacto Spring Corp. v. Comm'r of Internal Revenue, 196 F.3d 833, 838–39 (7th Cir. 1999). If so, the deduction is presumptively reasonable. *Id.* Just as shareholder-employees are incented to disguise dividends as salaries to avoid tax liability and increase their ultimate returns, an undercapitalizing shareholder foregoes necessary insurance premiums in an attempt to do the same. If, when accounting for reasonable insurance, an independent third-party shareholder would too find the corporate stock's rate of return too low, there could similarly be a presumption that a court should pierce the corporate veil.

218 *See* STOUT, *supra* note 65, at 38.

219 *See* STOUT, *supra* note 59, at 351.

the fact that the costs of capital are unlikely to rise substantially. Corporations can, through their officers and directors, use due care to prevent undercapitalization, just as the vast majority of chemical spills by railroads are preventable by due care. If this statement is true, strict liability should only cause a slight, not substantial, increase in the cost of capital because the incremental liability it would create would also be slight.[220] Similarly, critics of shareholder limited liability may not find strict shareholder personal liability to be the panacea they hope it to be given the only slightly increased incremental liability. Additionally, expected accident costs may not meaningfully change (or even increase), resulting in the same (or greater) incentive to externalize costs under the present regimes of shareholder limited liability.

This investigation presents two ideas for possible further areas of research. First, to the extent piercing the corporate veil differs from an action in negligence, corporate law may unnecessarily invite unwelcome opportunism through the current limited liability regime. Second, recall that Hansmann and Kraakman argue that limited liability is likely a historical accident. Perhaps there is a historical connection between the rise of strict liability and limited liability worthy of further study.

The corporate form ultimately benefits society but invites detrimental opportunism through its potential to externalize costs. Though at first glance it may be appealing to argue that shareholders ought to be personally liable for corporate torts given such potential, corporate law seems to correctly follow tort law in concluding that shareholders are not strictly personally liable for corporate torts—negligence applies; that is, the limited liability regime. Tort law does not justify itself based on finding the deepest pockets, but rather on asking which liability regime best addresses the relevant tort. It suggests that negligence, not strict liability, is the appropriate regime in tort for shareholders of a corporation. Corporate law correctly follows this intuition.

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220 *See* Ind. Harbor Belt R.R. Co. v. Am. Cyanamid Co., 916 F.2d 1174, 1179–80 (7th Cir. 1990).

Contract Interpretation and the Parol Evidence Rule: Toward Conceptual Clarification

*Joshua M. Silverstein**

Contract interpretation is one of the most important topics in commercial law. Unfortunately, the law of interpretation is extraordinarily convoluted. In essentially every American state, the jurisprudence is riddled with inconsistency and ambiguity. This causes multiple problems. Contracting parties are forced to expend additional resources when negotiating and drafting agreements. Disputes over contractual meaning are more likely to end up in litigation. And courts make a greater number of errors in the interpretive process. Together, these impacts result in significant unfairness and undermine economic efficiency. Efforts to remedy the doctrinal incoherence are thus warranted.

The goal of this Article is to clarify various legal concepts and principles that play a critical role in the interpretation caselaw and secondary literature. By untying some of the knots that entangle contract interpretation and the parol evidence rule, the Article will aid judges, lawyers, and professors in addressing interpretive issues in the contexts of adjudication, contract drafting, scholarship, and teaching.

This Article addresses the following seven issues: (1) the two types of latent ambiguity; (2) the many definitions of "parol evidence"; (3) the stages of contract interpretation; (4) determining whether a court is using textualism or contextualism; (5) contextualism and the ambiguity determination; (6) the circumstances in which contract interpretation raises a jury question; and (7) contextualism and the parol evidence rule.

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I. INTRODUCTION

Contract interpretation is one of the most important topics in commercial law.[1] It lies at the center of contract doctrine, which contains numerous rules that regulate the construction of agreements.[2] Interpretation is the subject addressed most often by contract lawyers, whether they are litigators or transactional attorneys.[3] And interpretive disputes constitute the largest source of contract litigation.[4]

The significance of contract interpretation explains why the field has received extensive academic attention since the turn of the century.[5] Indeed, the subject is recognized as "the least settled, most contentious area of contemporary contract doctrine and scholarship."[6]

Unfortunately, the law of contract interpretation is extraordinarily convoluted. "In virtually every jurisdiction, one finds irreconcilable cases, frequent changes in doctrine, confusion, and cries of despair."[7] The precise formulation of a

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1 *See* NEIL ANDREWS, *Interpretation of Written Contracts*, *in* ARBITRATION AND CONTRACT LAW: COMMON LAW PERSPECTIVES, 229, 230 (2016) ("The technique of construing written contracts is probably the most important topic within commercial contract law."); STEVEN J. BURTON, ELEMENTS OF CONTRACT INTERPRETATION § 1.1, at 1 (2009) ("Issues of contract interpretation are important in American law.").

2 *See* BENJAMIN E. HERMALIN ET AL., *Contract Law*, *in* 1 HANDBOOK OF LAW AND ECONOMICS 3, 68 (A. Mitchell Polinsky & Steven Shavell eds., 2007) ("The problem of contract interpretation thus provides a central backdrop for the law of contracts, which contains many rules and principles that are designed to address it."); Melvin Aron Eisenberg, *Expression Rules in Contract Law and Problems of Offer and Acceptance*, 82 CALIF. L. REV. 1127, 1127 (1994) ("The issue of interpretation is central to contract law, because a major goal of that body of law is to facilitate the power of self-governing parties to further their shared objectives through contracting.").

3 MICHAEL HUNTER SCHWARTZ & DENISE RIEBE, CONTRACTS: A CONTEXT AND PRACTICE CASEBOOK 463 (2009).

4 HERMALIN ET AL., *supra* note 2, at 68 ("Probably the most common source of contractual disputes is differences in interpretation. . . ."); Alan Schwartz & Robert E. Scott, *Contract Interpretation Redux*, 119 YALE L.J. 926, 928 & n.3 (2010) ("[C]ontract interpretation remains the largest single source of contract litigation between business firms.") (collecting authorities).

5 *See* Steven J. Burton, *A Lesson on Some Limits of Economic Analysis: Schwartz and Scott on Contract Interpretation*, 88 IND. L.J. 339, 340 (2013) ("After decades of relative neglect, contract interpretation became a hot topic of scholarly debate after 2003."); *id.* at 340 n.8 (collecting authorities); David McLauchlan, *Contract Interpretation: What Is It About?*, 31 SYDNEY L. REV. 5, 5 (2009) ("In recent times contract interpretation has become one of the most contentious areas of the law of contract.").

6 Ronald J. Gilson et al., *Text and Context: Contract Interpretation as Contract Design*, 100 CORNELL L. REV. 23, 25 (2014).

7 Eric A. Posner, *The Parol Evidence Rule, the Plain Meaning Rule, and the Principles of Contractual Interpretation*, 146 U. PA. L. REV. 533, 540 (1998); *accord* JOSEPH M. PERILLO, CALAMARI AND PERILLO ON CONTRACTS § 3.1, at 106 (6th ed. 2009) [hereinafter CALAMARI AND PERILLO] (noting that the courts do not consistently follow the

rule is frequently inconsistent with the way the rule is applied.[8] And courts often set forth inconsistent standards within a single opinion.[9] In fact, the caselaw is so muddled that commentators differ over which approach to interpretation—textualism or contextualism—is the majority rule.[10]

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rules of contract interpretation); *id.* § 3.2(b), at 110 n.29 (collecting secondary authorities that address the confused state of the law in Alaska, California, Illinois, Montana, Oregon, Texas, and Wisconsin, and further noting that "[o]ther jurisdictions could be cited"); RICHARD A. LORD, 11 WILLISTON ON CONTRACTS § 33:42, at 1191 (4th ed. 2012) [hereinafter WILLISTON] ("Not only do various jurisdictions disagree as to how and when extrinsic evidence of the circumstances surrounding the execution of a contract becomes admissible, but the decisions within a given jurisdiction are often difficult, and sometimes impossible, to reconcile on this point."). For my favorite "cry of despair," see Jake C. Byers, Inc. v. J.B.C. Investments, 834 S.W.2d 806, 811 (Mo. Ct. App. 1992).

8 *See* PETER LINZER, 6 CORBIN ON CONTRACTS § 25.14[A], at 148–61 (Joseph M. Perillo ed., rev. ed. 2010) (collecting examples).

9 *See id.* § 25.15[c], at 192 ("At times a state court seems to be saying contradictory things."); *id.* at 192–95 (discussing Wadi Petrol., Inc. v. Ultra Res., Inc., 65 P.3d 703, 706–10 (Wyo. 2003), to illustrate the problem); *see also infra* notes 253–270 and accompanying text.

10 *Compare* BURTON, *supra* note 1, § 4.3.2, at 126 ("Most courts follow the four corners rule when deciding whether a contract is ambiguous, sometimes . . . under the guise of the parol evidence rule."), *and* Schwartz & Scott, *supra* note 4, at 928 n.1 ("A strong majority of U.S. courts continue to follow the traditional, 'formalist' approach to contract interpretation. A state-by-state survey of recent court decisions shows that thirty-eight states follow the textualist approach to interpretation. Nine states, joined by the Uniform Commercial Code for sales cases (UCC) and the Restatement (Second) of Contracts, have adopted a contextualist or 'antiformalist' interpretive regime. The remaining states are indeterminate."), *with* 11 WILLISTON, *supra* note 7, § 30:5, at 80 ("While there is authority that the court is limited in its consideration solely to the face of the written agreement, many more courts take the position that a court may provisionally receive all credible evidence concerning the parties' intentions to determine whether the language of the contract is reasonably susceptible to the interpretation urged by the party claiming ambiguity; if it is, this evidence may then be admitted and heard by the trier of fact."). *See also* Lawrence A. Cunningham, *Contract Interpretation 2.0: Not Winner-Take-All but Best-Tool-for-the-Job*, 85 GEO. WASH. L. REV. 1625, 1630 (2017) ("[M]any states are classified as contextualist by one leading authority . . . and as textualist in another. . . .") (further noting that "the best explanation" for why scholars disagree over whether to classify a state as textualist or contextualist "is the inherent untidiness of the cases").

The picture appears to be clearer abroad, with contextualism now dominant both in other nations and in international law. *See* GERARD MCMEEL, THE CONSTRUCTION OF CONTRACTS: INTERPRETATION, IMPLICATION, AND RECTIFICATION § 2.01 (2nd ed. 2011) (explaining that the general trend in common-law jurisdictions is towards adoption of the contextualist approach); CATHERINE MITCHELL, INTERPRETATION OF CONTRACTS: CURRENT CONTROVERSIES IN LAW 58 (2007) (explaining that the same trend exists in European civil-law jurisdictions); *see also* United Nations Convention on Contracts for the International Sales of Goods, Apr. 11, 1980, at art. 8(3), http://www.uncitral.org/pdf/english/texts/sales/cisg/V1056997-CISG-e-book.pdf [http://perma.cc/7EPS-BFWY]; Unidroit Principles of International Commercial Contracts, at art. 4.3 (UNIDROIT INT'L INST. FOR THE UNIFICATION OF PRIVATE L. 2010), http://www.unidroit.org/english/principles/contracts/principles2010/integralversionprinciples2010-e.pdf [http://perma.cc/3MEX-K7HC]; *The Principles of European Contract Law*, at art. 5:102 (COMM'N ON EUR. CONT. L. 2002), http://www.jus.uio.no/lm/eu.contract.principles.parts.1.to.3.2002/ [http://perma.cc/2EU4-S8TN].

There are two primary theories as to the source of this disarray. Some believe that it results from courts failing to carefully distinguish between the principles of contract interpretation and the parol evidence rule.[11] Others suggest that it is because interpretation and the parol evidence rule cannot truly be distinguished.[12] I think both explanations have considerable validity. And I would supplement them with the point that textualism and contextualism are each supported by compelling policy arguments.[13] These arguments pull courts in opposite directions, sometimes resulting in judicial opinions that attempt to harmonize fundamentally incommensurable rules and normative theories—a recipe for unintelligible legal analysis.[14]

The inconsistency and ambiguity in the jurisprudence cause multiple problems. Contracting parties are forced to expend additional resources when negotiating and drafting agreements. Disputes over contractual meaning are more likely to end up in litigation. And courts make a greater number of errors in the interpretive process. Together, these impacts produce significant unfairness and undermine economic efficiency.[15] Efforts to remedy the doctrinal incoherence are thus warranted.

No single article—or even book—could entirely solve the puzzle that is the caselaw on contract interpretation and the parol evidence rule. But some scholars have made valiant efforts at bringing greater transparency to these subjects.[16] This Article is in that tradition. My goal here is to clarify various legal concepts and principles that play a critical role in the interpretation jurisprudence and secondary literature. By untying some of the knots that entangle contract

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11 *See, e.g.,* BURTON, *supra* note 1, § 3.1, at 64, and § 4.2.4, at 120; Margaret N. Kniffin, *Conflating and Confusing Contract Interpretation and the Parol Evidence Rule: Is the Emperor Wearing Someone Else's Clothes?*, 62 RUTGERS L. REV. 75 (2009) (discussing how courts and scholars confuse interpretation and the parol evidence rule and the injustice that results).

12 *See, e.g.*, CALAMARI AND PERILLO, *supra* note 7, § 3.9, at 128–29; Peter Linzer, *The Comfort of Certainty: Plain Meaning and the Parol Evidence Rule*, 71 FORDHAM L. REV. 799, 801 (2002).

13 *See* Joshua M. Silverstein, *Using the West Key Number System as a Data Collection and Coding Device for Empirical Legal Scholarship: Demonstrating the Method Via a Study of Contract Interpretation*, 34 J.L. & COM. 203, 261–84 (2016).

14 *See infra* Part VI. For an excellent example, see URI, Inc. v. Kleberg County, 543 S.W.3d 755 (Tex. 2018). I discuss this case briefly in footnote 265 *infra*.

15 *See* Kniffin, *supra* note 11, at 86 ("A central theme of this Article is that a clear distinction between the parol evidence rule and interpretation does exist but that in a significant proportion of cases, courts have indeed found themselves confused, have thereby ignored the distinction, and have thus reached unjust conclusions concerning admission or exclusion of evidence."); *id.* at 110–20 (collecting examples).

16 *See, e.g.*, BURTON, *supra* note 1; Kniffin, *supra* note 11.

interpretation and the parol evidence rule, this Article will aid judges, lawyers, and professors in addressing interpretive issues in the contexts of adjudication, contract drafting, scholarship, and teaching.

Part II sets forth a brief overview of contract interpretation and the parol evidence rule. Each of the next seven parts—Parts III through IX—analyzes a particular area of confusion in the caselaw and commentary.

Part III explains that there are two distinct types of latent ambiguity and that properly distinguishing between them allows for a more accurate description of textualism and contextualism.

Part IV identifies six different definitions of the term "parol evidence" that exist in the caselaw and argues that courts and commentators should cease using "parol evidence" because of the incoherence created by the term's multiple meanings.

Part V explains that the standard picture of textualism and contextualism as involving two stages—(1) the ambiguity determination, and (2) the resolution of ambiguity—critically oversimplifies the operation of each approach. Most importantly, textualism actually contains three substantive steps rather than two. And the number of steps involved in contextualism varies because there is more than one version of that system. Part V also addresses the relationship of the stages of interpretation to the three basic phases of civil litigation—(1) pleading, (2) discovery and summary judgment, and (3) trial.

Part VI discusses how inconsistent and vague language in judicial opinions regularly makes it impossible to determine which interpretive approach a court is endorsing or applying. Part VI also provides suggestions regarding how to address this problem, including a recommendation that judges and lawyers standardize their use of certain words frequently employed when describing the interpretive process.

Part VII demonstrates that contextualism's theory of language entails that all versions of this approach dispense with the ambiguity determination and substitute in its place a general assessment of the weight of the interpretive evidence.

Part VIII constructs a taxonomy of interpretive disputes and analyzes whether each type of dispute should be resolved by a judge as question of law or by a jury as question of fact under existing caselaw.

Part IX shows that, as conceptual matter, contextualism's elimination of the ambiguity determination does not automatically result in the evisceration of the parol evidence

rule, and that many contextualist jurisdictions have in fact retained the parol evidence rule.

Part X briefly concludes.

II. A BRIEF OVERVIEW OF CONTRACT INTERPRETATION AND THE PAROL EVIDENCE RULE

A. Contract Interpretation

Contract interpretation is the process of determining the meaning of the language of a contract.[17] The goal of contract interpretation is to ascertain the intent of the parties at the time the agreement was formed.[18] But accomplishing this task can be difficult. Party intent is often unclear and disputed.[19] And contracts frequently contain ambiguous language.

Contractual ambiguities exist for numerous reasons.[20] For example, parties typically lack the knowledge and foresight necessary to anticipate every contingency that might be worth addressing in their agreement.[21] Likewise, the stakes in most transactions do not justify the costly and protracted negotiations that are needed to carefully address all of the issues known to the parties.[22] Finally, and perhaps most fundamentally, language is simply an imperfect medium for expressing ideas.[23]

There are two general approaches to contract interpretation set forth in the caselaw.[24] These approaches have multiple names, but the most useful labels are "textualist" and

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17 RESTATEMENT (SECOND) OF CONTRACTS § 200 (AM. L. INST. 1981); E. ALLAN FARNSWORTH, CONTRACTS § 7.7, at 439 (4th ed. 2004).

18 BURTON, *supra* note 1, § 1.1, at 1 ("American courts universally say that the primary goal of contract interpretation is to ascertain the parties' intention at the time they made their contract."); *accord* 11 WILLISTON, *supra* note 7, § 30:2, at 17–18; CALAMARI AND PERILLO, *supra* note 7, § 3.13, at 136; *contra* Val D. Ricks, *The Possibility of Plain Meaning: Wittgenstein and the Contract Precedents*, 56 CLEV. ST. L. REV. 767, 807 (2008) (distinguishing between the intention of the parties and the meaning of words).

19 *See* George M. Cohen, *Interpretation and Implied Terms in Contract Law*, *in* 6 ENCYCLOPEDIA OF LAW AND ECONOMICS: CONTRACT LAW AND ECONOMICS 125, 130 (Gerrit De Geest ed., 2d ed. 2011) (discussing the uncertainty of party intent).

20 *See* FARNSWORTH, *supra* note 17, § 7.8, at 443–44 (setting forth a list).

21 BURTON, *supra* note 1, § 1.2.2, at 12–13.

22 *Id.* at 13.

23 CHARLES L. KNAPP ET AL., PROBLEMS IN CONTRACT LAW 382 (8th ed. 2016).

24 Gilson et al., *supra* note 6, at 25 ("Two polar positions have competed for dominance in contract interpretation.") (referring to textualism and contextualism); Shahar Lifshitz & Elad Finkelstein, *A Hermeneutic Perspective on the Interpretation of Contracts*, 54 AM. BUS. L.J. 519, 520 (2017) ("Two approaches dominate the debate over contract interpretation: the textualist and the contextualist.").

"contextualist."[25] Under textualism, interpretation focuses principally on the text of the parties' agreement.[26] The locus of contextualist interpretation is broader. While adherents of contextualism grant critical weight to the words set forth in the parties' contract,[27] contextualist interpretation emphasizes reading contractual language *in context*.[28] Thus, contextualist authorities focus on both the contract's express terms and extrinsic evidence.[29] Extrinsic evidence is evidence of contractual intent beyond the four corners of the parties' written agreement.[30] Such evidence includes preliminary negotiations, statements made at the time the contract was executed, the surrounding commercial circumstances (such as market conditions), course of performance, course of dealing, and usages of trade.[31]

Textualist jurisdictions follow what is typically called the "plain meaning rule" or "four corners rule."[32] That rule sets forth

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25 For other scholars that employ these two labels, see, for example, Cohen, *supra* note 19, at 131, 137, and Schwartz & Scott, *supra* note 4, at 928. For other approaches to labelling the two schools, see FARNSWORTH, *supra* note 17, § 7.12, at 465 ("restrictive" interpretation versus "liberal" interpretation); James W. Bowers, *Murphy's Law and the Elementary Theory of Contract Interpretation: A Response to Schwartz and Scott*, 57 RUTGERS L. REV. 587, 589–90 (2005) ("formalist" interpretation versus "contextualist" interpretation); *see also* Grumman Allied Indus., Inc. v. Rohr Indus., Inc., 748 F.2d 729, 733–34 (2d Cir. 1984) ("classical" interpretation versus "modern" interpretation).

26 *See Grumman Allied Indus.*, 748 F.2d at 733–34 ("Adherents of the classical approach, animated by a belief that a contractual agreement manifests the intent of the parties in a completely integrated form, favor the construction of contracts by reference to explicit textual language.").

27 Bowers, *supra* note 25, at 592 ("Words the parties expressly use play decisive roles in interpretation questions [for contextualist courts].").

28 *See Grumman Allied Indus.*, 748 F.2d at 734 ("Modern . . . interpretation . . . seems to derive from the premise that a contextual inquiry is a necessary and proper prerequisite to an understanding of the parties' intent.").

29 *See, e.g.*, Casey v. Semco Energy, Inc., 92 P.3d 379, 383 (Alaska 2004) ("[E]xtrinsic evidence is always admissible on the question of the meaning of the words of the contract itself."); RESTATEMENT (SECOND) OF CONTRACTS § 212 cmt. b (AM. L. INST. 1981) ("Any determination of meaning or ambiguity should only be made in the light of the relevant evidence of the situation and relations of the parties, the subject matter of the transaction, preliminary negotiations . . . , usages of trade, and the course of dealing between the parties.").

30 Nautilus Marine Enter., Inc. v. Exxon Mobile Corp., 305 P.3d 309, 316 (Alaska 2013); BURTON, *supra* note 1, § 3.1.1, at 68.

31 CALAMARI AND PERILLO, *supra* note 7, § 3.9, at 128–29. A "course of performance" is essentially the parties' conduct in performance of the contract at issue. *See* U.C.C. § 1-303(a). A "course of dealing" is the parties' conduct under prior contracts between them. *Id.* § 1-303(b). And a "usage of trade" is a practice or method of dealing in the industry or location where the parties operate that the parties should know about and should expect to be followed with respect to the contract at issue. *Id.* § 1-303(c). For an excellent overview of the types of extrinsic evidence, see BURTON, *supra* note 1, Ch. 2, at 35–62.

32 *See* MARGARET N. KNIFFIN, 5 CORBIN ON CONTRACTS § 24.7, at 33 (Joseph M. Perillo ed., rev. ed. 1998); Aaron D. Goldstein, *The Public Meaning Rule: Reconciling*

a two-stage process.[33] During the first stage, the court assesses whether the contract is ambiguous.[34] An ambiguity exists when the relevant contractual language is "reasonably susceptible" to more than one meaning.[35] The ambiguity determination is a question of law for the judge.[36] And in making that determination, the only evidence the judge may consider is the contract itself; the investigation is restricted to the "four corners" of the document.[37]

Two points of elaboration regarding stage one are in order. First, in assessing ambiguity, textualist courts generally interpret the document "in light of rules of grammar and the canons of construction."[38] They also use dictionaries.[39] It is only *evidence* from beyond the four corners that is forbidden.[40]

Second, when analyzing whether a contract is ambiguous, the question is not whether the agreement is ambiguous *per se*.

Meaning, Intent, and Contract Interpretation, 53 SANTA CLARA L. REV. 73, 75 (2013). Courts often use the descriptions "four-corners rule" and "plain meaning rule" synonymously. *See, e.g.*, *In re* Zecevic, 344 B.R. 572, 578 (Bankr. N.D. Ill. 2006); Gary's Implement, Inc. v. Bridgeport Tractor Parts, Inc., 702 N.W.2d 355, 376 (Neb. 2005); Benz v. Town Ctr. Land, LLC, 314 P.3d 688, 694 (N.M. Ct. App. 2013); *but see* BURTON, *supra* note 1, § 4.2.1, at 111, and § 6.3, at 224–25 (distinguishing the "four corners rule" from the "plain meaning rule"). And sources frequently distinguish between the "plain meaning rule" and the "context rule." *See, e.g.*, Brown v. Scott Paper Worldwide Co., 20 P.3d 921, 929 (Wash. 2001); Goldstein, *supra*, at 75. But some scholars use the phrase "plain meaning rule" more broadly to refer to both textualist authorities and most contextualist authorities. *See, e.g.*, CALAMARI AND PERILLO, *supra* note 7, § 3.10, at 129–30; FARNSWORTH, *supra* note 17, § 7.12, at 466.

33 FARNSWORTH, *supra* note 17, § 7.12, at 463.

34 *Id.*

35 KNIFFIN, 5 CORBIN ON CONTRACTS, *supra* note 32, § 24.7, at 33–34, 41–42 (explaining that both textualist and contextualist courts use this definition of ambiguity); *see, e.g.*, Pioneer Peat, Inc. v. Quality Grassing & Servs., Inc., 653 N.W.2d 469, 473 (Minn. Ct. App. 2002) (textualist decision); California Tchrs.' Ass'n v. Governing Bd. of Hilmar Unified Sch. Dist., 115 Cal. Rptr. 2d 323, 328 (Cal. Ct. App. 2002) (contextualist decision).

36 Quake Const., Inc. v. Am. Airlines, Inc., 565 N.E.2d 990, 994 (Ill. 1990); W.W.W. Assocs., Inc. v. Giancontieri, 566 N.E.2d 639, 642 (N.Y. 1990); Gulf Ins. Co. v. Burns Motors, Inc., 22 S.W.3d 417, 423 (Tex. 2000); CALAMARI AND PERILLO, *supra* note 7, § 3.10, at 131.

37 BURTON, *supra* note 1, § 4.2.2, at 111–12; KNIFFIN, 5 CORBIN ON CONTRACTS, *supra* note 32, § 24.7, at 33.

38 BURTON, *supra* note 1, § 4.3.2, at 126; *see generally id.* § 2.4, at 57–60 (surveying the canons of construction); FARNSWORTH, *supra* note 17, § 7.10, at 456–61 (same). Note that I generally use the terms "interpretation" and "construction" interchangeably throughout this Article. *See* FARNSWORTH, *supra*, § 7.7, at 439–40 ("This distinction between interpretation and construction is a difficult one to maintain in practice and will not be stressed here."); KNAPP ET AL, *supra* note 23, at 382 (same); *but see* JOHN EDWARD MURRAY, JR., MURRAY ON CONTRACTS § 87[A], at 447–48 (5th ed. 2011) (attempting to distinguish between interpretation and construction).

39 BURTON, *supra* note 1, § 2.1.2, at 38.

40 *Id.* § 4.3.2, at 126; *see also* Anchor Sav. Bank, FSB v. United States, 121 Fed. Cl. 296, 311 (2015) (explaining that dictionaries "are not considered extrinsic evidence").

Rather, the question is whether the contract is ambiguous as between the different interpretations presented by the parties in the case. In other words, the ambiguity determination is concerned with whether the language of the agreement is reasonably susceptible to the meanings *proffered by both parties*, not whether it is reasonably susceptible to *any* two (or more) potential meanings.[41] This is helpfully described by Professor Steven Burton as ambiguity "in the contested respect."[42]

For example, a contract stating that lumber must be delivered by "early December" is ambiguous where the buyer argues that the goods must arrive by the fifth of December and the seller contends that delivery is permissible up through the tenth of that month.[43] But if the seller instead asserts that the goods may arrive any time before January 1st, then the agreement is unambiguous as between the buyer's and the seller's interpretations. That is because the phrase "early December" cannot plausibly be understood to mean "any time before the first of January."[44]

If the court concludes that the contract is unambiguous, it simply applies the unambiguous, "plain meaning" of the language to the facts of the case.[45] The judge never reviews any extrinsic evidence.[46] And the case can be disposed of via a motion to dismiss, a motion for summary judgment, or some other pre-trial proceeding.[47]

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41 Agrigenetics, Inc. v. Pioneer Hi-Bred Int'l, Inc., 758 F. Supp. 2d 766, 771 (S.D. Ind. 2010) (applying Illinois law) ("Ambiguity exists only when *both parties* [sic] interpretive positions [are] reasonable.") (emphasis added and internal quotation marks omitted); Allen v. United States, 119 Fed. Cl. 461, 480 (2015) ("In order to demonstrate ambiguity, the interpretations offered by *both parties* must fall within a zone of reasonableness.") (emphasis added and internal quotation marks omitted).

42 BURTON, *supra* note 1, Ch. 4, at 105–06, and § 4.1, at 106.

43 This hypothetical is based upon *Donald W. Lyle, Inc. v. Heidner & Co.*, 278 P.2d 650, 653 (Wash. 1954).

44 *See also* William Blair & Co., LLC v. FI Liquidation Corp., 830 N.E.2d 760, 771 (Ill. App. Ct. 2005) ("In point of principle, the fact that a term is ambiguous in one context does not necessarily make it ambiguous in another."). Note also that "[a]n ambiguity does not arise simply because the parties advance conflicting interpretations of the contract." Columbia Gas Transmission Corp. v. New Ulm Gas, Ltd., 940 S.W.2d 587, 589 (Tex. 1996); *accord* CALAMARI AND PERILLO, *supra* note 7, § 3.10, at 131. An ambiguity exists only when the language is in fact reasonably susceptible to the meanings asserted by both parties. Finally, "[e]ven if both parties assert that a contract is unambiguous, a court may hold that a contract is ambiguous." Horseshoe Bay Resort, Ltd. v. CRVI CDP Portfolio, LLC, 415 S.W.3d 370, 377 (Tex. Ct. App. 2013); *see, e.g.*, Zeiser v. Tajkarimi, 184 S.W.3d 128, 133 (Mo. Ct. App. 2006) (finding contract ambiguous despite both parties arguing that it was unambiguous).

45 BURTON, *supra* note 1, § 4.2.3, at 118 ("If the document does not appear to be ambiguous, the analysis ends; the plain meaning rule comes into play to require that the judge give the unambiguous meaning to the contract as a matter of law.").

46 *Id.* ("No extrinsic evidence then is admissible for the purpose of giving meaning to

If the judge concludes that the contract is ambiguous, then interpreting the agreement moves to the second stage—resolving the ambiguity. At that stage, extrinsic evidence regarding the contract's meaning may be considered,[48] and interpretation is generally described as a question of fact.[49] However, if the parties do not submit any relevant extrinsic evidence, or if the textual and extrinsic evidence presented is so one-sided that there is no genuine issue of material fact regarding the contract's meaning, then the judge resolves the ambiguity as a matter of law, typically via summary judgment. If relevant extrinsic evidence is submitted *and* a reasonable jury could rule for either side, then the jury resolves the ambiguity at trial.[50]

Because textualist courts conduct the initial ambiguity determination without considering materials beyond the four corners of the document, the text of the contract is often the only evidence reviewed in ascertaining the meaning of the agreement. Hence the name of this interpretive school: "textualism."

Contextualism is generally understood as involving the same two-stage process.[51] But the contextualist approach differs in the method used to establish whether a contract is ambiguous. According to this view, both the language of the agreement *and* extrinsic evidence are relevant in deciding if an ambiguity exists.[52] In other words, at stage one, the judge must consider extrinsic evidence proffered by the parties—something prohibited by textualism. However, the ambiguity issue is still a question of

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the writing.").

47 Abundance Partners LP v. Quamtel, Inc., 840 F. Supp. 2d 758, 767 (S.D.N.Y. 2012); Seaco Ins. Co. v. Barbosa, 761 N.E.2d 946, 951 (Mass. 2002); Salewski v. Music, 54 N.Y.S. 3d 203, 205 (N.Y. App. Div. 2017).

48 BURTON, *supra* note 1, § 4.2.3, at 118 ("If the contract is ambiguous on its face, extrinsic evidence is admissible for [the] purpose [of interpreting the contract].").

49 *See, e.g.*, Seaco Ins. Co., 761 N.E.2d at 951; Archer v. DDK Holdings LLC, 463 S.W.3d 597, 606 (Tex. Ct. App. 2015).

50 *See* Nycal Corp. v. Inoco PLC, 988 F. Supp. 296, 299–300 (S.D.N.Y. 1997); Zale Constr. Co. v. Hoffman, 494 N.E.2d 830, 834 (Ill. App. Ct. 1986); RESTATEMENT (SECOND) OF CONTRACTS § 212(2) & cmt. e (AM. L. INST. 1981); BURTON, *supra* note 1, § 4.2.3, at 118; *id.* § 5.1.1, at 152–53; CALAMARI AND PERILLO, *supra* note 7, § 3.15, at 141–42. There is actually a division in the authorities regarding the standard for deciding whether the resolution of ambiguity is for the judge or the jury. I address this split in Part VIII.C *infra*.

51 *See* FARNSWORTH, *supra* note 17, § 7.12, at 466–67 (explaining that *Pac. Gas & Elec. Co. v. G.W. Thomas Drayage & Rigging Co.*, 442 P.2d 641 (Cal. 1968), the foundational and seminal contextualist case, endorsed the same two-stage process used by textualist authorities); BURTON, *supra* note 1, § 4.2.2, at 112–14; *see generally id.* § 4.1, at 106–20 (outlining both the textualist and contextualist approaches to the ambiguity determination).

52 BURTON, *supra* note 1, § 4.2.2, at 112.

law for the judge.[53] And it can be resolved via summary judgment, or at trial by holding an evidentiary hearing or ruling upon a motion for a directed verdict.[54] Note that while extrinsic evidence plays a larger role under contextualism than under textualism, contextualist authorities emphasize that the language of the contract remains the most important evidence in determining contractual meaning.[55]

Both textualist and contextualist courts generally consider all relevant extrinsic evidence at stage two once a contract is determined to be ambiguous.[56] The touchstone of their disagreement is whether

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53 *Id.* § 4.2.3, at 118–19.

54 BNC Mortg., Inc. v. Tax Pros, Inc., 46 P.3d 812, 819–20 (Wash. Ct. App. 2002), *overruled on other grounds by* Columbia Cmty. Bank v. Newman Park, LLC, 304 P.3d 472, 479 (Wash. 2013); BURTON, *supra* note 1, § 4.2.3, at 118–19.

55 *See, e.g.*, RESTATEMENT (SECOND) OF CONTRACTS § 212 cmt. b ("[T]he words of an integrated agreement remain the most important evidence of intention.").

56 BURTON, *supra* note 1, § 1.2.3, at 14 ("Under the prevailing law, all of the elements [of extrinsic evidence] are available after a court has determined that a contract is ambiguous."); *accord id.* Ch. 5, at 151; *id.* § 5.2, at 158; Schwartz & Scott, *supra* note 4, at 963 n.94 ("But what if there is a genuine ambiguity in the written agreement? In such a case, the divide between formalist and anti-formalist positions essentially disappears: a court will consider extrinsic evidence to resolve the ambiguity."); *see, e.g.*, Bank of New York Tr. Co., N.A. v. Franklin Advisers, Inc., 726 F.3d 269, 276 (2d Cir. 2013) (applying New York law) (textualist decision); Wagner v. Columbia Pictures Indus., Inc., 52 Cal. Rptr. 3d 898, 901 (Cal. Ct. App. 2007) (contextualist decision).

Note that there is a split in the courts over whether ambiguities should be resolved at stage two using a subjective standard of interpretation or an objective standard. 11 WILLISTON, *supra* note 7, § 31:1, at 354–55. "A standard of interpretation is the test applied by the law to words and to other manifestations of intention in order to determine the meaning to be given to them." RESTATEMENT (FIRST) OF CONTRACTS § 227 (AM. L. INST. 1932).

Objective standards focus on what a reasonable person would have understood the contract to mean at formation given the text and the relevant extrinsic evidence. *See* Neverkovec v. Fredericks, 87 Cal. Rptr. 2d 856, 867 (Cal. Ct. App. 1999) (explaining that the "trier of fact must decide how a reasonable person" standing in the "shoes" of the parties would have understood the contract); Behrens v. S.P. Constr. Co., Inc., 904 A.2d 676, 681 (N.H. 2006) ("An objective standard places a reasonable person in the position of the parties, and interprets a disputed term according to what a reasonable person would expect it to mean under the circumstances.").

Subjective standards focus on determining the actual intent of the parties. Accordingly, under subjectivism, the contract typically means what one or both of the parties in fact understood it to mean at formation. For example, the *Restatement (Second) of Contracts* adopts a three-part subjective test. *See* Lawrence M. Solan, *Contract as Agreement*, 83 NOTRE DAME L. REV. 353, 358–64 (2007) (explaining that the *Restatement (Second)* applies a subjective standard). First, if the text and extrinsic evidence establish that the parties shared the same understanding of ambiguous contractual language, that shared meaning governs even if a reasonable third party would read the language differently. RESTATEMENT (SECOND) OF CONTRACTS § 201(1); KNAPP ET AL., *supra* note 23, at 384. Second, if the parties understood the ambiguous language in different ways, then the subjective meaning of the party least at fault for the misunderstanding controls. RESTATEMENT (SECOND) OF CONTRACTS § 201(2); *see also* BURTON, *supra* note 1, § 2.5, at 62 (describing § 201(2) as a "fault rule"); FARNSWORTH, *supra* note 17, § 7.9, at 448–49 (same). Third, if the parties are equally at fault, then neither party's subjective

evidence may be considered during stage one in making the ambiguity determination.[57] In sum, under textualism, ambiguity must be apparent on the face of the agreement before extrinsic evidence of the context may be considered.[58] Such ambiguity is typically called "patent," "intrinsic," or "facial."[59] Under contextualism, extrinsic evidence of the context may be used to establish the existence of an ambiguity.[60] This type of ambiguity is typically called "latent" or "extrinsic."[61] Put simply—too simply as you will soon see[62]— textualism recognizes only patent ambiguities, whereas contextualism recognizes both patent and latent ambiguities.

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understanding is controlling, RESTATEMENT (SECOND) OF CONTRACTS § 201(3), and the disputed language is treated like a gap in the contract, see *id.* § 201 cmt. d. In deciding whether the parties had a shared meaning or whether one was more at fault than the other for a misunderstanding, the court considers all relevant extrinsic evidence. *Id.* § 202(1) ("Words and other conduct are interpreted in the light of *all* the circumstances. . . .") (emphasis added). (For a textualist case that employed the *Restatement (Second)* standard at stage two of the interpretive process, see *Joyner v. Adams*, 361 S.E.2d 902, 903–05 (N.C. Ct. App. 1987).)

There are multiple objective and subjective interpretation standards. *See* RESTATEMENT (FIRST) OF CONTRACTS § 227 cmts. a & b (identifying four objective standards and two subjective standards); *id.* § 227 cmt. c (observing that other standards exist beyond those six); 11 WILLISTON, *supra* note 7, § 31:1, at 339–41 (discussing the six standards set forth in the *Restatement (First)*). And it is unclear which standard is the majority view. *Compare* FARNSWORTH, *supra* note 17, § 7.9, at 447–48 (contending that the subjective standard set out in the *Restatement (Second)* is the dominate approach), *and* KNAPP ET AL., *supra* note 23, at 388 (same), *with* 11 WILLISTON, *supra*, § 31:1, at 341–42 (asserting that an objective standard is the majority rule), *and id.* § 31:2, at 366–67 & 367 n.12 (same and collecting case authorities). Fortunately, in most situations, the various interpretation standards will lead to the same meaning when applied to particular contractual language and extrinsic evidence. *See* RESTATEMENT (FIRST) OF CONTRACTS § 227 cmt. b (explaining that the six standards of interpretation discussed in the *Restatement (First)* will vary in result "only in exceptional cases"). That is because people generally understand language by applying the principles of standard English. Moreover, in my experience, judges often entirely ignore the question of which standard to apply when resolving ambiguities. *See, e.g.*, Frigaliment Imp. Co. v. B.N.S. Int'l Sales Corp., 190 F. Supp. 116 (S.D.N.Y. 1960). And the model jury instructions in some states do not even identify the applicable standard. *See, e.g.*, ARK. MODEL JURY INSTRUCTIONS—CIVIL 2412 to 2424 (2020).

57 Goldstein, *supra* note 32, at 80 ("The various jurisdictions then diverge as to what additional evidence [beyond the language of the contract] courts should consider to determine whether the contract is ambiguous."); *see also* BURTON, *supra* note 1, § 4.2.2, at 111 ("On the question of ambiguity, there is significant controversy among the courts.").

58 BURTON, *supra* note 1, § 4.2.2, at 111–12; *see, e.g.*, IDT Corp. v. Tyco Grp., 918 N.E.2d 913, 916 (N.Y. App. Div. 2009).

59 *See* Watkins v. Ford, 304 P.3d 841, 847 (Utah 2013); BURTON, *supra* note 1, § 4.1, at 107; FARNSWORTH, *supra* note 17, § 7.12, at 464.

60 BURTON, *supra* note 1, § 4.2.2, at 112; *see, e.g.*, Shay v. Aldrich, 790 N.W.2d 629, 641 (Mich. 2010).

61 BURTON, *supra* note 1, § 4.1, at 107; FARNSWORTH, *supra* note 17, § 7.12, at 464 & n.15.

62 See *infra* Part III.

While most scholars and many courts endorse this basic textualist/contextualist framework,[63] the framework is a considerable oversimplification of the jurisprudence.[64] Both contextualism and textualism can be subdivided in various ways.[65] And as a result of the complexity in the caselaw, most (or perhaps all) states fall somewhere along a continuum between textualism and contextualism, rather than firmly in one camp.[66] Finally, the law in some jurisdictions is simply too opaque to permit classification as either textualist or contextualist.[67]

B. The Parol Evidence Rule

The parol evidence rule begins with the concept of an "integration." An integration is a written document that is intended by the parties to constitute a final expression of one or more terms of their contract.[68] An integration is "partial" when it is intended to be final with respect to only *some* of the contractual terms.[69] An integration is "complete" when it is intended to be final with respect to *all* terms of the agreement.[70]

The parol evidence rule itself contains two pieces. First, the rule prohibits parties from introducing extrinsic evidence intended to prove contractual terms that *contradict* either type of integration and that were agreed upon prior to or contemporaneously with the execution of the integration.[71] Second, the rule prohibits parties from introducing extrinsic evidence intended to prove contractual terms that *add* to a complete integration and that were agreed upon prior to or contemporaneously with the execution of the integration.[72] Put

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63 For several examples, see *supra* note 25. *But see* Kniffin, *supra* note 11, at 95 (dividing the cases into three broad schools rather than two).

64 MCMEEL, *supra* note 10, § 1.31, at 22–23 (explaining that dividing the interpretation caselaw into literalist and purposivist schools is "too simplistic").

65 Silverstein, *supra* note 13, at 258–59; *see also infra* Part V.B.

66 Silverstein, *supra* note 13, at 259–60; Posner, *supra* note 7, at 553 ("No jurisdiction has a bright-line hard-PER [parol evidence rule] or soft-PER. Courts might state one or the other as a general rule, but all sorts of subsidiary doctrines provide exceptions."); *id.* at 534–35 (explaining that "hard-PER" and "soft-PER" refer to both contract interpretation and the parol evidence rule); *see also* Cunningham, *supra* note 10, at 1627 (explaining that "the law in many states . . . evades tidy classification as textualist or contextualist because, rather than wedded to one school, courts often choose the more suitable doctrine given the interpretation task at hand.").

67 Silverstein, *supra* note 13, at 301.

68 RESTATEMENT (SECOND) OF CONTRACTS § 209(1) (Am. L. Inst. 1981).

69 KNAPP ET AL., *supra* note 23, at 416.

70 RESTATEMENT (SECOND) OF CONTRACTS § 210(1).

71 *Id.* §§ 213(1), 215; KNAPP ET AL., *supra* note 23, at 413.

72 RESTATEMENT (SECOND) OF CONTRACTS §§ 213(2), 216(1); KNAPP ET AL., *supra* note 23, at 413.

simply, complete integrations bar evidence of both contradictory terms and consistent additional terms, whereas partial integrations only bar evidence of contradictory terms. An important corollary is that the parol evidence rule does *not* prohibit parties from introducing extrinsic evidence intended to prove contractual terms that supplement a partial integration.[73]

As with contract interpretation, parol evidence rule analysis involves a two-stage process.[74] At stage one, the court addresses whether the writing at issue is a complete integration, a partial integration, or not integrated at all.[75] Most authorities provide that this is a question of law for the judge.[76] If there is no integration, then the parol evidence rule is inapplicable.[77] If the document is a complete or partial integration, then the analysis moves to stage two, at which the court applies the parol evidence rule to bar evidence of contradictory terms and/or consistent additional terms,[78] which I will sometimes refer to together as "side terms."

There are two primary policy justifications for the parol evidence rule. First, final agreements supersede and render inoperative preliminary negotiations and tentative agreements. Evidence concerning the latter two categories is thus irrelevant.[79] Second, an integration is considered the best evidence of the parties' contract.[80] Therefore, the parol evidence rule gives a final writing "preferred status so as to render it immune to perjured testimony and the risk of 'uncertain testimony of slippery memory.'"[81]

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73 RESTATEMENT (SECOND) OF CONTRACTS § 216(1).

74 *See id.* §§ 209(2), 210(3).

75 MURRAY, *supra* note 38, § 84[D], at 423. Note that some authorities propose subdividing the first stage into two pieces: First, is the writing at issue an integration? Second, if so, is it partial or complete? *See, e.g.*, FARNSWORTH, *supra* note 17, § 7.3, at 419.

76 RESTATEMENT (SECOND) OF CONTRACTS § 209 cmt. c ("Ordinarily the issue whether there is an integrated agreement is determined by the trial judge in the first instance as a question preliminary . . . to the application of the parol evidence rule."); FARNSWORTH, *supra* note 17, § 7.3, at 425–26 ("However, most courts have favored resolution of these issues by the trial judge before the evidence goes to the jury."); BURTON, *supra* note 1, § 3.2.3.3, at 92.

77 CALAMARI AND PERILLO, *supra* note 7, § 3.3, at 112.

78 MURRAY, *supra* note 38, § 84[D], at 423.

79 CALAMARI AND PERILLO, *supra* note 7, § 3.2, at 107; LINZER, 6 CORBIN ON CONTRACTS, *supra* note 8, § 25.3, at 27.

80 KNAPP ET AL., *supra* note 23, at 416.

81 CALAMARI AND PERILLO, *supra* note 7, § 3.2(b), at 109 (quoting Charles T. McCormick, *The Parol Evidence Rule as a Procedural Device for Control of the Jury*, 41 YALE L.J. 365, 367 n.3 (1932)).

Several points of elaboration are necessary. First, the parol evidence rule is not a rule of evidence; it is a substantive rule of contract law.[82] Second, while "parol" means oral, the parol evidence rule applies to both oral and written extrinsic evidence of side terms.[83] Third, when the rule is applicable, it bars evidence of alleged prior or contemporaneous side terms regardless of whether the parties in fact agreed to those terms.[84] Fourth, the parol evidence rule does not apply to evidence (1) concerning terms agreed to *after* the execution of the integration,[85] (2) offered to *interpret* a contract,[86] or (3) presented to *invalidate* an agreement,[87] among other categories.[88]

Fifth, courts are divided over how to determine whether a writing is unintegrated, partially integrated, or completely integrated.[89] This split is comparable in structure to the interpretation division between textualism and contextualism. Some courts follow what I will call the classical approach to integration.[90] Under this approach, the judge analyzes only the four corners of the document in deciding whether the writing is a partial or complete integration.[91] And a merger clause

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82 RESTATEMENT (SECOND) OF CONTRACTS § 213 cmt. a (AM. L. INST. 1981); KNAPP ET AL., *supra* note 23, at 412.

83 RESTATEMENT (SECOND) OF CONTRACTS § 213 cmt. a; FARNSWORTH, *supra* note 17, § 7.2, at 416. However, the majority approach is that the parol evidence rule does not apply to *contemporaneous written* evidence. BURTON, *supra* note 1, § 3.1.1, at 64; CALAMARI AND PERILLO, *supra* note 7, § 3.2(a), at 108.

84 CALAMARI AND PERILLO, *supra* note 7, § 3.2, at 111.

85 BURTON, *supra* note 1, § 3.1.1, at 67; Kniffin, *supra* note 11, at 104.

86 RESTATEMENT (SECOND) OF CONTRACTS § 214(c).

87 *Id.* § 214(d); FARNSWORTH, *supra* note 17, § 7.4, at 427. These three contexts—(a) post-formation, (b) interpretation, and (c) invalidation—are frequently described as "exceptions" to the parol evidence rule. *See, e.g.*, KNAPP ET AL., *supra* note 23, at 418. But they are better conceived of as situations that are simply beyond the scope of the rule since in none of the three is evidence of prior or contemporaneous terms used to contradict or add to an integration. BURTON, *supra* note 1, § 3.1.1, at 66–67. Note, however, that the line between interpreting, on the one hand, and contradicting and adding, on the other hand, breaks down on the margins. *See infra* Parts VII, IX.

88 *See* RESTATEMENT (SECOND) OF CONTRACTS § 214; BURTON, *supra* note 1, § 3.3, at 93–104.

89 As Professor Burton has explained, "[t]he parol evidence rule itself does not determine what elements a court may consider when deciding the question of integration." BURTON, *supra* note 1, § 3.1.1, at 66; *accord* RESTATEMENT (SECOND) OF CONTRACTS § 214(a)–(b).

90 *See* Michael P. Van Alstine, *Of Textualism, Party Autonomy, and Good Faith*, 40 WM. & MARY L. REV. 1223, 1233–34 (1999).

91 *Id.*; CALAMARI AND PERILLO, *supra* note 7, § 3.4(a), at 113; KNAPP ET AL., *supra* note 23, at 417. The classical approach is often referred to as the "four-corners" approach. *See*, *e.g.*, CALAMARI AND PERILLO, *supra* note 7, § 3.4(a), at 113. I decided to use the "classical" label instead to avoid confusing the four-corners rule for *integration* with the four-corners rule for *ambiguity* that is the hallmark of textualist interpretation. *See supra* notes 32–37 and accompanying text.

conclusively establishes that the document is a complete integration unless the writing is obviously incomplete on its face.[92] This approach is akin to textualist contract interpretation.[93]

Other courts follow what I will call the modern approach to integration,[94] under which the judge considers both the text of the agreement *and* extrinsic evidence that bears upon whether the parties intended the writing to be final and complete.[95] The latter category includes evidence of the additional or contradictory term that might ultimately be excluded by the parol evidence rule if the court determines that the document is partly or completely integrated.[96] In modern states, a merger clause is powerful evidence that the agreement is a complete integration.[97] But it is not dispositive on this matter; instead, the clause is only a factor for the court to consider.[98] The modern approach to integration is akin to contextualist contract interpretation.

In parol evidence rule litigation, the level of integration "is often the key issue,"[99] as opposed to whether the proffered evidence contradicts or adds to the written agreement. Unfortunately, the integration caselaw is just as convoluted as

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92 BURTON, *supra* note 1, § 3.2.3.1, at 78–79; CALAMARI AND PERILLO, *supra* note 7, § 3.6, at 122; KNAPP ET AL., *supra* note 23, at 417. A "merger clause"—also known as an "integration clause"—is a contractual provision stating that "the writing is intended to be final and complete; all prior understandings are deemed to have been 'merged' into or superseded by the final writing." KNAPP ET AL., *supra* note 23, at 417 (also setting forth an example of such a clause).

93 *See also* KNAPP ET AL., *supra* note 23, at 432 ("Courts that rely on the facial completeness of a written contract to conclude that it is fully integrated are likely to rely on the apparent plain meaning of words to bar use of extrinsic evidence to aid interpretation. . . .").

94 *See* Jason Blumberg, *Bringing Back the Yard-Man Inference*, 4 U. PA. J. LAB. & EMP. L. 195, 204 (2001).

95 RESTATEMENT (SECOND) OF CONTRACTS § 209 cmt. c (AM. L. INST. 1981); *id.* § 210 cmt. b; *id.* § 214 cmt. a; KNAPP ET AL., *supra* note 23, at 417.

96 MURRAY, *supra* note 38, § 85[B], at 426 ("Thus, for a court to determine whether the agreement is integrated, it will have to receive (provisionally) the same extrinsic evidence that the parol evidence rule will bar if the court determines that the writing is integrated.").

97 RESTATEMENT (SECOND) OF CONTRACTS § 216 cmt. e (stating that a merger clause is "likely to conclude the issue whether the agreement is completely integrated"); *see, e.g.*, King v. Rice, 191 P.3d 946, 950 n.17 (Wash. Ct. App. 2008) (explaining that "integration clauses are strong evidence of integration").

98 RESTATEMENT (SECOND) OF CONTRACTS § 216 cmt. e (explaining that a merger clause does not "control" whether a writing is completely integrated); KNAPP ET AL., *supra* note 23, at 417; *see, e.g.*, *King*, 191 P.3d at 950 n.17 (stating that integration clauses "are not operative if they are factually incorrect").

99 CALAMARI AND PERILLO, *supra* note 7, § 3.4, at 113.

the caselaw on interpretation.[100] Courts employ a wide variety of tests along a continuum from classical to modern.[101] The authorities within many states are in conflict over the governing standard.[102] And commentators disagree over which approach is the majority view nationwide.[103]

Courts are also divided on the question of what constitutes "contradicting" a contract rather than merely "adding" to one,[104] which implicates stage two of the parol evidence analysis. For example, under the Uniform Commercial Code ("U.C.C."), some decisions provide that evidence of a side term contradicts an integration when there is an "absence of reasonable harmony" between the extrinsic evidence and the written agreement as a whole.[105] Other cases state that a contradiction exists only when there is a direct conflict between the alleged side term and a term in the integration.[106]

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100 *See* FARNSWORTH, *supra* note 17, § 7.3, at 423 ("Surprisingly little light is shed on the problem by the hundreds of decisions resolving the issue of whether an agreement is completely integrated.").

101 *See* BURTON, *supra* note 1, § 3.2.3, at 77–93; CALAMARI AND PERILLO, *supra* note 7, § 3.4, at 113–20; *id.* § 3.6, at 122–23; MURRAY, *supra* note 38, § 85, at 423–441; *see also* FARNSWORTH, *supra* note 17, § 7.3, at 421 ("The sharpest disagreement in connection with the parol evidence rule has been over the application of this test [for completeness]."); *id.* at 422 ("The point in dispute is whether the fact that the writing appears on its face to be a complete and exclusive statement of the terms of the agreement establishes conclusively that the agreement is completely integrated.").

102 BURTON, *supra* note 1, § 3.2.3, at 78 ("The courts employ all three approaches [to integration] at different times, even within a particular jurisdiction.").

103 *Compare* BURTON, *supra* note 1, § 3.1.1, at 67 (concluding that "most courts hold, that parol evidence may be admitted for the purpose of showing that an agreement is or is not integrated"), *and* FARNSWORTH, *supra* note 17, § 7.3, at 420 (identifying the modern approach to integration as "the prevailing view"), *with* LINZER, 6 CORBIN ON CONTRACTS, *supra* note 8, § 25.7, at 59 (explaining that "an examination of recent cases raises doubts" over Professor Farnsworth's conclusion).

104 CALAMARI AND PERILLO, *supra* note 7, § 3.5, at 121–22; 11 WILLISTON, *supra* note 7, § 33:29, at 1064–66.

105 Apex LLC v. Sharing World, Inc., 142 Cal. Rptr. 3d 210, 222–23 (Cal. Ct. App. 2012) (internal quotation marks omitted); *accord* 2 LARY LAWRENCE, LAWRENCE'S ANDERSON ON THE UNIFORM COMMERCIAL CODE § 2-202:28 [Rev], at 572 (3d ed. 2012).

106 Apex LLC, 142 Cal. Rptr. 3d at 222–23; 2 LAWRENCE, *supra* note 105, § 2-202:28, at 572. Note that this split in the caselaw is centered on the first paragraph of U.C.C. § 2-202 and on § 2-202(b), which together govern side parol terms generally. *See* Apex LLC, 142 Cal. Rptr. 3d at 223 (referring to § 2-202(b)). There is a separate split concerning course of performance, course of dealing, and trade usage, which are governed by §§ 1-303 and 2-202(a). *See* Joshua M. Silverstein, *Contract Interpretation Enforcement Costs: An Empirical Study of Textualism versus Contextualism Conducted Via the West Key Number System*, 47 HOFSTRA L. REV. 1011, 1075–82 (2019) (outlining this division in the authorities).

In their ideal forms, contract interpretation and the parol evidence rule address distinct but closely related subjects. The law of interpretation governs the process for determining the *meaning* of the terms of a contract. The parol evidence rule governs whether evidence of prior or contemporaneous terms may be used to *contradict* or *add* to a written agreement.[107]

III. ISSUE 1: THE TWO TYPES OF LATENT AMBIGUITY

In the overview of contract interpretation in Part II.A., I summarized the difference between textualism and contextualism as follows: Textualism recognizes only patent ambiguities, whereas contextualism recognizes both patent and latent ambiguities.[108] Many other scholars have described the two approaches to interpretation in those terms.[109] But as I also said in Part II.A., this conceptualization somewhat oversimplifies matters. In part, that is because textualist courts *do* recognize one type of latent ambiguity—what one might call a "subject-matter latent ambiguity."[110]

A subject-matter latent ambiguity is an ambiguity that results when the language of the contract is applied to the real world—to the subject matter of the agreement.[111] The Idaho Supreme Court explained the concept this way: "A latent

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107 Kniffin, *supra* note 11, at 90 ("When courts interpret a contract, they seek to discover the parties' intention concerning the meaning of a particular term found within the contract. When courts apply the parol evidence rule, in contrast, they seek to discover the parties' intentions concerning whether a particular prior or contemporaneous term was agreed to be added to the main, written contract.").

108 *See supra* text accompanying note 62.

109 *See, e.g.*, BURTON, *supra* note 1, § 4.1, at 108 ("Most courts, however, recognize intrinsic but not extrinsic ambiguities . . . . Some courts recognize both intrinsic and extrinsic ambiguities."); *id.* § 4.2.2 at 111–12 ("The classical view is that . . . a court may find that the contract is ambiguous only if it finds an intrinsic ambiguity . . . . Two rival views . . . recognize the possibility of an extrinsic ambiguity."); *id*. at 115 (calling the two rivals views "objective contextualism" and "subjective contextualism"); KNAPP ET AL., *supra* note 23, at 432 ("While all courts will allow use of extrinsic evidence to interpret a contract with a patent or facial ambiguity, the point of difference is that 'plain meaning' adherents will not allow use of extrinsic evidence to uncover latent ambiguity."); BEN TEMPLIN, CONTRACTS: A MODERN COURSEBOOK 503 (2d ed. 2019) ("A classic jurisdiction considers only patent ambiguities, while a modern jurisdiction considers both patent and latent ambiguities."). I also used this description in my first article concerning contract interpretation. *See* Silverstein, *supra* note 13, at 257–58.

110 A second reason this conceptualization oversimplifies is that contextualism actually dispenses with the ambiguity determination entirely. *See infra* Part VII.

111 Midkiff v. Castle & Cooke, Inc., 368 P.2d 887, 894 (Haw. 1962) ("An ambiguity may arise from words which are plain in themselves, but uncertain when applied to the subject matter of the instrument.").

ambiguity exists where an instrument is clear on its face, but loses that clarity when applied to the facts as they exist."[112]

The paradigms of subject-matter latent ambiguity are where language in a contract is intended to identify a single item in the world, but instead (1) two or more items fit the description, or (2) nothing in the world fits the description.[113] A classic example is the case of *Raffles v. Wichelhaus*.[114] There, the parties' contract provided that certain cotton would arrive on the ship "Peerless."[115] But there were two ships with that name, creating an ambiguity that only became apparent when the language of the agreement was applied to the subject matter of the contract—the cotton on the ship "Peerless."[116] Another helpful illustration was offered in an opinion of the Texas Supreme Court: "[I]f a contract called for goods to be delivered to 'the green house on Pecan Street,' and there were in fact two green houses on the street, it would be latently ambiguous."[117] This hypothetical contract would also suffer from a subject-matter latent ambiguity if there were *no* green houses on Pecan Street.[118]

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112 Knipe Land Co. v. Robertson, 259 P.3d 595, 601 (Idaho 2011); *accord* Charter Oil Co. v. Am. Emps.' Ins. Co., 69 F.3d 1160, 1167 (D.C. Cir. 1995) ("Latent ambiguity can arise where language, clear on its face, fails to resolve an uncertainty when juxtaposed with circumstances in the world that the language is supposed to govern.").

113 *See* 32A C.J.S. *Evidence* § 1454 (2008) ("The most common form of a latent ambiguity arises where an instrument or writing contains a reference to a particular person or thing and is thus apparently clear on its face, but it is shown by extrinsic evidence that there are two or more persons or things to whom or to which the description in the instrument might properly apply. Where a grant is issued to a certain person, but no person of that name ever existed, it is a case of latent ambiguity and evidence is admissible to show who was the person intended. . . ."); *see also* Univ. City, Mo. v. Home Fire & Marine Ins. Co., 114 F.2d 288, 295–96 (8th Cir. 1940) ("A latent ambiguity may be one in which the description of the property is clear upon the face of the instrument, but it turns out that there is more than one estate to which the description applies; or it may be one where the property is imperfectly or in some respects erroneously described, so as not to refer with precision to any particular object."); Williams v. Idaho Potato Starch Co., 245 P.2d 1045, 1048–49 (Idaho 1952) ("Where a writing contains a reference to an object or thing . . . and it is shown by extrinsic evidence that there are two or more things or objects . . . to which [the writing] might properly apply, a latent ambiguity arises . . . .").

114 159 Eng. Rep. 375 (Exch. 1864).

115 *Id.*

116 *Id. See also* RESTATEMENT (SECOND) OF CONTRACTS § 214 illus. 4 (AM. L. INST. 1981) ("A and B make an integrated contract by which A promises to sell and B to buy goods 'ex Peerless.' Evidence is admissible to show that there are two ships of that name, which one each party meant, and, in case of misunderstanding, whether either had knowledge or reason to know of the other's meaning.").

117 Nat'l Union Fire Ins. Co. of Pittsburgh, PA v. CBI Indus., Inc., 907 S.W.2d 517, 520 n.4 (Tex. 1995).

118 Subject-matter latent ambiguities frequently arises in contracts that contain real estate descriptions. *See, e.g.*, Meyer v. Stout, 914 N.Y.S.2d 834, 836–37 (N.Y. App. Div. 2010) (holding that a deed for the sale of land contained a latent ambiguity because an

In both the *Peerless* case and the Pecan Street hypothetical, the contract language was perfectly clear; there was no patent ambiguity.[119] But once the language of the agreement was applied to circumstances in the world, the language became unclear; it could no longer adjudicate between the parties' constructions, just as in the case of patent ambiguity. Which boat named "Peerless"? Which green house on Pecan Street? The ambiguities here are "latent" because they cannot be seen via an examination of the four corners of the contract. The ambiguity remains hidden until one considers extrinsic evidence regarding the subject matter of the transaction. Accordingly, "subject-matter latent ambiguity" is an apt description of this type of ambiguity.

As a conceptual matter, textualist jurisdictions have no choice but to allow for subject-matter latent ambiguities. Judge Richard Posner explains: "The contract's words point out to the real world, and the real world may contain features that make seemingly clear words, sentences, and even entire documents ambiguous."[120] It should thus not be surprising that numerous authorities from textualist states recognize this type of latent ambiguity, including cases from New York,[121] Texas,[122]

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easement description set forth in the deed improperly referenced property that the seller did not actually own); Emerald Pointe, L.L.C. v. Jonak, 202 S.W.3d 652, 659 (Mo. Ct. App. 2006) ("Where an uncertainty in the description of land conveyed does not appear upon the face of the deed but evidence discloses that the description applies equally to two or more parcels, a latent ambiguity is said to exist and extrinsic evidence or parol evidence is admissible to show which tract or parcel of land was intended.") (internal quotation marks and citations omitted); Warren v. Tom, 946 S.W.2d 754, 758 (Mo. Ct. App. 1997) ("A latent ambiguity in the description of land in a deed or mortgage is an uncertainty not appearing on the face of the instrument, but which is shown to exist for the first time by matter outside the writing, when an attempt is made to apply the language to the ground.") (internal quotation marks and citations omitted); 32A C.J.S. *Evidence* § 1454 (2008) ("Latent ambiguities also arise through the difficulty in applying to the land itself a description thereof contained in a written instrument . . . .").

119 For the Pecan Street hypothetical, assume away any issues regarding green shading into other colors. While the color green is patently ambiguous in marginal cases, the Texas Supreme Court presumably had in mind the core meaning of the concept "green," not a hue on the periphery.

120 Richard A. Posner, *The Law and Economics of Contract Interpretation*, 83 TEX. L. REV. 1581, 1597–98 (2005) (citing *Raffles v. Wichelhaus*).

121 *See, e.g.*, Teig v. Suffolk Oral Surgery Assocs., 769 N.Y.S.2d 599, 600 (N.Y. App. Div. 2003) ("Even where an agreement seems clear on its a face, a 'latent ambiguity' may exist by reason of 'the ambiguous or obscure state of extrinsic circumstances to which the words of the instrument refer.'") (quoting Lerner v. Lerner, 508 N.Y.S.2d 191, 194 (1986)); *see also In re* S.E. Nichols Inc., 120 B.R. 745, 748 (Bankr. S.D.N.Y. 1990) (applying New York law) ("Although parol evidence is inadmissible to vary or contradict the terms of a written contract, it is properly admitted for the purpose of identifying the subject matter of the agreement.").

122 *See, e.g.*, Friendswood Dev. Co. v. McDade + Co., 926 S.W.2d 280, 282–83 (Tex.

Oklahoma,[123] Missouri,[124] and Idaho.[125] Indeed, in my research on contract interpretation, I have yet to come across a textualist state that does *not* permit the use of extrinsic evidence to establish the existence of a subject-matter latent ambiguity.[126]

One additional point of clarification is in order. Recall the notion of ambiguity "in the contested respect" discussed above: An agreement is not ambiguous merely because it is amenable to more than one construction in the abstract. Instead, an ambiguity exists only when the contract is reasonably susceptible to the meanings asserted by both parties.[127] This requirement applies to subject-matter latent ambiguities.[128] To illustrate, in the *Peerless* case, the contract plausibly referred to either of the two ships named "Peerless." But suppose that one of the parties contended that the agreement identified the first "Peerless" and the other party argued that the contract identified a ship named "Titanic." On those facts, the agreement would not suffer from a subject-matter latent ambiguity in the contested respect and thus a court would deem the contract unambiguous.

Non-subject-matter latent ambiguities—the type that should be recognized only by contextualist jurisdictions—occur when the contracting parties use a word or phrase in an unconventional way. This second category of latent ambiguities might usefully be described as "non-standard-meaning latent ambiguities."

Contract interpretation is generally concerned with standard meanings—the meanings established by standard

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1996) ("A latent ambiguity exists when a contract is unambiguous on its face, but fails by reason of some collateral matter when it is applied to the subject matter with which it deals."); Security Sav. Ass'n v. Clifton, 755 S.W.2d 925, 930 (Tex. Ct. App. 1988) ("However, it is well established that parol evidence is admissible for the purpose of applying the contract to its subject matter even where the contract is not ambiguous.").

123 *See, e.g.*, Eureka Water Co. v. Nestle Waters N. Am., Inc., 690 F.3d 1139, 1152–53 (10th Cir. 2012) (applying Oklahoma law) (explaining that subject-matter latent ambiguities are an exception to the general rule that extrinsic evidence may not be used to interpret a facially unambiguous contract).

124 *See, e.g.*, Finova Cap. Corp. v. Ream, 230 S.W.3d 35, 49 (Mo. Ct. App. 2007) ("An ambiguity is . . . latent if language, which is plain on its face, becomes uncertain upon application.").

125 *See, e.g.*, Knipe Land Co. v. Robertson, 259 P.3d 595, 601 (Idaho 2011) ("Although parol evidence generally cannot be submitted to contradict, vary, add or subtract from the terms of a written agreement that is deemed unambiguous on its face, there is an exception to this general rule where a latent ambiguity appears.").

126 *See also* 32A C.J.S. *Evidence* § 1513 (2008) ("Parol evidence may be admissible where it is necessary in order to identify, explain, or define the subject matter of a grant, mortgage, contract, or other writing, or where it is necessary to apply the instrument or a description therein to its subject matter and to enable the court to execute it.").

127 *See supra* notes 41–44 and accompanying text.

128 *See* BURTON, *supra* note 1, § 4.1, at 106–07.

definitions of words and the basic rules of grammar. Put another way, the interpretation of contracts focuses on the meaning of language as used in ordinary English.[129] That helps to explain why textualist states restrict the ambiguity determination to the four corners of the agreement, dictionaries, and certain rules of construction:[130] Those are arguably the only tools needed to address whether the ordinary meaning of a contract is unclear.

But words can have alternative definitions, and those definitions are sometimes used in agreements. The *Restatement (Second) of Contracts* explains:

> Parties to an agreement often use the vocabulary of a particular place, vocation or trade, in which new words are coined and common words are assigned new meanings. . . . Moreover, the same word may have a variety of technical and other meanings. "Mules" may mean animals, shoes or machines; a "ram" may mean an animal or a hydraulic ram; "zebra" may refer to a mammal, a butterfly, a lizard, a fish, a type of plant, tree or wood, or merely to the letter "Z."[131]

We can call these alternative definitions "non-standard meanings," "non-standard definitions," or "special meanings." Under contextualism, evidence of a non-standard meaning may be used to establish a latent ambiguity.[132]

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129 RESTATEMENT (SECOND) OF CONTRACTS § 202 cmt. e (AM. L. INST. 1981) ("In the United States the English language is used far more often in a sense which would be generally understood throughout the country than in a sense peculiar to some locality or group. In the absence of some contrary indication, therefore, English words are read as having the meaning given them by general usage, if there is one."); *see also* Leachman v. Beech Aircraft Corp., 694 F.2d 1301, 1307 (D.C. Cir. 1982) ("In interpreting a contract, a court will presume that the parties intended the words to have the meaning they have in ordinary English usage unless there is some reason to believe the parties had a different one in mind."); Gabriel v. Gabriel, 152 A.3d 1230, 1243 (Conn. 2016) ("[T]he language used [in a contract] must be accorded its common, natural, and ordinary meaning and usage where it can be sensibly applied to the subject matter of the contract[.]"); Harkless v. Laubhan, 219 So. 3d 900, 904 (Fla. Dist. Ct. App. 2016) ("We interpret contracts in accordance with their plain and ordinary meaning when the contractual language is clear and unambiguous."); Penn Ins. & Annuity Co. v. Kuriger, 495 S.W.3d 540, 546 (Tex. Ct. App. 2016) ("We give words and phrases their ordinary and generally accepted meaning, reading them in context and in light of the rules of grammar and common usage."); East Texas Copy Sys., Inc. v. Player, 528 S.W.3d 562, 566 (Tex. Ct. App. 2016) ("Contract terms are given their plain and ordinary meaning unless the instrument indicates a different meaning is intended by the parties.").

130 *See supra* note 37 and accompanying text (identifying the materials textualist courts may consider at stage one of the interpretive process).

131 RESTATEMENT (SECOND) OF CONTRACTS § 202 cmt. f (AM. L. INST. 1981).

132 Kent Greenawalt, *A Pluralist Approach to Interpretation: Wills and Contracts*, 42 SAN DIEGO L. REV. 533, 591 (2005) (explaining that contextualist authorities "permit evidence of context that would lead a reasonable outsider viewing the contract to assign a meaning that was *different from the standard meaning*.") (emphasis added); *see, e.g.*, ACL Techs., Inc. v. Northbrook Prop. & Cas. Ins. Co., 22 Cal. Rptr. 2d 206, 219 (Cal. Ct. App. 1993) ("[C]ourts should allow parol evidence to explain *special* meanings which the

The archetype of a non-standard-meaning latent ambiguity is where the parties allegedly used special industry terminology in drafting their contract.[133] Consider the case of *Western States Construction Co. v. United States*.[134] There, the issue was whether a contract provision concerning "metallic pipes" applied to pipes made of cast iron.[135] The court explained that while "the dictionary definition of 'metallic pipes' would embrace [cast iron pipes]," a latent ambiguity was established by extrinsic evidence of an industry trade usage that the phrase "metallic pipes" excludes pipe made of cast iron.[136] In other words, contextual

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individual parties to a contract may have given certain words.") (emphasis in original).

133 *See* 12 WILLISTON ON CONTRACTS § 34:1, at 8–9 (4th ed. 2012) ("Indeed, often terms that are unambiguous on their face may be ambiguous or have a different meaning as a matter of fact, as when the terms have both an ordinary meaning and a special trade meaning."); *id.* § 34:5, at 45–50 ("[N]umerous cases have been decided in which words with a clear normal meaning were shown by usage to bear a meaning which was not suggested by the ordinary language used. . . . Therefore, evidence of usage may be admissible to give meaning to apparently unambiguous terms of a contract when other parol evidence would be inadmissible.") (collecting authorities); *see also* Alexander v. Buckeye Pipe Line Co., 374 N.E.2d 146, 151 (Ohio 1978) (explaining that trade usage evidence "is permissible to show that the parties to a written agreement employed terms having a special meaning within a certain geographic location or a particular trade or industry, not reflected on the face of the agreement"); Scapa Tapes N. Am., Inc. v. Avery Dennison Corp., 384 F. Supp. 2d 544, 550 (D. Conn. 2005) ("However, even where language of a commercial contract is unambiguous, testimony concerning trade custom and usage may be offered to define terms that have a technical meaning within a particular [industry]."); Emp. Television Enters., LLC v. Barocas, 100 P.3d 37, 43 (Colo. Ct. App. 2004) ("In deciding whether usage of trade evidence makes a term ambiguous, a court should first consider any evidence of trade usage that proposes an alternative definition. Thus, trade usage evidence is admissible even if the language is plain and unambiguous on its face, as long as the evidence is sufficient to suggest an alternative meaning."); RESTATEMENT (SECOND) OF CONTRACTS § 220 cmt. d ("Hence usage relevant to interpretation is treated as part of the context of an agreement in determining whether there is ambiguity or contradiction as well as in resolving ambiguity or contradiction. There is no requirement that an ambiguity be shown before usage can be shown, and no prohibition against showing that language or conduct have a different meaning in the light of usage from the meaning they might have apart from the usage."); *id.* § 222(3) ("Unless otherwise agreed, a usage of trade in the vocation or trade in which the parties are engaged or a usage of trade of which they know or have reason to know gives meaning to or supplements or qualifies their agreement."); U.C.C. § 1-303(d) ("A . . . usage of trade . . . is relevant in ascertaining the meaning of the parties' agreement, may give particular meaning to specific terms of the agreement, and may supplement or qualify the terms of the agreement."); Schwartz & Scott, *supra* note 4, at 962 ("Contests over the meaning of contract terms thus follow a predictable pattern: one party claims that the words in a disputed term should be given their *standard dictionary meaning*, as read in light of the contract as a whole, the pleadings, and so forth. The counterparty argues either that the contract term in question is ambiguous and extrinsic evidence will resolve the ambiguity, or that extrinsic evidence will show that the parties intended the words to be given a *specialized or idiosyncratic meaning* that varies from the meaning in the standard language.") (emphasis added).

134 26 Cl. Ct. 818 (1992).

135 *Id.* at 820.

136 *Id.* at 824–26.

evidence supported the conclusion that the parties did not use the standard meaning of "metallic" in their contract. Instead, they employed a non-standard or technical meaning specific to their field of trade.

Corbin on Contracts offers another helpful example: In the baking industry, the word "dozen" means something different (thirteen) than it does in ordinary English (twelve). Hence, the expression "baker's dozen." Suppose a contract between a baker and a customer uses the word "dozen." The ordinary meaning of that term is unambiguous. But once the interpreter considers extrinsic evidence from the baking industry, "dozen" now appears reasonably susceptible to more than one meaning—twelve *or* thirteen.[137]

As with the *Peerless* case and the Pecan Street hypothetical, the contract language was perfectly clear in *Western States* and the baker's dozen example. Neither agreement suffers from a patent ambiguity. But when extrinsic evidence of the trade usage was considered, the language became unclear. Which definition of "metallic" or "dozen" did the parties intend: The standard meaning or the special industry meaning? Once again, the ambiguities here are "latent" because they cannot be seen through an analysis of the four corners of the contract. The ambiguity remains hidden until one considers extrinsic evidence supporting the conclusion that the parties used a non-standard meaning. Accordingly, "non-standard-meaning latent ambiguity" is an apt description of this type of ambiguity.[138]

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137 *See* KNIFFIN, 5 CORBIN ON CONTRACTS, *supra* note 32, § 24.13, at 118.

138 For some additional examples of non-standard meanings, see RESTATEMENT (SECOND) OF CONTRACTS § 220 illus. 8 ("A leases a rabbit warren to B. The written lease contains a covenant that at the end of the term A will buy and B will sell the rabbits at '60 [Pounds Sterling] per thousand.' The parties contract with reference to a local usage that 1,000 rabbits means 100 dozen. The usage is part of the contract.") (based upon Smith v. Wilson, 3 B. & Ad. 728, 110 Eng. Rep. 266, 1832 WL 4162 (K.B. 1832)); *id.* § 222 illus. 6 ("A and B enter into a contract for the purchase and sale of 'No. 1 heavy book paper guaranteed free from ground wood.' Usage in the paper trade may show that this means paper not containing over 3% ground wood.") (based upon Gumbinsky Bros. Co. v. Smalley, 197 N.Y.S. 530 (N.Y. App. Div. 1922), *aff'd* 139 N.E. 758 (N.Y. 1923)); *see also infra* notes 317–322 and accompanying text (discussing these and other examples and setting forth multiple sources collecting authorities).

Note that non-standard-meaning latent ambiguities are distinguishable from undefined technical and industry terms that appear on the face of an agreement and possess no ordinary meaning. Courts rightfully treat the latter situation as constituting a type of *patent* ambiguity. For example, in *Rogers & Sons, Inc. v. Santee Risk Managers, L.L.C.*, an insurance policy contained "Coldfire" requirements. 631 S.E.2d 821, 823 (Ga. Ct. App. 2006). "Coldfire" has no meaning in common usage; the word is not contained in any general or legal dictionaries that I checked. It is "the trade name of a fire suppression product." *Id.* at 823. And the insurance policy did not define the term. *Id.* at 824. This

The two types of latent ambiguity are different in critical respects. Subject-matter latent ambiguities do not implicate alternative definitions of words. Instead, they result from a disconnect between the standard meaning of the contract terms and facts in the real world, such as where two items fit a contractual description that is presumed to apply to only one

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created a patent ambiguity, which, the opinion explained, justified admitting extrinsic evidence to establish the proper understanding of "Coldfire." *Id.*

To elaborate, in the case of a non-standard-meaning latent ambiguity, the text of the contract is facially unambiguous because the written terms are consistent with only one party's construction of the agreement when employing ordinary English. The instrument is thus fully comprehensible by itself; extrinsic evidence is not necessary to establish the standard meaning of the words. Moreover, the contract provides no indication that the parties contemplated an alternative understanding. Any uncertainty as to the parties' intent only becomes apparent upon the submission of extrinsic evidence suggesting that they employed a special meaning. Once again, this explains why such an ambiguity is considered "latent" or "extrinsic."

In a situation like *Rogers & Sons*, by contrast, the relevant express term or phrase has no standard meeting. This makes the ambiguity patent: Extrinsic evidence is not necessary to discover the ambiguity because the lack of clarity is apparent immediately upon reading the agreement (and consulting dictionaries). Indeed, such a contract is literally impossible to understand without reviewing extrinsic evidence because the critical express terms have no meaning independent of the context surrounding the transaction–unlike the words employed in general English. *See also* Startex Drilling Co., Inc. v. Sohio Petrol. Co., 680 F.2d 412, 415 (5th Cir. 1982) (holding that a contract was patently ambiguous, and thus that extrinsic evidence was properly presented to the jury, because the agreement's "undefined technical terms . . . convey little meaning without explanation"); Busch & Latta Painting Corp. v. State Highway Comm'n, 597 S.W.2d 189, 202 (Mo. Ct. App. 1980) ("Missouri follows the general rule that where a written instrument contains words or expressions of a technical nature connected with some art, science, or occupation *unintelligible to the common reader* but susceptible of definite interpretation by [an] expert, parol evidence is admissible to explain the language used.") (emphasis added); 32A C.J.S. *Evidence* § 1459 (2008) (same).

For other examples comparable to *Rogers & Sons*, see United States v. Midwest Constr. Co., 619 F.2d 349, 350–52 (5th Cir. 1980) (holding that the phrase "1 on 5 slope" combined with "dotted lines around the breakwater" on a diagram in a dredging contract constituted a patent ambiguity, justifying the admission of extrinsic evidence to "to prove the meaning of ambiguities in contract language"); May v. S.E. GA Ford, Inc., 811 S.E.2d 14, 17–18 (Ga. Ct. App. 2018) (finding a contract patently ambiguous because it contained "numerous undefined terms and abbreviations apparently used in the car sales industry"; further concluding that extrinsic evidence of trade usage resolved the ambiguity as to one of the terms—"draw against commissions"); Sierra Life Ins. Co. v. First Nat'l Life Ins. Co., 512 P.2d 1245, 1247–48 (N.M. 1973) (approving of the admission of extrinsic evidence to explain "technical terms of the life insurance business," including the phrase "cede back, by treaty of bulk reinsurance"). *But see* NCP Lake Power, Inc. v. Fla. Power Corp., 781 So. 2d 531, 536–37 (Fla. Dist. Ct. App. 2001) (explaining that even if a contract is not patently ambiguous, extrinsic evidence may be admitted to construe technical terms in the contract "that may not be understood by the court"). For authorities appearing to recognize the distinction between non-standard-meaning latent ambiguities and undefined technical terms with no ordinary meaning, see 29A AM. JUR. 2D *Evidence* § 1121 (2019) ("Parol evidence is always admissible to define and explain the meaning of words or phrases in a written instrument which are technical and not commonly known, *or* which have two meanings, the one common and universal, and the other technical.") (emphasis added); Wells Fargo Bank, N.A. v. Cherryland Mall Ltd. P'ship, 812 N.W.2d 799, 809 (Mich. Ct. App. 2011) (same).

item. By contrast, alternative definitions *are* implicated with non-standard-meaning latent ambiguities. Here, ambiguity arises because the words in the agreement have both an ordinary or standard meaning and a special or non-standard meaning, such as with the word "dozen."

As should be expected, the distinction between the two classes of latent ambiguity blurs on the margins. For a case that probably could be placed into either category, consider *In re Soper's Estate*.[139] There, a contract provided that the benefits of an insurance policy were to be paid to the "wife" of Ira Soper if he died.[140] Soper had previously deserted his wife, had pretended suicide, and was bigamously married to a second woman at the time the contract was executed.[141] The court held that Soper intended to make the second woman the beneficiary of the insurance proceeds under the contract, even though legally the first woman was his "wife."[142] *Soper's Estate* could be described as involving a subject-matter latent ambiguity because, as the word "wife" is generally understood, Soper arguably had two wives. Alternatively, the case could be understood as involving a non-standard-meaning latent ambiguity because Soper was using the word "wife" in a specialized way—to refer to the woman he was living with and holding out as his "wife" at the time the contract was executed, not to the woman who was his legal wife.[143]

"Subject-matter latent ambiguity" and "non-standard-meaning latent ambiguity" are phrases that I created. They are not present in the caselaw or the secondary literature. In part, that is because many courts do not carefully distinguish between the two types of latent ambiguity. For example, in *Mind & Motion Utah Investments, LLC v. Celtic Bank Corp.*,[144] the court started by defining a latent ambiguity as an ambiguity that results when a contract is "applied or executed"[145]—meaning a subject-matter latent ambiguity. But the opinion subsequently explained that a latent ambiguity can arise when evidence of "trade usage, course of dealing, or some other linguistic particularity" demonstrates that

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139 264 N.W. 427 (Minn. 1935).

140 *Id.* at 429.

141 *Id.* at 428–29.

142 *Id.* at 431.

143 *See* Ricks, *supra* note 18, at 774–83 (essentially arguing that *Soper's Estate* concerns a non-standard-meaning latent ambiguity).

144 367 P.3d 994 (Utah 2016).

145 *Id.* at 1004.

the terms of the contract "fail to reflect the parties' intentions,"[146] which describes the method by which a non-standard-meaning latent ambiguity is established. In other words, the court conflated the categories of latent ambiguity.[147]

Note that at one point I considered adopting the phrase "special-meaning latent ambiguity" instead of "non-standard-meaning latent ambiguity." But then the acronyms for each type of latent ambiguity would be the same—SMLA. That would create issues when I teach this material to my students. Accordingly, I selected "non-standard-meaning latent ambiguity," for which the acronym is NSMLA. That enables me to retain SMLA exclusively for "subject-matter latent ambiguity" in class.

If courts and scholars began to use the terms "subject-matter latent ambiguity" and "non-standard-meaning latent ambiguity" to distinguish between the two types of latent ambiguity, that would significantly reduce confusion both in and regarding the contract interpretation caselaw. For example, when I began my work on interpretation, I attempted to find textualist states by looking for jurisdictions that refuse to recognize latent ambiguities, following the guidance of various secondary sources stating that only contextualist territories allow for such ambiguities.[148] But as far as I can tell, no such textualist states exist because they all permit the use of extrinsic evidence to establish subject-matter latent ambiguities. Had I been aware of the distinction between the two categories of latent ambiguity from the start, that would have greatly facilitated my research. In addition, I have used the labels "subject-matter latent ambiguity" and "non-standard-meaning latent ambiguity" in class for several years and this has noticeably improved my students' understanding of latent ambiguities specifically and the operation of textualism and contextualism generally.

I thus recommend that judges, commentators, and lawyers adopt these locutions.[149] And when teaching contract interpretation,

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146 *Id.* at 1004–05.

147 *See also* Stryker Corp. v. Nat'l Union Fire Ins. Co., 842 F.3d 422, 427 (6th Cir. 2016) (applying Michigan law) (discussing cases involving each type of latent ambiguity under the general label of "latent ambiguity" and failing to distinguish between them); Shay v. Aldrich, 790 N.W.2d 629, 641–43 (Mich. 2010) (same).

148 Some of the authorities are set out in footnote 109.

149 I am certainly not the first contracts scholar to suggest that new terminology might assist with contract interpretation and the parol evidence rule. *See, e.g.*, Kniffin, *supra* note 11, at 128 ("If courts will substitute 'contract supplementation requirements' or 'contract alteration requirements' as a label for 'the parol evidence rule,' they will achieve enormous progress in avoiding confusion and resultant injustice.").

professors should be careful when representing to their students that textualist states only recognize patent ambiguities. While that is a useful heuristic early in the interpretation unit—one that I actually employ myself—I believe it is critical to subsequently explain to the students that textualist authorities *do* recognize one class of latent ambiguity: subject-matter latent ambiguity.

Given my revised nomenclature, I can now offer a more accurate statement of the difference between textualism and contextualism based on the types of ambiguity each approach permits. Textualism recognizes patent ambiguities and subject-matter latent ambiguities,[150] while contextualism recognizes patent ambiguities, subject-matter latent ambiguities, *and* non-standard-meaning latent ambiguities.[151]

IV. ISSUE 2: THE MANY DEFINITIONS OF "PAROL EVIDENCE"

In cases involving contract interpretation and/or the parol evidence rule, judges regularly employ the phrase "parol evidence." Unfortunately, they use the phrase in many different ways. In other words, "parol evidence" has multiple definitions in the caselaw. This contributes to the confusion regarding interpretation and the parol evidence rule.

Before presenting the various definitions of "parol evidence," it is worth revisiting the distinction between interpretive evidence and evidence subject to the parol evidence rule. Evidence relates to interpretation when it addresses the meaning of language set forth in the parties' agreement. Evidence is

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150 And some courts describe textualism in precisely this form. *See, e.g.*, Gen. Convention of New Jerusalem in the U.S. of Am., Inc. v. MacKenzie, 874 N.E.2d 1084, 1087 (Mass. 2007) (explaining that "extrinsic evidence may be admitted when a contract is ambiguous on its face or as applied to the subject matter"); *see also* Wiener v. E. Ark. Planting Co., 975 F.2d 1350, 1356 (8th Cir. 1992) (applying Arkansas law) ("Ambiguities may be patent or latent. . . . A patent ambiguity is an ambiguity which appears on the face of the contract . . . . [A] latent ambiguity is one developed by extrinsic evidence, where the particular words, in themselves clear, apply equally well to two different objects.") (citations and internal quotation marks omitted).

151 Note that this breakdown applies to textualism and contextualism in their unadulterated forms. But as I have said, the caselaw in most states is not purely textualist or contextualist. *See supra* notes 66–67 and accompanying text. And numerous decisions in textualist jurisdictions recognize non-standard-meaning latent ambiguities, particularly in the context of trade usage. *See* 12 WILLISTON, *supra* note 133, § 34:5, at 45–50 ("[N]umerous cases have been decided in which words with a clear normal meaning were shown by usage to bear a meaning which was not suggested by the ordinary language used. . . . Therefore, evidence of usage may be admissible to give meaning to apparently unambiguous terms of a contract when other parol evidence would be inadmissible.") (collecting authorities, including many from states that generally follow textualism).

governed by the parol evidence rule when it addresses contradictory or consistent additional terms agreed to prior to or contemporaneously with execution of the contract.[152] Now we can turn to the definitions.

First, courts sometimes use the phrase "parol evidence" to refer to evidence that is barred by the parol evidence rule. For example, in *Bilow v. Preco, Inc.*, the Idaho Supreme Court stated that "[p]arol evidence is any . . . written or oral agreements or understandings . . . made prior to or contemporaneously with the written contract."[153]

Second, courts sometimes use "parol evidence" to refer to a subset of interpretation evidence. To illustrate, in *4 G Properties, LLC v. Gals Real Estate, Inc.*, the Georgia Court of Appeals explained that "[u]nless an ambiguity exists, the court may not look outside the terms of the contract to consider surrounding circumstances *or* parol evidence."[154] Because the court distinguished evidence of the "surrounding circumstances" from "parol evidence," the court appeared to be employing the latter term to mean only certain types of interpretation evidence.

Next, courts sometimes use "parol evidence" to refer to a combination of the first two categories. For example, in *Luttrell v. Cooper Industries, Inc.*, a federal district court judge applying Kentucky law wrote that "[p]arol evidence consists of evidence of agreements between *or* the behavior of the parties prior to or contemporaneous with the contract."[155] The language before the "or" refers to evidence governed by the parol evidence rule (because it concerns "agreements"), while the language after refers to interpretation evidence (because it concerns "the behavior of the parties"). Likewise, in *Meyer-Chatfield v. Century Business Servicing, Inc.*, a federal district court judge applying Pennsylvania law stated that "[p]arol evidence is any oral testimony, written agreements, or other writings created prior to the contract that would serve to explain *or* vary the terms of the contract."[156] This time, the court identified the interpretation evidence before the "or" (using the word "explain") and the

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152 *See supra* text accompanying note 107 (explaining the difference between contract interpretation and the parol evidence rule).

153 966 P.2d 23, 28 (Idaho 1998) (internal quotation marks omitted); *accord In re* Linerboard Antitrust Litig., 443 F. Supp. 2d 703, 715 (E.D. Pa. 2006) (applying Minnesota law) ("Parol evidence is extrinsic evidence of prior or contemporaneous oral agreements, or prior written agreements. . . .") (internal quotation marks omitted).

154 656 S.E.2d 922, 924 (Ga. Ct. App. 2008) (emphasis added).

155 60 F. Supp. 2d 629, 631 (E.D. Ky. 1998) (emphasis added).

156 732 F. Supp. 2d 514, 519 (E.D. Pa. 2010) (emphasis added).

parol-evidence-rule evidence after the "or" (using the word "vary"). Finally, in *Wells Fargo Bank Wyoming, N.A. v. Hodder*, the Wyoming Supreme Court defined parol evidence as "prior or contemporaneous collateral agreements of the parties *or* [the parties'] understanding of what particular terms in their agreement mean."[157]

Notice that the three opinions discussed in the last paragraph define "parol evidence" in separate ways. In each decision, the phrase encompasses both parol-evidence-rule evidence and interpretation evidence. But the cases refer to divergent subsets of interpretation evidence when identifying what constitutes parol evidence. According to *Luttrell*, interpretation evidence concerning "the behavior of the parties prior to or contemporaneous with the contract" falls within the scope of parol evidence.[158] In *Meyer-Chatfield*, the judge identified "oral testimony, written agreements, or other writings created prior to the contract that would serve to explain . . . the . . . contract" as being parol evidence.[159] And in *Hodder*, the court stated that the category of parol evidence contains the parties' "understanding of what particular terms in their agreement mean."[160] Adding these three understandings of "parol evidence" to the first two brings the total number of definitions of that phrase up to five.

Here is yet another: Courts sometimes use "parol evidence" as a synonym for "extrinsic evidence." For example, in *Krizovensky v. Krizovensky*, a Pennsylvania trial judge wrote the following: "Where the contract terms are ambiguous . . . , however, the court is free to receive extrinsic evidence, i.e., parol evidence, to resolve the ambiguity."[161]

That increases the count to six definitions of "parol evidence." And I came across still more during my research.[162] It

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157 144 P.3d 401, 412 n.5 (Wyo. 2006) (emphasis added).

158 60 F. Supp. 2d at 631.

159 732 F. Supp. 2d at 519.

160 144 P.3d at 412 n.5.

161 624 A.2d 638, 642 (Pa. Super. Ct. 1993); *accord* Sylvia v. Wisler, No. 13-2534-EFM-TJJ, 2015 WL 6454794, at *3 (D. Kan. Oct. 26, 2015) ("'Parol evidence' simply refers to extrinsic evidence relating to a contract."); Schron v. Troutman Sanders LLP, 986 N.E.2d 430, 433 (N.Y. 2013) ("Parol evidence—evidence outside the four corners of the document—is admissible only if a court finds an ambiguity in the contract."); *see also* BURTON, *supra* note 1, § 3.1.1, at 68 ("This term [extrinsic evidence] may be defined as evidence relating to a written contract that does not appear within the four corners of the contract. It is a synonym for 'parol evidence' and will be used from time to time in this book.").

162 Note that the multiple definitions of "parol evidence" in the caselaw likely result from imprecise opinion drafting and a lack of understanding rather than from courts

is not difficult to imagine how these varied meanings of "parol evidence" confuse judges and lawyers, leading to inconsistency and incoherence in the caselaw.

Here, my primary recommendation is that we simply drop the phrase "parol evidence." The term is beyond rehabilitation. Instead, judges, lawyers, and professors should describe evidence using more detailed terminology, such as "evidence of prior or contemporaneous agreements," "evidence of contrary terms," "evidence of additional terms," "preliminary negotiations evidence," "evidence of the parties' subjective understanding of the contract's meaning," "course of performance," "course of dealing," "usages of trade," and so forth.

I teach contract interpretation before the parol evidence rule. During the interpretation unit, I cover eight categories of evidence—the text of the agreement, dictionaries, and six classifications of extrinsic evidence. When discussing items in the last group, I never use the phrase "parol evidence." Instead, I employ specific terms like those at the end of the list in the prior paragraph. And when I subsequently cover the parol evidence rule, I generally avoid the locution "parol evidence," and instead talk in terms of "evidence that contradicts a contract," "evidence that adds to a contract," and "evidence that is used to interpret a contract."

Professor Margaret Kniffin contends that we should replace the phrase "parol evidence rule" with "contract supplementation requirements" or "contract alteration requirements" to increase clarity in the caselaw.[163] I agree. But I also believe that we should go a step further and eliminate the phrase "parol evidence" as well.[164]

Unfortunately, neither "parol evidence rule" nor "parol evidence" are disappearing from judicial decisions any time soon.

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knowingly endorsing distinct meanings. Indeed, in the course of my research, I have seen no decisions that analyze which definition of the phrase to adopt. "Parol evidence" is usually defined in passing when judges lay out general principles of contract interpretation or the parol evidence rule.

163 Kniffin, *supra* note 11, at 128; *accord* Juanda Lowder Daniel, *K.I.S.S. the Parol Evidence Rule Goodbye: Simplifying the Concept of Protecting the Parties' Written Agreement*, 57 SYRACUSE L. REV. 227, 235–37 (2007) ("The eradication of the term 'parol evidence rule' can be performed in a similar manner. Let's just agree not to use this term anymore. . . ."); *id.* at 261 (arguing that "parol evidence rule" should be changed to "written contract exclusionary rule").

164 *See also* Kniffin, *supra* note 11, at 129 (recommending that courts use "extrinsic evidence" rather than "parol evidence" when referring to all evidence external to a written contract).

Accordingly, my secondary recommendation is that lawyers, judges, and professors read the phrase "parol evidence" critically. Keep in mind that the term possesses multiple meanings and think about which definition the author is using in the opinion, brief, article, or treatise. At least some confusing discussions of contract interpretation and the parol evidence rule will make more sense once the reader identifies precisely which definition of "parol evidence" is being employed.

V. ISSUE 3: THE STAGES OF CONTRACT INTERPRETATION

Both textualism and contextualism are generally understood as involving two stages. At stage one, the court assesses whether the contract is ambiguous. At stage two, the court resolves any ambiguity uncovered at stage one.[165] However, this framework oversimplifies the interpretive process. First, textualism has three substantive steps rather than two. Second, one version of contextualism has two stages, but the stages do not fit into the ambiguity/resolution framework in the same way that the steps of textualism do. And third, it is not possible to concisely describe the number of stages in the second type of contextualism.

A. Textualism

I will begin with textualism because the structure of that approach is more straightforward. Start by recalling that a patent ambiguity is resolved by the judge in two circumstances: (1) if the parties do not submit any relevant extrinsic evidence, or (2) if the evidence presented at stage two is so one-sided that there is no genuine issue of material fact regarding the contract's meaning. The jury resolves an ambiguity if (a) the parties submit relevant extrinsic evidence at stage two, *and* (b) a reasonable jury could rule for either side.[166] Given these principles, stage two of the interpretive process must be divided into two phases under textualism. And that means that textualism actually involves three stages rather than two.

Stage one is the ambiguity determination. That determination is restricted to the four corners of the contract[167] (unless there is a subject-matter latent ambiguity[168]) and it can

165 *See supra* notes 32–55 and accompanying text.
166 *See supra* notes 49–50 and accompanying text.
167 *See supra* note 37 and accompanying text.
168 *See supra* text accompanying notes 126 and 150. Part V and the subsequent parts of this Article generally set aside subject-matter latent ambiguities.

be addressed at the pleading stage or by summary judgment.[169] If the judge concludes that the contract is unambiguous, he or she simply applies the unambiguous meaning to the facts of the case. If the judge decides that the contract is patently ambiguous, then the case proceeds to stage two.[170]

At stage two, the judge assesses whether the ambiguity can be resolved as a matter of law or must instead be submitted to the jury for resolution as a question of fact. Here, the judge considers both the language of the agreement and extrinsic evidence.[171] Note again that resolving ambiguity is a question of law in two circumstances: First, if the parties offer no relevant extrinsic evidence;[172] second, if the contract language together with the relevant extrinsic evidence so heavily favors one side that there exists no genuine issue of material fact as to the agreement's meaning.[173] The second circumstance can also be described as follows: The judge resolves the ambiguity if a rational jury would necessarily decide in favor of one of the parties; if a rational jury could rule for either side, then the interpretive issue must be left to the jury and the case proceeds to stage three.[174] The court can make the stage-two

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169 Kirsch v. Brightstar Corp., 968 F. Supp. 2d 931, 938–40 (N.D. Ill. 2013) (indicating that the ambiguity determination can be addressed via a motion to dismiss and denying such a motion after finding that the contract at issue was ambiguous); Seaco Ins. Co. v. Barbosa, 761 N.E.2d 946, 951 (Mass. 2002) ("If a contract . . . is unambiguous, its interpretation is a question of law that is appropriate for a judge to decide on summary judgment."); Salewski v. Music, 54 N.Y.S. 3d 203, 205 (N.Y. App. Div. 2017) ("Whether the language set forth in a release unambiguously bars a particular claim is a question of law appropriately determined on a motion [to dismiss] based upon the entire release and without reference to extrinsic evidence . . . .") (brackets in original; internal quotation marks omitted).

170 *See supra* notes 45–48 and accompanying text.

171 *See supra* notes 48, 56, and accompanying text.

172 This happens (1) when the parties decide to submit no evidence at all and instead rest on their arguments regarding the language of the agreement, or (2) when all of the evidence submitted is not relevant and is thus rejected by the judge.

173 Nycal Corp. v. Inoco PLC, 988 F. Supp. 296, 299–300 (S.D.N.Y. 1997) ("[A] court appropriately may dispose of a contract interpretation dispute on summary judgment, although the contract is [patently] ambiguous, if the court finds either that there is no relevant extrinsic evidence or that there is relevant extrinsic evidence, but such evidence is so one-sided that it does not create a genuine issue of material fact."); Zale Constr. Co. v. Hoffman, 494 N.E.2d 830, 834 (Ill. App. Ct. 1986) ("Various commentators have stated, however, that even where such a question of fact exists, where the meaning is so clear that reasonable men could reach only one conclusion, the court should decide the [interpretive] issue as it does when the resolution of any question of fact is equally clear.") (citations and internal quotation marks omitted).

174 RCJV Holdings, Inc. v. Collado Ryerson, S.A. de C.V., 18 F. Supp. 3d 534, 541 (S.D.N.Y. 2014) ("If there is no relevant extrinsic evidence, the Court must resolve the ambiguity as a matter of law. The same is true if the evidence presented about the parties' intended meaning [is] so one-sided that no reasonable person could decide the

determination pre-trial via summary judgment[175] or at trial through a motion for a directed verdict or a motion for judgment notwithstanding the verdict.[176]

If the parties submit relevant extrinsic evidence and the judge concludes that a reasonable jury could find for either side, then the case continues to stage three. At that stage, the jury resolves the ambiguity through the normal trial procedures employed to address questions of fact.[177]

The three stages of textualism generally line up with the three basic phases of civil litigation: (1) ambiguity determination—pleadings; (2) resolving the ambiguity—discovery and summary judgment; and (3) resolving the ambiguity—trial. At stage one, the judge may not consider extrinsic evidence. The ambiguity determination is thus well suited to adjudication via a motion to dismiss or for judgment on the pleadings. Once the court decides that an ambiguity exists, the parties are entitled to present extrinsic evidence. And parties proffer such evidence in most litigated cases involving ambiguous contracts.[178] The resolution of ambiguity therefore generally cannot take place until after discovery. Accordingly, courts normally resolve ambiguities by summary judgment or through a trial, with the appropriate procedure depending on whether the evidence overwhelmingly supports one side or not. The parallel between the three steps of textualist interpretation and the three steps of a civil action is not perfect.[179] But the similar

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contrary.") (alteration in original) (citations and internal quotation marks omitted); Mamo v. Skvirsky, 960 A.2d 595, 599 (D.C. 2008) (same); RESTATEMENT (SECOND) OF CONTRACTS § 212 cmt. e (AM. L. INST. 1981) ("[A] question of interpretation is not left to the trier of fact where the evidence is so clear that no reasonable person would determine the issue in any way but one. But if the issue depends on evidence outside the writing, and the possible inferences are conflicting, the choice is for the trier of fact."); *see also* Swift & Co. v. Elias Farms, Inc., 539 F.3d 849, 851 (8th Cir. 2008) (applying Minnesota law) ("If the contract is [patently] ambiguous, however, the meaning of the contract becomes a question of fact, and summary judgment is inappropriate *unless the evidence of the parties' intent is conclusive*.") (emphasis added).

As mentioned previously, *see supra* note 50, the authorities are actually split regarding the standard for determining whether an ambiguity should be resolved as a question of law or fact. Any distinction between the various approaches is not relevant in this part. But it will be important in Part VIII.C.

175 *See* the authorities cited in footnotes 173–174 *supra*.

176 *See* BURTON, *supra* note 1, § 5.1.1, at 154 ("In any event, the normal procedural rules can turn questions of fact into questions of law, as when it is appropriate to dismiss a case on the pleadings, to grant summary judgment on the issue, or to grant a directed verdict or a judgment NOV.").

177 *See* RESTATEMENT (SECOND) OF CONTRACTS § 212(2); BURTON, *supra* note 1, § 5.1, at 152; *see also* the authorities cited in notes 173–174 *supra*.

178 *Cf.* Steven O. Weise, *"Plain English" Will Set the UCC Free*, 28 LOY. L.A. L. REV. 371, 387 (1994) ("Parties to disputes often seek to introduce extrinsic evidence to explain or supplement the written terms of the agreement.").

179 For example, the ambiguity determination may be conducted at the summary

structures help to illustrate why textualism ultimately involves three stages rather than two.[180]

Despite textualism's three-stage framework, there are good reasons to conceptualize this interpretive approach as involving only two stages. First, the same label applies to the second and third stages—"resolving ambiguity." Second, courts and commentators almost universally describe textualism as possessing two stages. Portraying this approach otherwise thus has the potential to create confusion. Accordingly, textualism is best understood as a two-stage process where the second stage contains two substantive phases. Stage one is the ambiguity determination and stage two is the resolution of ambiguity. Stage two is then divided in the following way: At stage 2A, the judge analyzes whether the ambiguity ought to be resolved as a question of law or fact. Typically, this means the judge must assess whether both parties' interpretations are reasonable given the contract language and extrinsic evidence.[181] If the answer is "yes," then at stage 2B the jury decides which reasonable interpretation wins.[182]

In sum, there are three substantive *steps* to textualist interpretation that are organized conceptually into two *stages* by the caselaw and secondary literature. Stage 1/step 1 is the ambiguity determination. Stage 2A/step 2 asks whether the ambiguity can be resolved as a question of law. And stage

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judgment phase. *See supra* note 169 and accompanying text. And the resolution of ambiguity can take place through dispositive motions at trial. *See supra* note 176 and accompanying text.

180 *Cf.* Zale Constr. Co. v. Hoffman, 494 N.E.2d 830, 834 (Ill. App. Ct. 1986) ("Various commentators have stated, however, that even where such a question of fact exists, where the meaning is so clear that reasonable men could reach only one conclusion, the court should decide the [interpretive] issue as it does when the resolution of any question of fact is equally clear. Such a statement simply grafts principles of summary judgment law onto the underlying contract law. . . .") (citations and internal quotation marks omitted); BURTON, *supra* note 1, § 4.2.3, at 119–20 ("Note that there is an important convergence between the substantive law of contracts and the law of civil procedure. If the court finds a contract to be unambiguous in the contested respect, there can be no material dispute of fact as to its meaning. A judge should decide the question of meaning on a motion for summary judgment. Similarly, if a contract is unambiguous, no reasonable jury could come to any conclusion but one.").

181 Recall that the parties normally offer extrinsic evidence to support their interpretations of ambiguous contracts. *See supra* note 178 and accompanying text.

182 Note that some cases divide stage one into two pieces. *See, e.g.*, Pursue Energy Corp. v. Perkins, 558 So. 2d 349, 352–53 (Miss. 1990) (identifying the following three stages in the interpretive process: (1) whether the contract is ambiguous based on a four-corners analysis; (2) whether a contract remains ambiguous given the four-corners of the contract *and* the canons of construction; and (3) resolving any ambiguity that remains using extrinsic evidence).

2B/step 3 is the resolution of the ambiguity as a question of fact.[183]

To bring some concreteness to this analysis, and to outline how a typical interpretation case might operate under textualism, consider the following hypothetical. A contract provides that the seller will complete performance by "early December."[184] The seller finishes on December 14. The buyer contends that this is too late and sues for breach of contract.

In litigation, parties to an agreement frequently both contend that the contract is unambiguous.[185] Accordingly, at the pleading stage, the hypothetical buyer argues that "early December" unambiguously means delivery by December 5 and the seller argues that "early December" unambiguously means delivery by December 15. Given the contractual language, the court can reach one of four rulings at stage 1: (1) the contract unambiguously means what the plaintiff/buyer claims (December 5); (2) the contract unambiguously means what the defendant/seller claims (December 15); (3) the contract unambiguously means something in between what the two parties claim (for example, December 10); or (4) the contract is ambiguous and the matter must proceed to stage 2A. Assume that the judge correctly rules that the phrase "early December" is reasonably susceptible to the meanings proffered by both parties and orders that the lawsuit continue to the next stage.

Before proceeding, let me note that not all interpretation cases will allow for option (3). An ambiguous contract might be susceptible to only two meanings and no more. For example, in *Paul W. Abbott, Inc. v. Axel Newman Heating & Plumbing Company*,[186] there was a dispute over whether one piece of language in an agreement modified another piece. That is a "yes or no" question. Thus, there was no middle-ground option.[187]

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183 Because I use "stage 2A" and "stage 2B" throughout the rest of this Article, I also use "stage 1" rather than "stage one" for purposes of consistency.

184 This hypothetical is based upon Donald W. Lyle, Inc. v. Heidner & Co., 278 P.2d 650 (Wash. 1954).

185 Sunline Com. Carriers, Inc. v. CITGO Petrol. Corp., 206 A.3d 836, 847 n.68 (Del. 2019) ("Indeed, in many contract disputes, both parties argue for different interpretations, but claim that the contract is unambiguous.").

186 166 N.W.2d 323, 324–25 (Minn. 1969).

187 For another case where only two constructions were possible, see Lion Oil Trading & Transp., Inc. v. Statoil Marketing and Trading Inc., 728 F. Supp. 2d 531 (S.D.N.Y. 2010). There, a contract for the sale of oil provided that the price was to be determined by market information "for the calendar month of delivery." *Id.* at 532. A dispute arose as to whether the language referred to the month intended at the time an order was made or to the month the oil was actually delivered. *Id.* at 531–32. At summary judgment, the court

"Early December" raises a question of degree, and thus is susceptible to a meaning *between* those argued for by the parties in my hypothetical.[188]

At stage 2A, after discovery, the parties file cross motions for summary judgment with each motion supported by relevant extrinsic evidence, as is common in disputes over contractual meaning. The seller argues that the ambiguity must be resolved in its favor because of a trade usage that "early December" means by December 15. The buyer counters that the ambiguity must be resolved in its favor because preliminary negotiation documents indicate that the seller would complete performance by December 5. The judge once again can reach one of four conclusions: (1) only the plaintiff/buyer's interpretation is plausible given the contract language and the relevant extrinsic evidence (December 5); (2) only the defendant/seller's interpretation is plausible given the same materials (December 15); (3) the only plausible reading of the contract is something between what the two parties claim (again, for example, December 10); or (4) the ambiguity must be resolved as a question of fact at trial and thus the case must proceed to stage 2B. Assume that the judge correctly rules that a rational jury could decide the meaning of "early December" for either party and sets a trial date.

Stage 2B is a jury trial to resolve the ambiguity in the phrase "early December." At this final stage, the jury can reach one of three outcomes: (1) the plaintiff/buyer's interpretation governs (December 5); (2) the defendant/seller's interpretation governs (December 15); or (3) an intermediate interpretation governs (for example, December 10). Here, there is no fourth option because stage 2B is the last step in the process.

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found that the agreement was facially ambiguous as between these two readings after analyzing several aspects of the text. *Id.* at 536.

For another case involving a potential middle-ground interpretation, see Gastar Expl. Inc. v. Rine, 806 S.E.2d 448 (W. Va. 2017). In that lawsuit, the grantee of a piece of land argued that the deed transferred all of the grantors' oil and gas rights and the grantors argued that the deed transferred none of the grantors' oil and gas rights. *Id.* at 457. The West Virginia Supreme Court concluded that both of those interpretations were plausible, but also found that the deed may have transferred half of the grantor's oil and gas rights. *Id.* Given the existence of three plausible understandings, the court ruled that the contract was ambiguous. *Id.*

188 Agreements can also be reasonably susceptible to more than two meanings in circumstances that go beyond simple questions of degree. *See, e.g.*, Mae v. Creagan, 129 F. Supp. 3d 994, 998–1000 (D. Nev. 2013) (identifying nine potential meanings of two sentences in a contract).

B. Contextualism

The structure of contextualism is more complicated. In part, that is because there are two basic types of contextualist interpretation. Recall that the difference between textualism and contextualism is that the latter approach permits the judge to consider extrinsic evidence in deciding whether a contract is ambiguous, while the former restricts the ambiguity analysis to the four corners of the agreement.[189] Critically, contextualist authorities are divided over the scope of material that the judge may consider in making the ambiguity determination.

Some courts endorse what I call "full contextualism." Under that approach, the judge considers all relevant extrinsic evidence in determining whether an agreement is ambiguous.[190] This means that courts following full contextualism analyze the same materials at both stages of the interpretive process since judges also assess all relevant extrinsic evidence when resolving an ambiguity.[191] By contrast, the stage 1 and stage 2 materials differ under textualism because that approach restricts the ambiguity determination to the contract itself, but allows extrinsic evidence to resolve ambiguities.

Other courts embrace what I call "partial contextualism." As the name suggests, partial contextualism falls between textualism and full contextualism. According to this approach, the judge reviews only a subset of the relevant extrinsic evidence in addressing whether the contract is ambiguous. For example, some authorities limit the ambiguity determination to the contract language and "objective" extrinsic evidence—i.e., evidence of objectively verifiable aspects of the contract's context and/or that is provided by disinterested third parties. This typically includes the surrounding commercial circumstances, trade usage, and course of performance. "Subjective" evidence—such as testimony by the parties regarding the preliminary negotiations—is excluded at stage 1.[192] Likewise,

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189 *See supra* notes 51–62 and accompanying text.

190 *See, e.g.*, Adams v. MHC Colony Park Ltd. P'ship, 169 Cal. Rptr. 3d 146, 161 (Cal. Ct. App. 2014); Ward v. Intermountain Farmers Ass'n, 907 P.2d 264, 268 (Utah 1995); *see also* BURTON, *supra* note 1, § 4.2.2, at 112–14, 117 (explaining this approach and describing it as the "subjective theory").

191 *See supra* note 56 and accompanying text (explaining that all relevant extrinsic evidence is considered at stage 2 under both textualism and contextualism).

192 *See, e.g.*, Stryker Corp. v. Nat'l Union Fire Ins. Co., 842 F.3d 422, 428 (6th Cir. 2016) ("But in the ordinary course, a latent ambiguity must be revealed by objective means—for instance, an admission, uncontested evidence, or the testimony of a disinterested third party."); AM Int'l, Inc. v. Graphic Mgmt. Assocs., Inc., 44 F.3d 572, 575

when interpreting contracts governed by the U.C.C., many courts restrict the ambiguity determination to the text of the agreement and the "incorporation tools"—course of performance, course of dealing, and usage of trade.[193] Under partial contextualism, the materials analyzed by the court are different at stages 1 and 2, as with textualism, since only *some* extrinsic evidence is considered at the first stage while *all* extrinsic evidence is considered at the second.[194]

1. Full Contextualism

Recall that textualism possesses three steps that are structured into two stages.[195] *Full* contextualism also has two stages, but it only contains two steps. The first stage/step is the ambiguity determination. Here, the judge analyzes the language of the contract and all relevant extrinsic evidence in deciding

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(7th Cir. 1995) ("By 'objective' evidence we mean evidence of ambiguity that can be supplied by disinterested third parties . . . . By 'subjective' evidence we mean the testimony of the parties themselves as to what they believe the contract means . . . . 'Objective' evidence is admissible to demonstrate that apparently clear contract language means something different from what it seems to mean; 'subjective' evidence is inadmissible for this purpose."); *see also* BURTON, *supra* note 1, § 4.2.2, at 112, 114–15, 117 (explaining this approach and describing it as the "objective" theory); *id.* § 2.2 (identifying the "Objectivist" elements of contract interpretation to include, *inter alia*, "Objective Circumstances," "Trade Usages and Customs," and "Practical Construction (Course of Performance)"); *id.* § 2.3 (identifying the "Subjectivist" elements of contract interpretation to include, *inter alia*, "Prior Course of Dealing," "The Course of Negotiations," "A Party's Testimony as to Its Intention," and "Subjective Circumstances").

193 *See, e.g.*, Paragon Res., Inc. v. Nat'l Fuel Gas Distrib. Corp., 695 F.2d 991, 995–96 (5th Cir. 1983) (applying New York law); *see also* Silverstein, *supra* note 106, at 1065 & n.318, 1074–75 & nn.364–65 (describing course of performance, course of dealing, and usage of trade as the "incorporation tools," explaining partial contextualism under the U.C.C., and collecting authorities).

For additional types of partial contextualism, see, for example, *Manley v. City of Coburg*, 387 P.3d 419, 423, 425 (Or. Ct. App. 2016) (limiting stage 1 to extrinsic evidence that concerns "the circumstances under which the agreement was made" and thus concluding that "evidence of the parties' conduct during the life of an agreement [i.e., course of performance evidence] is available to *resolve* a contract ambiguity, not to *create* one") (emphasis in original); John D. Calamari & Joseph M. Perillo, *A Plea for a Uniform Parol Evidence Rule and Principles of Contract Interpretation*, 42 IND. L.J. 333, 347 (1967) (describing Williston's version of contextualism as permitting any type of extrinsic evidence to establish an ambiguity except for testimony regarding what the parties said orally to each other during the preliminary negotiations).

194 Bohler-Uddeholm Am. Inc. v. Ellwood Grp., Inc., 247 F.3d 79, 93–94 (3d Cir. 2001) (applying Pennsylvania law) (explaining that "the court may consider . . . objective evidence" in making the ambiguity determination, but that the factfinder examines the objective evidence "along with all the other evidence" in resolving any ambiguity) (internal quotation marks and citation omitted); Paragon Res., Inc., 695 F.2d at 996 ("If the contract provision appears ambiguous after evidence of course of dealing, usage of trade, and course of performance has been admitted, other extrinsic evidence may then be admitted as well.").

195 *See supra* text accompanying note 183.

whether the contract is reasonably susceptible to the meanings advanced by both parties.[196]

If the answer is no—if only one party's interpretation is reasonable[197]—then the judge adopts the reasonable meaning and rejects the alternative construction advanced by the other party. If the answer is yes, then the case proceeds to the second stage/step where the court resolves the ambiguity via a jury trial that is based on the same materials considered at stage 1.[198]

Under full contextualism, the parties are entitled to submit extrinsic evidence at stage 1.[199] Accordingly, the ambiguity determination normally must occur after discovery.[200] The issue of whether an ambiguity exists can be addressed at summary judgment or at trial through a motion for a directed verdict or for judgment notwithstanding the verdict. If the contract is found to be ambiguous, then the jury resolves the ambiguity at trial.[201]

Given this structure, full contextualism can be conceptualized as either (1) combining stages 1 and 2A of textualism into a single step, or (2) eliminating stage 1 entirely and jumping directly to stage 2A. Stage 2A of textualism concerns whether the case should be decided by the judge or the

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196 *See, e.g.*, Winet v. Price, 6 Cal. Rptr. 2d 554, 557 (Cal. Ct. App. 1992).

197 As noted previously, in some cases, the judge can adopt an interpretation that is between those argued for by the parties. *See supra* notes 186–188. But I am leaving that additional complexity behind from this point forward.

198 *See, e.g.*, Focus Point Props., LLC v. Johnson, 330 P.3d 360, 367 (Ariz. Ct. App. 2014).

199 Pac. Gas & Elec. Co. v. G.W. Thomas Drayage & Rigging Co., 442 P.2d 641, 645 (Cal. 1968) ("Accordingly, rational interpretation requires at least a preliminary consideration of all credible evidence offered to prove the intention of the parties."); A. Kemp Fisheries, Inc. v. Castle & Cooke, Inc., 852 F.2d 493, 496 (9th Cir. 1988) (explaining that California law "requires that courts consider extrinsic evidence to determine whether the contract is ambiguous"); Wolf v. Superior Ct., 8 Cal. Rptr. 3d 649, 655–56 (Cal. Ct. App. 2004) ("Indeed, it is reversible error for a trial court to refuse to consider such extrinsic evidence on the basis of the trial court's own conclusion that the language of the contract appears to be clear and unambiguous on its face.").

200 *See* Woods v. Google, Inc., 889 F. Supp. 2d. 1182, 1191 (N.D. Cal. 2012) (applying California law) ("A 'court may not dismiss on the pleadings when one party claims that extrinsic evidence renders the contract ambiguous.'") (quoting A. Kemp Fisheries, Inc., 852 F.2d at 496 n.2).

201 *See* BNC Mortg., Inc. v. Tax Pros, Inc., 46 P.3d 812, 819–20 (Wash. Ct. App. 2002) ("A court can consider a written contract and its context either before trial or at trial. Before trial, a court examines affidavits or other materials offered in support of a motion for summary judgment. At trial, a court listens to witnesses and considers exhibits. If the contract's written words have but one reasonable meaning when read in context, a court may grant summary judgment before trial, or direct a verdict at trial. If the contract's written words have two or more reasonable meanings (i.e., are 'ambiguous') when read in context, a court may not grant summary judgment or direct a verdict; instead, it must put the case to a trier of fact.") (footnotes omitted), *overruled on other grounds by* Columbia Cmty. Bank v. Newman Park, LLC, 304 P.3d 472, 479 (Wash. 2013).

jury, given the language of the contract and all extrinsic evidence, and is typically addressed at summary judgment or via a trial motion.[202] That is also how "stage 1"—the ambiguity determination—operates under full contextualism.[203] In other words, whether a contract is ambiguous and whether the case raises an issue of law or fact are generally the same question for full contextualism. The Third Circuit explains:

> This preliminary inquiry [regarding ambiguity] to be made by the court in the process of contract interpretation is the same as the role of the court in ruling on a summary judgment motion on a question of contract interpretation under Michigan law. The availability of summary judgment turns on whether a proper jury question is presented. *The decision whether an ambiguity may exist is the same as the decision whether a jury question is presented as to the meaning of the contract.* When ruling on a summary judgment motion, the court is being asked to rule on whether, as a matter of law, the contract is susceptible of only one interpretation.[204]

At both stage 2A of textualism and stage 1 of full contextualism, the judge analyzes whether the parties' interpretations are reasonable in light of the contract terms and all extrinsic

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202 *See supra* notes 173–176, 181, and accompanying text.

203 *See supra* notes 196–201 and accompanying text.

204 Tigg Corp. v. Dow Corning Corp., 822 F.2d 358, 363 (3d. Cir. 1987) (emphasis added and citations omitted); *accord* Boston Five Cents Sav. Bank v. Sec'y of Dep't of Hous. & Urb. Dev., 768 F.2d 5, 8 (1st Cir. 1985) (Breyer, J.) ("Courts, noting that the judge, not the jury, decides such a threshold matter, have sometimes referred to this initial question of language ambiguity as a question of 'law,' which we see as another way of saying that there is no 'genuine' factual issue left for a jury to decide."); ConocoPhillips Co. v. Lyons, 299 P.3d 844, 849 (N.M. 2012) ("The standard to be applied in determining whether a contract term is ambiguous . . . is the same standard applied in a motion for summary judgment.") (internal quotation marks and original alterations omitted); *see also* BURTON, *supra* note 1, § 6.1.2.1, at 204–05 ("To elaborate, having identified a contract's terms, a court must decide upon motion—to dismiss, for summary judgment; to exclude evidence; or for a directed verdict—whether a term or the contract is ambiguous in the contested respect. If there is no such ambiguity, there is nothing for a fact-finder to decide. If there is only one reasonable meaning as between the meanings advanced by the parties, there can be no genuine issue on the interpretive point. And no reasonable fact-finder could come to any conclusion but one.").

Note that if the parties do not submit any relevant extrinsic evidence, then interpretation of the agreement is a question of law under contextualism, C.R. Anthony Co. v. Loretto Mall Partners, 817 P.2d 238, 244 n.5 (N.M. 1991); Winet v. Price, 6 Cal. Rprt. 2d 554, 557 (Cal. Ct. App. 1992), just as it is under textualism, *see supra* notes 49–50 and accompanying text. And despite contextualism's permissiveness regarding extrinsic evidence, sometimes parties choose not to submit such evidence in cases governed by that interpretive approach. *See, e.g.*, Colaco v. Cavotec SA, 236 Cal. Rptr. 3d. 542, 567 (Cal. Ct. App. 2018); *see also infra* notes 241–244 and accompanying text.

Note also that the standard for deciding whether interpretation raises a question of law or fact is more complicated in California, a leading contextualist state. *See infra* note 493.

evidence.[205] Textualist authorities label this step as "resolving the ambiguity" and courts endorsing full contextualism label this step as "the ambiguity determination."[206] But in *substance*, judges are engaged in the same basic inquiry under both approaches, and at the same point in the litigation.

To provide a bit more elaboration, consider the use of summary judgment in contract interpretation cases. Textualist courts generally describe summary judgment as being part of stage 2—resolving the ambiguity—while contextualist courts describe summary judgment as being part of stage 1—the ambiguity determination.[207] But summary judgment is summary judgment regardless of how it is labelled for purposes of contract interpretation doctrine (at least in most circumstances).[208] And courts are considering the text and all relevant extrinsic evidence in deciding the agreement's meaning at the summary judgment stage under both textualism and full contextualism.

The parallel between stage 2A of textualism and stage 1 of full contextualism explains why the latter approach can be understood as eliminating stage 1 and beginning the analysis with stage 2A. Alternatively, since cases applying full contextualism refer to the first stage as "the ambiguity determination," contextualism can also be understood as consolidating stages 1 and 2A into a single step. Either conceptualization fits the operation of full contextualism.

2. Partial Contextualism

The structure of partial contextualism is less clear because there appears to be very little authority discussing the stages of this approach, except under the U.C.C. Since the Code raises additional complexities, I will start with the operation of partial

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205 *See supra* text accompanying notes 181 and 196.

206 *Id.*

207 *Compare* 3Com Corp. v. Banco do Brasil, 171 F.3d 739, 746–47 (2d Cir. 1999) (applying New York law, which follows textualism) (explaining that upon a motion of summary judgment a "court may *resolve ambiguity* in contractual language as a matter of law if the evidence presented about the parties' intended meaning [is] so one-sided that no reasonable person could decide the contrary") (alteration in original, emphasis added, and internal quotation marks omitted), *with* Morgan Creek Prods., Inc. v. Franchise Pictures LLC (*In re* Franchise Pictures LLC), 389 B.R. 131, 144–45 (Bankr. C.D. Cal. 2008) (applying California law, which follows contextualism) (explaining that when a court grants summary judgment in a contract interpretation dispute, it has concluded that the contract is "unambiguous").

208 There are a few situations where the relationship of summary judgment law to contract law is more complicated. *See infra* Part VIII.C.

contextualism under the common law and then turn to the U.C.C.

In cases governed by the common law, partial contextualism *should* have the following structure given the legal principles discussed in this Article so far. Stage 1 is the ambiguity determination. At that stage, the judge analyzes the language of the contract and the permissible subset of extrinsic evidence—for example, objective evidence—in deciding whether the agreement is reasonably susceptible to the meanings argued for by both parties.[209] If the answer is no, then the judge adopts the single reasonable meaning. If the answer is yes, then the case proceeds to stage 2A.

At stage 2A, the judge addresses whether the ambiguity can be resolved as a matter of law. Under partial contextualism, this stage operates as it does under textualism and full contextualism: The judge considers the contract text and *all* relevant extrinsic evidence.[210] If the evidence overwhelmingly favors the reading advanced by one party, then the court resolves the ambiguity in favor of that party. If not, then the case proceeds to stage 2B—a jury trial at which the contract language and all relevant extrinsic evidence are admissible.

Four points of elaboration or qualification are in order. First, under this schema, partial contextualism has elements in common with both textualism and full contextualism. Partial contextualism distinguishes between stages 1 and 2A. Thus, this approach returns interpretation to a three-step framework, like textualism[211] and unlike full contextualism.[212] But the ambiguity determination under partial contextualism generally cannot take place until after discovery because that assessment requires the judge to consider extrinsic evidence,[213] as is the case with full contextualism.[214] In a textualist state, by contrast, the judge may

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209 *See supra* notes 192–193 and accompanying text.

210 *See supra* note 194 and accompanying text.

211 *See supra* notes 167–177, 183, and accompanying text.

212 *See supra* notes 195–198 and accompanying text.

213 *See* Cole Taylor Bank v. Truck Ins. Exch., 51 F.3d 736, 738 (7th Cir. 1995) ("What is true is that the doctrine of extrinsic ambiguity, even when confined to situations in which the ambiguity is demonstrated by objective evidence, makes it difficult to decide contract cases on the pleadings; for it is always open to one of the parties to try to present objective evidence that will show that an ostensibly clear contract is unclear when the usages of the trade or other contextual factors are taken into account.").

214 *See supra* notes 199–200 and accompanying text.

address the ambiguity question at the pleading stage[215] because the inquiry is restricted to the four-corners of the agreement.[216]

Second, while partial contextualism has three distinct steps, the first two steps—stages 1 and 2A—generally should be addressed at the same juncture in the litigation. To explain, in my experience, stage 2A usually occurs at summary judgment regardless of the interpretive approach. If the contract language and extrinsic evidence do not justify summary judgment, then they will seldom require a directed verdict or judgment notwithstanding the verdict. That is because the standard is the same for all three motions[217] and the balance of the evidence is not likely to change between the close of discovery and trial in the typical interpretation dispute. Next, recall that the ambiguity determination (stage 1) cannot take place until summary judgment under partial contextualism because of the parties' right to submit extrinsic evidence obtained in discovery.[218] This means that a court employing partial contextualism should address both stage 1 and stage 2A during summary judgment. Accordingly, while partial textualism has three steps for purposes of contract law, it has only two steps for purposes of civil procedure.

Third, I have not come across a single case applying partial contextualism that resolved an ambiguity as a matter of law at stage 2A based on all of the textual and extrinsic evidence after finding an ambiguity at stage 1 based on a subset of the evidence. Let me offer a theory to explain the paucity of such authority. For a case to advance past stage 1, the judge must conclude that the text of the contract and the permissible extrinsic evidence plausibly supports two different constructions of the agreement. Once that occurs, what is the likelihood that expanding the inquiry to all types of extrinsic evidence will so heavily tip the balance in favor of one reading that no reasonable jury could adopt the alternative reading? I submit that the chances of this happening are very low. One can certainly imagine a hypothetical scenario where partial contextualism would require a judge to take the case from the jury once all extrinsic evidence becomes relevant.[219] But I believe that such cases are quite rare

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215 *See supra* notes 169, 178 and accompanying text.

216 *See supra* note 167 and accompanying text.

217 9B CHARLES ALAN WRIGHT ET AL., FEDERAL PRACTICE & PROCEDURE, § 2532 (3d ed. 2017) (Westlaw database updated April 2020).

218 See the material in the immediately preceding paragraph.

219 Suppose parties X and Y enter into a facially unambiguous contract in a

in the real world. Therefore, while *conceptually* partial contextualism contains three steps, *in practice* it effectively contains only two. Stage 2A (resolution of the ambiguity at summary judgment) is largely a formality and thus partial contextualism is primarily concerned with stage 1 (the ambiguity determination at summary judgment) and stage 2B (resolution of the ambiguity at trial). This means that the ambiguity determination and deciding whether a jury question exists are substantially the same inquiry under partial contextualism, just as they are under full contextualism.[220]

Fourth, the few authorities I have found that address the stages of common law partial contextualism seem to go further; they seem to stand for the proposition that partial contextualism has only two stages as a matter of law—again, stages 1 and 2B. For example, in *Bohler-Uddeholm America, Inc., v. Ellwood Group, Inc.*, the court wrote the following:

> Once the court determines that a party has offered [objective] extrinsic evidence capable of establishing latent ambiguity, a decision as to which of the competing interpretations of the contract is the correct one is reserved for the factfinder, who would examine the content of the extrinsic evidence (along with all the other evidence) in order to make this determination.[221]

This language appears to provide that if a contract is found to be ambiguous based on the text and the relevant subset of extrinsic evidence (stage 1), then the ambiguity is resolved by the jury as a question of fact (stage 2B)—interpretation is "reserved for the factfinder"—regardless of the nature of the additional extrinsic evidence that becomes relevant at stage 2. As a result, the judge need not address whether both constructions of the agreement are reasonable based on the express terms and *all* of the extrinsic

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jurisdiction where only objective extrinsic evidence is permissible at stage 1 of the interpretive process. During the ambiguity determination, X argues for the ordinary meaning of the agreement and Y argues for a special meaning based on trade usage evidence. The judge rules that the contract is ambiguous and the case proceeds to stage 2A. There, the only additional extrinsic evidence is preliminary negotiation documents in which X and Y agreed that the trade usage relied upon by Y at stage 1 would not apply to the contract at issue. On these facts, a judge could plausibly find that no reasonable jury would endorse Y's construction, and thus X's interpretation governs as a matter of law. My thanks to my colleague Professor Nick Kahn-Fogel for assistance in developing this example.

220 *See supra* notes 202–205 and accompanying text.

221 247 F.3d 79, 94 (3d Cir. 2001) (applying Pennsylvania law); *accord* AM Int'l, Inc. v. Graphic Mgmt. Assocs., Inc., 44 F.3d 572, 575 (7th Cir. 1995) (applying Illinois law) ("Objective evidence claimed to show that an apparently clear contract is in fact ambiguous must be presented first to the judge, and only if he concludes that it establishes a genuine ambiguity is the question of interpretation handed to the jury.").

evidence, the analysis conducted at stage 2A under textualism and full contextualism. And thus once again, deciding whether a jury question exists is indistinguishable from deciding whether a contract is ambiguous under partial contextualism.[222]

However, there are two other ways to read decisions like *Bohler-Uddeholm*. First, these authorities could merely reflect the point I made two paragraphs above, that even if partial contextualism technically includes stage 2A, that stage will virtually never be implicated in real cases. Second, under the law of civil procedure, questions of fact become questions of law when a reasonable factfinder could rule for only one of the parties.[223] Accordingly, the phrase "is reserved for the factfinder" in the quotation from *Bohler-Uddeholm* may not actually rule out stage 2A. Instead, the court might have been referring generally to stage 2 of the interpretive process—which is typically described as involving a question of fact[224] even though a case can be resolved at stage 2A as a question of law[225]—rather than referring to stage 2B specifically.

Pulling the third and fourth points of elaboration together, partial contextualism under the common law either involves only two stages as a matter of law (point four) or substantially involves only two stages as a matter of fact (point three).

Next consider the stages of interpretation under the U.C.C. The language of the Code can be read to support either full contextualism or partial contextualism.[226] However, the U.C.C.'s version of partial contextualism is critically different from the common law's version. According to the Code's approach, at stage 1, parties are entitled to present the text of the contract and evidence relating to the incorporation tools—course of performance, course of dealing, and usage of trade. But other types of extrinsic evidence are not regulated by the U.C.C. at all. Instead, they are governed by supplemental principles of law from the general law of contracts (typically common law).[227]

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222 *See supra* text accompanying note 220.

223 BURTON, *supra* note 1, § 5.1.1, at 154 ("In any event, the normal procedural rules can turn questions of fact into questions of law, as when it is appropriate . . . to grant summary judgment on the issue, or to grant a directed verdict or a judgment NOV.").

224 *See supra* note 49 and accompanying text.

225 *See supra* note 50 and accompanying text; *see also supra* notes 171–176, 202–206, and accompanying text.

226 Silverstein, *supra* note 106, at 1065–73. Note, however, that some cases interpret the Code as endorsing a form of textualism. *Id.* at 1078–80 (collecting authorities).

227 *Id.* at 1065–70, 1072–73 (explaining the statutory basis for partial contextualism); *see also* U.C.C. § 1-103(b) ("Unless displaced by the particular provisions of [the Uniform

Thus, the role of non-incorporation-tools evidence varies from state to state.[228]

To illustrate, if the Code endorses this type of partial contextualism, then a court located in a jurisdiction with *textualist* common law may only consider the express terms and the incorporation tools in deciding whether an agreement is ambiguous. That is because (i) the Code allows the parties to submit the text of the contract and the incorporation tools, and (ii) supplemental principles of law bar the judge from receiving any other categories of extrinsic evidence. The additional classes of evidence are excluded unless and until the case reaches stage 2 (resolving the ambiguity), as generally required by textualism. If the court is located in a state with *full contextualist* common law, by contrast, then the Code's partial contextualism obligates the judge to examine *all* extrinsic evidence in making the ambiguity determination. That is because (i) the U.C.C. requires consideration of the text and the incorporation tools, and (ii) the common law requires that the court examine the remaining types of evidence.[229]

If the Code endorses full contextualism, then the stages of interpretation under the U.C.C. are the same as for common law full contextualism. Full contextualism is full contextualism regardless of whether it is adopted by statute or judicial decision. Likewise, if the Code endorses partial contextualism, but the applying court is in a jurisdiction with full contextualist common law, then again the stages of interpretation under the U.C.C. are the same as under common law full contextualism: stage 1/stage 2A is an ambiguity determination based on the contractual text and all extrinsic evidence; and any identified ambiguity is resolved at stage 2B based on the same materials.

If the Code embraces partial contextualism and the adjudicating court is located in a state with textualist common law, then the process is more complex. As per usual, stage 1 is the ambiguity determination. But here, ambiguity can be established in two different ways. First, if the express terms of the contract are patently ambiguous. Second, if incorporation tools evidence

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Commercial Code], the principles of law and equity . . . supplement its provisions.") (alteration in original).

228 Silverstein, *supra* note 106, at 1065.

229 *Id.* There are other possible permutations. For example, the court could be located in a state with partial contextualist common law. However, the two permutations of partial contextualism under the Code discussed in the body should be sufficient to explain the operation of the U.C.C.

establishes that the agreement contains a non-standard-meaning latent ambiguity.[230] It is critical to note that these are two independent pathways to stage 2. In particular, if the contract is ambiguous on its face, the court need not review evidence of course of performance, course of dealing, or usage of trade before moving to the next stage of the interpretive process.[231] This makes sense because, under textualism, a patent ambiguity is sufficient to allow for the consideration of *all* relevant extrinsic evidence.[232]

If a contract is ambiguous on its face, stage 1 may take place in full at the pleading stage. If the contractual text is clear and one party wishes to establish a non-standard-meaning latent ambiguity using extrinsic evidence of the incorporation tools, then the assessment of ambiguity must continue at summary judgment.

If the court determines that the contract is unambiguous, then it adopts the unambiguous meaning. If the court concludes that the agreement is *patently* ambiguous, then the case proceeds to stage 2A. And if the court decides that the agreement suffers from a *non-standard-meaning latent* ambiguity, then the case effectively moves directly to stage 2B (a jury trial), for the reasons discussed above concerning partial contextualism under the common law: It is exceedingly unlikely that adding extrinsic evidence beyond the incorporation tools to the analysis will result in the textual and extrinsic evidence overwhelmingly supporting one reading *after* the judge has found at stage 1 that the contract is ambiguous based on just the text and the incorporation tools.[233]

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230 Of course, extrinsic evidence could also establish the existence of a subject-matter latent ambiguity. But as I noted above, I am generally setting aside that type of latent ambiguity in the rest of this Article. *See supra* note 168.

231 Paragon Res., Inc. v. Nat'l Fuel Gas Distrib. Corp., 695 F.2d 991, 995–96 (5th Cir. 1983) (applying New York law) ("[T]he Code poses *three* inquiries: 1. Were the express contract terms ambiguous? 2. If not, are they ambiguous after considering evidence of course of dealing, usage of trade, and course of performance? 3. If the express contract terms by themselves are ambiguous, or if the terms are ambiguous when course of dealing, usage of trade, and course of performance are considered (that is, if the answer to either of the first two questions is yes), what is the meaning of the contract in light of *all* extrinsic evidence?") (emphasis in original); *accord* J. Lee Milligan, Inc. v. CIC Frontier, Inc., 289 Fed. Appx. 786, 789 & n.4 (5th Cir. 2008) (applying Oklahoma law and following *Paragon*); Walk-In Med. Ctrs., Inc. v. Breuer Cap. Corp., 818 F.2d 260, 264 (2d Cir. 1987) (applying New York law and following *Paragon*); Chase Manhattan Bank v. First Marion Bank, 437 F.2d 1040, 1046, 1048 (5th Cir. 1971) (applying New York law); Dawn Enters. v. Luna, 399 N.W.2d 303, 306 n.3 (N.D. 1987).

232 *See supra* notes 48, 167–171, and accompanying text.

233 *See supra* note 219 and accompanying text.

If the case moves to stage 2A, then the judge addresses whether the ambiguity can be resolved as a matter of law in light of the text of the contract and all extrinsic evidence, not just evidence regarding course of performance, course of dealing, and trade usage. If the evidence overwhelmingly favors the reading advanced by one party, then the court resolves the ambiguity in favor of that party. If not, then the case proceeds to stage 2B—a jury trial at which the contract language and all relevant extrinsic evidence are admissible.[234]

As a matter of statutory interpretation, the consensus among commentators is that the U.C.C. adopts full contextualism.[235] But the secondary literature also recognizes that courts favor partial contextualism.[236] And I have come to the same conclusion based on my own research: Partial contextualism is the dominant approach to the Code in the decisional law.[237] Accordingly, the structure of contract interpretation under the U.C.C. varies depending on whether the adjudicating court is located in a jurisdiction with textualist common law or contextualist common law.

C. Overview and Elaboration

Chart 1 summarizes the structure of textualism, full contextualism, and partial contextualism based on the analysis set forth above in this part.

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234 My description of the operation of U.C.C. partial contextualism in states with textualist common law is derived from the legal principles set forth earlier in this Article and from the cases cited *supra* in note 231.

235 Silverstein, *supra* note 106, at 1074 & n.363 (collecting authorities).

236 *Id.* at 1074 & n.364 (collecting authorities).

237 *Id.* at 1074 & n.365 (collecting authorities).

Chart 1: The Structure of Contract Interpretation

Textualism	
Stage 1: The Ambiguity Determination.	Decided by the judge—based on the contract alone[238]—at the pleading stage. If the contract is unambiguous, apply the unambiguous meaning. If the contract is ambiguous, proceed to Stage 2A.
Stage 2A: Resolve the Ambiguity.	Decided by the judge—based on the contract and all relevant extrinsic evidence—at summary judgment. If the evidence overwhelmingly supports one party, rule for that party. If not, go to Stage 2B.
Stage 2B: Resolve the Ambiguity.	Decided by the jury—based on the four corners and all relevant extrinsic evidence—at trial.
Full Contextualism (which includes Partial Contextualism Under the U.C.C. in a Contextualist State)	
Stage 1 and/or 2A: The Ambiguity Determination and/or Resolve the Ambiguity.	Decided by the judge—based on the contract and all relevant extrinsic evidence—at summary judgment. If the contract is unambiguous/if the evidence overwhelmingly supports one party, rule for that party. If the contract is ambiguous/the evidence does not overwhelmingly support one party, proceed to Stage 2B.
Stage 2B: Resolve the Ambiguity.	Decided by the jury—based on the four corners and all relevant extrinsic evidence—at trial.

238 Note that as I explained previously, I am setting aside the issue of subject-matter latent ambiguities. *See supra* note 168.

Partial Contextualism Under the Common Law	
Stage 1: The Ambiguity Determination.	Decided by the judge—based on the four corners and *some* of the relevant extrinsic evidence—at summary judgment. If the contract is unambiguous, apply the unambiguous meaning. If the contract is ambiguous, proceed to Stage 2A; in practice, proceed to Stage 2B.
Stage 2A: Resolve the Ambiguity; again, in practice, this stage is largely a formality.	Decided by the judge—based on the contract and *all* relevant extrinsic evidence—at summary judgment. If the evidence overwhelmingly supports one party, rule for that party. If not, go to Stage 2B.
Stage 2B: Resolve the Ambiguity.	Decided by the jury—based on the four corners and all relevant extrinsic evidence—at trial.
Partial Contextualism Under the U.C.C. in a Textualist State	
Stage 1: The Ambiguity Determination.	Decided by the judge—based on the four corners and potentially the incorporation tools. —at the pleading stage if the contract is patently ambiguous. —at summary judgment if a party presents evidence supporting a non-standard-meaning latent ambiguity. If the contract is unambiguous, apply the unambiguous meaning. If the contract is patently ambiguous, proceed to Stage 2A. If the contract is latently ambiguous, proceed to Stage 2A; in practice, proceed to Stage 2B.
Stage 2A: Resolve the Ambiguity; relevant in practice only if there is a patent ambiguity.	Decided by the judge—based on the contract and *all* relevant extrinsic evidence—at summary judgment. If the evidence overwhelmingly supports one party, rule for that party. If not, go to Stage 2B.
Stage 2B: Resolve the Ambiguity.	Decided by the jury—based on the four corners and all relevant extrinsic evidence—at trial.

The framework set forth in this part and summarized in Chart 1 is intended to detail the operation of textualism, full contextualism, and partial contextualism in the typical case for purposes of both contract law and civil procedure. But not all lawsuits are typical and thus the framework somewhat

oversimplifies how the various interpretive approaches work in practice. Consider several examples.

First, the final step for each approach is a jury trial. However, the parties are legally entitled to waive their right to a jury. If they do so, then the judge resolves the ambiguity at stage 2B via a bench trial.[239]

Second, according to my structure, a judge applying textualist principles should address ambiguity at the pleading stage based on the contract alone. Suppose, however, that the parties concede that the agreement is ambiguous.[240] In such a case, there is no need to conduct an ambiguity determination, based on the pleadings or otherwise.

Third, both full contextualism and common law partial contextualism eliminate the pleading stage under my framework. That is because each approach allows the parties to present extrinsic evidence at the earliest point in the interpretation analysis. And the gathering of such evidence generally requires discovery, which takes place after pleading and any related motions are finished. But there are some circumstances in which interpretation cases can be addressed on the pleadings under full and partial contextualism. To illustrate, suppose the parties waive their right to submit extrinsic evidence. In that situation, the judge can adjudicate the interpretive dispute without discovery.[241] Alternatively, a party might admit extrinsic facts in its pleading and briefs that conclusively undermine the party's asserted interpretation of the agreement.[242] Similarly, a party can defeat its own construction of the contract via extrinsic evidence that is attached as exhibits to its pleading.[243] Finally, a party may fail to allege in its pleading that language in a facially unambiguous contract was intended to possess a special meaning, eliminating the party's right to discovery and allowing

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239 *See, e.g.*, Volunteer Energy Servs., Inc. v. Option Energy, LLC, 579 F. App'x 319, 321 (6th Cir. 2014).

240 *See, e.g.*, Holston Valley Hosp. and Med. Ctr., Inc. v. Ashford Group Ltd., 661 F. Supp. 72, 73 (E.D. Tenn. 1986).

241 *See, e.g.*, Colaco v. Cavotec SA, 236 Cal. Rptr. 3d. 542, 567 (Cal. Ct. App. 2018). Such a waiver occurs, for example, where the complaint and answer admit that there is no relevant extrinsic evidence, or where the briefs relating to a motion to dismiss or a motion for judgment on the pleadings provide that the parties choose to stand exclusively on the pleadings and the arguments set forth in the briefs.

242 *See, e.g.*, Hicks v. PGA Tour, Inc., 165 F. Supp. 3d 898, 904–05 (N.D. Cal. 2016), *aff'd in part, vac. in part on other grounds*, 897 F.3d 1109 (9th Cir. 2018).

243 *See, e.g.*, Woods v. Google, Inc., 889 F. Supp. 2d 1182, 1191–93 (N.D. Cal. 2012).

the court to adjudicate the dispute based solely on the four corners of the agreement.[244]

Three final points should be noted. First, contextualist courts analyze a broader range of issues than textualist courts in deciding whether a jury question exists. That is because textualist courts will only reach stage 2A when there is a patent or subject-matter latent ambiguity, whereas courts following full or partial contextualism will address both of those types of ambiguity *and* non-standard-meaning latent ambiguities in deciding whether the case should be resolved as a question of law or fact. Because each type of contextualism allows for non-standard-meaning latent ambiguities, the precise operation of contextualism in assessing whether a jury questions exists is somewhat more complicated than I have suggested so far. I address this issue in Part VIII.

Second, may a contextualist court adjudicate a lawsuit on the pleadings when the judge concludes that the interpretation argued for by one party is too bizarre to warrant discovery and the review of extrinsic evidence? That question is addressed in Part VII,[245] which concerns the relationship of contextualism to the ambiguity determination.

Third, from this point forward, I will generally refer to the assessment of ambiguity under full contextualism and partial contextualism as "stage 1" rather than "stage 2A" or "stage 1/stage 2A" and the resolution of ambiguity under those approaches as "stage 2" rather than "stage 2B."

VI. ISSUE 4: DETERMINING WHETHER A COURT IS USING TEXTUALISM OR CONTEXTUALISM.

When reading a judicial opinion regarding the construction of an agreement, it is frequently difficult or even impossible to determine which interpretive approach the court employed or endorsed. That is because decisions are often unclear regarding whether extrinsic evidence may be or was in fact used during the ambiguity determination. Part VI discusses this problem.

Consider first the type of phrasing that properly identifies the relevant approach to interpretation. Cases describe textualism in a suitable manner when they expressly note that

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244 *See, e.g.*, Hervey v. Mercury Cas. Co., 110 Cal. Rptr. 3d 890, 896–98 (Cal. Ct. App. 2010) (affirming dismissal based exclusively on the text of the agreement).

245 *See infra* text accompanying notes 403–406.

the ambiguity determination must be restricted to the four corners of the contract or that extrinsic evidence may not be employed during stage 1. For example, here is the Minnesota Supreme Court's definition of ambiguity: "A contract is ambiguous if, *based upon its language alone*, it is reasonably susceptible of more than one interpretation."[246] A federal district court applying Kansas law set forth an even better description:

> Contractual ambiguity appears only when "the application of pertinent rules of interpretation to *the face of the instrument* leaves it generally uncertain which one of two or more possible meanings is the proper meaning." . . . As explained above, in ascertaining whether the contract is ambiguous, the Court is limited to the *four corners* of the written agreement.[247]

And the Iowa Supreme Court explained the ambiguity determination in this way: "We may not refer to extrinsic evidence in order to create ambiguity."[248]

Decisions appropriately describe contextualism when they expressly state that extrinsic evidence may be used in assessing contractual ambiguity. Here is a synopsis of the contextualist approach written by the California Court of Appeal:

> First the court provisionally receives (without actually admitting) all credible evidence concerning the parties' intentions to determine "ambiguity," i.e., whether the language is "reasonably susceptible" to the interpretation urged by a party. If in light of the extrinsic evidence the court decides the language is "reasonably susceptible" to the interpretation urged, the extrinsic evidence is then admitted to aid in the second step—interpreting the contract.[249]

Likewise, the Colorado Supreme Court described contextualist interpretation in this manner: "Thus, extrinsic evidence may be

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246 Art Goebel, Inc. v. North Suburban Agencies, Inc., 567 N.W.2d 511, 515 (Minn. 1997) (emphasis added).

247 Fisherman Surgical Instruments, LLC v. Tri-Anim Health Servs., Inc., 502 F. Supp. 2d 1170, 1179–80 (D. Kan. 2007) (emphasis added) (quoting Marquis v. State Farm Fire & Cas. Co., 256 Kan. 317, 324 (Kan. 1998)).

248 Bituminous Cas. Corp. v. Sand Livestock Sys., Inc., 728 N.W.2d 216, 222 (Iowa 2007). For proper descriptions of textualism in secondary sources, see, for example, BURTON, *supra* note 1, § 4.2.1, at 111 ("When deciding whether a contract is ambiguous, a court may consider only the contract on its face, excluding all extrinsic evidence."); KNIFFIN, 5 CORBIN ON CONTRACTS, *supra* note 32, § 24.7, at 33 ("Courts that subscribe to the 'plain meaning rule' hold that if a 'clear, unambiguous' meaning is discernible in the language of the contract, no extrinsic evidence of surrounding circumstances may be admitted to challenge this interpretation. The decision as to whether ambiguity exists must be made without reference to any source other than the contract itself."); 11 WILLISTON, *supra* note 7, § 30:5, at 80 (observing that "there is authority that the court is limited in its consideration solely to the face of the written agreement").

249 Winet v. Price, 6 Cal. Rptr. 2d 554, 557 (Cal. Ct. App. 1992).

conditionally admitted to determine whether the contract is ambiguous. . . . When an ambiguity has been determined to exist, the meaning of its terms is generally an issue of fact to be determined in the same manner as other factual issues."[250] Finally, the Illinois Supreme Court, in an opinion rejecting contextualism, explained that method of interpretation as follows:

> Under the provisional admission approach, although the language of a contract is facially unambiguous, a party may still proffer parol evidence to the trial judge for the purpose of showing that an ambiguity exists which can be found only by looking beyond the clear language of the contract. . . . Consequently, if after "provisionally" reviewing the parol evidence, the trial judge finds that an "extrinsic ambiguity" is present, then the parol evidence is admitted to aid the trier of fact in resolving the ambiguity.[251]

In each of the three opinions addressing contextualism, the court carefully distinguished between the role of extrinsic evidence at stage 1 and its role at stage 2. When a judge assesses whether a contract is ambiguous, extrinsic evidence is "provisionally received," "conditionally admitted," or "provisionally admitted." If the jury is subsequently required to resolve an ambiguity at trial, then the extrinsic evidence is simply "admitted." It is helpful to conceptualize this difference in the following way: Stage 1 involves the preliminary *consideration* of extrinsic evidence; stage 2 involves the *admitting* of extrinsic evidence. And some courts have employed this precise terminology when describing contextualist interpretation:

> First, the court asks whether, as a matter of law, the contract terms are ambiguous; that is, the court *considers* extrinsic evidence to determine whether the contract is reasonably susceptible to a party's proffered interpretation. Second, if ambiguity persists, the court *admits* extrinsic or parol evidence to help interpret the contract.[252]

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250 E. Ridge of Fort Collins, LLC v. Larimer and Weld Irrigation Co., 109 P.3d 969, 974 (Col. 2005).

251 Air Safety, Inc., v. Tchrs. Realty Corp., 706 N.E. 2d 882, 885 (Ill. 1999).

252 Yi v. Circle K Stores, Inc., 258 F. Supp. 3d 1075, 1083 (C.D. Cal. 2017) (applying California law) (emphasis added and citations omitted); *accord* Pac. Gas & Elec. Co. v. G.W. Thomas Drayage & Rigging Co., 442 P.2d 641, 645–46 (Cal. 1968); Taylor v. State Farm Mut. Auto. Ins. Co., 854 P.2d 1134, 1139–40 (Ariz. 1993); Chopin v. Chopin, 232 P.3d 99, 101–02 (Ariz. Ct. App. 2010); *see also* Hofmeyer v. Iowa Dist. Ct. for Fayette Cnty., 640 N.W.2d 225, 228 (Iowa 2001) (holding that the judge must "consult" extrinsic evidence in analyzing whether an agreement is ambiguous).

For proper descriptions of contextualism in secondary sources, see, for example, BURTON, *supra* note 1, § 4.3.3, at 128 ("In jurisdictions that recognize extrinsic ambiguities . . . the decision whether a contract is ambiguous follows judicial *consideration* of the *proffered or provisionally allowed* extrinsic evidence.") (emphasis

The logic behind this phrasing is that "admitting" suggests that the court is discussing the resolution of ambiguity at trial, whereas "considering" implies a form of preliminary review, such as summary judgment, where contextualist courts typically address whether a contract is ambiguous.

In my experience, the majority of opinions addressing contract interpretation sufficiently identify the interpretive approach at issue, much like the textualist and contextualist decisions quoted above. But in a large minority of cases, it is difficult or impossible to determine whether the court was using or describing textualism or contextualism.

There are two primary sources of this uncertainty. First, opinions frequently contain logically inconsistent statements about the interpretive process. Consider *Sun Oil Company v. Madeley*, a decision of the Texas Supreme Court involving an oil and gas lease.[253] The parties there disputed whether a judge may review extrinsic evidence as part of the ambiguity determination.[254] The lessors argued that contextualism was the governing law and the lessee asserted that textualism was the controlling standard.[255] The Texas Supreme Court began by agreeing with the lessors: "Lessors state the proper rule. Evidence of surrounding circumstances may be consulted [in assessing ambiguity]."[256] And the court quoted leading contextualist secondary sources in support of this conclusion.[257] After some additional explanation, however, the *Sun Oil* court reversed course:

> It follows that parol evidence is not admissible to render a contract ambiguous, which on its face, is capable of being given a definite certain legal meaning. This rule obtains even to the extent of prohibiting proof of circumstances surrounding the transaction when the instrument involved, by its terms, plainly and clearly discloses the

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added); LINZER, 6 CORBIN ON CONTRACTS, *supra* note 8, § 25.16[D], at 228–29 (explaining that contextualism requires "that the trial court, outside of the jury's presence, look at all of the evidence proffered, not admit it."); 11 WILLISTON, *supra* note 7, § 30:5, at 80 ("While there is authority that the court is limited in its *consideration* solely to the face of the written agreement, many more courts take the position that a court may *provisionally receive* all credible evidence concerning the parties' intentions to determine whether the language of the contract is reasonably susceptible to the interpretation urged by the party claiming ambiguity; if it is, this evidence may then be *admitted* and heard by the trier of fact.") (emphasis added).

253 626 S.W.2d 726, 727 (Tex. 1981).

254 *Id.* at 731.

255 *Id.*

256 *Id.*

257 *Id.* at 731 n.5.

> intention of the parties, or is so worded that it is not fairly susceptible of more than one legal meaning or construction.[258]

That is a perfect statement of textualism and thus directly contradicts the earlier quoted language.

The court then analyzed some of the extrinsic evidence proffered by the lessors, concluding that the evidence actually supported the lessee's construction of the agreement.[259] But the court did not identify whether it was (1) discussing this evidence as part of the ambiguity determination, or (2) explaining that even if the contract was ambiguous, extrinsic evidence would not help the lessors.

The opinion next stated that the intermediate appellate court had relied on extrinsic evidence in adopting the lessors' interpretation of the lease.[260] In response, the Texas Supreme Court held that "[w]e think the court of civil appeals erred in considering this extrinsic evidence. Only where a contract is first found to be ambiguous may the courts consider the parties' interpretation."[261] The court proceeded to find that the lease was unambiguous and thus held, "we shall confine our review to the lease and enforce it as written."[262] The rest of the opinion's analysis focused exclusively on the language of the agreement, and the court ultimately ruled in favor of the lessee.[263]

Sun Oil explicitly endorses both contextualism and textualism in its statements about the governing legal standard. And the rest of the decision does not resolve the conflict because one part of the court's application of the law focused on the four corners of the contract while another part focused on extrinsic evidence. Given the inconsistency, it should not be surprising that subsequent cases in Texas are divided over the meaning of *Sun Oil*, with some claiming that the Texas Supreme Court adopted textualism and others claiming the high court adopted contextualism.[264]

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258 *Id.* at 732.
259 *Id.*
260 *Id.*
261 *Id.*
262 *Id.*
263 *Id.* at 732–33.
264 *Compare* ExxonMobil Corp. v. Valence Operating Co., 174 S.W.3d 303, 312 (Tex. Ct. App. 2005) (interpreting *Sun Oil* as endorsing contextualism), *with* COC Servs., Ltd., v. CompUSA, Inc., 150 S.W.3d 654, 666 (Tex. Ct. App. 2004) (interpreting *Sun Oil* as endorsing textualism).

Sun Oil is illustrative. Many other opinions contain similar contradictions.[265] In fairness, sometimes cases with inconsistent

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265 *See, e.g.*, J.R. Simplot v. Chevron Pipeline Co., 563 F.3d 1102, 1109–11 (10th Cir. 2009) (applying Utah Law) (explaining that a "court first must decide whether a contract contains a facial ambiguity arising from the contractual language," but immediately thereafter stating that the court may consider extrinsic evidence in making the ambiguity determination; proceeding to analyze the language within the four corners; then noting that the court reviewed "all of the relevant extrinsic evidence," but immediately thereafter stating that the language of the contract alone controls whether the agreement is ambiguous, and only analyzing the contract itself from that point forward); BRC Rubber & Plastics, Inc. v. Cont'l Carbon Co., 876 F. Supp. 2d 1042, 1049–55 (N.D. Ind. 2012) (applying Indiana law) (stating that "[i]f the contract language is clear and unambiguous, the document is interpreted as a matter of law without looking to extrinsic evidence"; proceeding to analyze only the language of the agreement for several pages; concluding "as a matter of law that the plain language of the Agreement unambiguously indicates that the parties intended to enter into a requirements contract"; but then considering extrinsic evidence of course of performance and course of dealing because "the UCC makes clear that the provisions of a contract ought to be harmonized with the parties' course of performance, course of dealing, and the usage of trade"); Dore v. Arnold Worldwide, Inc., 139 P.3d 56, 60–61 (Cal. 2006) (expressly endorsing contextualism when discussing the governing legal principles, but then applying textualism when construing the agreement at issue; in particular, the court only analyzed language within the four-corners of the contract during the ambiguity determination, specifically stated that the proffered extrinsic evidence was irrelevant because the text of the contract was clear, and ruled that the trial court was correct to not consider the extrinsic evidence); Noble Roman's, Inc. v. Pizza Boxes, Inc., 835 N.E.2d 1094, 1098–1100 (Ind. Ct. App. 2005) (stating that the four-corners rule is the governing principle; proceeding to analyze the language within the four corners of the contract; then explaining that the U.C.C. requires that the court consider extrinsic evidence of course of performance and reviewing that evidence; but later stating that it was not necessary to resort to extrinsic evidence in the case); Affiliated FM Ins. Co. v. Const. Rein. Corp., 626 N.E.2d 878, 881–82 (Mass. 1994) (stating both that trade usage evidence is admissible when a contract is ambiguous and that ambiguity is not a prerequisite to introducing trade usage); Alexander Loc. Sch. Dist. v. Vill. of Albany, 101 N.E.3d 21, 34 (Ohio Ct. App. 2017) (quoting from a case providing that when a contract is facially unambiguous the court need not look beyond the four corners, and then restating that principle, but later quoting from another case holding that extrinsic evidence is admissible when a contract is facially ambiguous *or* when the surrounding circumstances support the conclusion that the language of the contract has a special meaning); Franklin Advisers, Inc. v. iHeart Commc'n. Inc., No. 04-16-00532-CV, 2017 WL 4518297, *2–4 (Tex. Ct. App. Oct. 11, 2017) (applying New York law) (stating that a "court determines ambiguity by looking within the four corners of the document, not to outside sources" but also that "[a]n ambiguity exists when the terms of a contract could suggest more than one meaning when viewed objectively by a reasonably intelligent person who has examined the context of the entire integrated agreement *and who is cognizant of the customs, practices, usages and terminology as generally understood in the particular trade or business*"; finding the contract at issue to be unambiguous based upon an analysis restricted to the four corners) (emphasis added); Gastar Expl. Inc. v. Rine, 806 S.E.2d 448, 454–55, 457 (W. Va. 2017) (holding that textualism is the governing standard, but discussing extrinsic evidence in addressing whether the contract was ambiguous); Wadi Petrol. v. Ultra Res., 65 P.3d 703, 708–10 (Wyo. 2003) (quoting two cases providing that textualism is the governing standard; then quoting from a case providing that courts may consider extrinsic evidence even if a contract is unambiguous; then appearing to state that the court need not resolve whether extrinsic evidence can be used to create an ambiguity; and finally quoting again from one of the textualist cases which stated that extrinsic evidence cannot create an ambiguity); *see also* Individual Healthcare Specialists,

statements of the legal rules are made clearer by the court's application of the law to the facts. For example, in *Belnick, Inc. v. TBB Global Logistics, Inc.*,[266] the court quoted from decisions that prohibit the use of extrinsic evidence if a contract is facially unambiguous and from decisions that permit the judge to consider objective extrinsic evidence in assessing contractual ambiguity.[267] But in conducting the ambiguity determination, the judge analyzed the proffered extrinsic evidence,[268] which means the court was using and probably endorsing contextualism.[269]

Inc. v. Bluecross Blueshield of Tenn., Inc., 566 S.W.3d 671, 693–94 (Tenn. 2019) (explaining that "[s]ome of the [Tennessee] cases with the strongest language on contextual principles also use textual principles as well, and vice-versa") (collecting authorities); LINZER, 6 CORBIN ON CONTRACTS, *supra* note 8, § 25.15[c], at 192 ("At times a state court seems to be saying contradictory things."); *id.* § 25.14[A], at 148–61 (collecting examples).

Perhaps the most confusing and contradictory decision on contract interpretation I have read is URI, Inc. v. Kleberg County, 543 S.W.3d 755 (Tex. 2018). In that case, the Texas Supreme Court went back and forth between textualism and contextualism so many times that it is not possible to summarize the decision in a parenthetical. And explaining it via standard text would take up too much space. So, I leave that opinion to the ambitious reader who wishes to further explore inconsistency in the interpretation jurisprudence.

Statutory rules governing contract interpretation also sometimes conflict. *Compare* CAL. CIV. § 1639 ("When a contract is reduced to writing, the intention of the parties is to be ascertained *from the writing alone*, if possible; subject, however, to the other provisions of this Title.") (emphasis added), *with* CAL. CIV. § 1647 ("A contract may be explained by reference to the circumstances under which it was made, and the matter to which it relates."). Section 1639 of the California Civil Code provides that courts should restrict interpretation to the four corners of the written contract, subject to other rules in the same title. *Id.* § 1639. Section 1647, which is in the same title, provides a blanket right to present extrinsic evidence for purposes of interpreting contracts. *Id.* § 1647. Accordingly, section 1647 eviscerates section 1639. *See also* LINZER, 6 CORBIN ON CONTRACTS, *supra* note 8, § 25.18[D], at 263–64 (stating that "it is hard to reconcile" section 1639 with Pac. Gas & Elec. Co. v. G.W. Thomas Drayage & Rigging Co., 442 P.2d 641, 643–44 (Cal. 1968)).

266 106 F. Supp. 3d 551 (M.D. Pa. 2015) (applying Pennsylvania law).

267 *Id.* at 563–64.

268 *See id.* at 564–65.

269 The same pattern played out in Sault Ste. Marie Tribe of Chippewa Indians v. Granholm, 475 F.3d 805, 812–14 (6th Cir. 2007) (applying Michigan law) (providing both that (1) "[o]nly where a contract contains ambiguous terms will consideration of outside evidence be necessary," and (2) "[i]f the alleging party presents evidence to prove a latent ambiguity it must be considered by the court"; further noting that a "latent ambiguity will often arise when a term is being used within a technical or specialized field"; and reviewing extrinsic evidence of a trade usage that the term "wager" has a special meaning within the gaming industry while conducting the ambiguity determination).

For another interesting example, consider Murphy v. Keystone Steel & Wire Co., 61 F.3d 560 (7th Cir. 1995). There, the court wrote that "although extrinsic evidence can be used to show that a contract is ambiguous, extrinsic evidence cannot be used to *create* an ambiguity." *Id.* at 565 (emphasis added and citations omitted). Such language is internally inconsistent. "Showing" that a contract is ambiguous *just is* "creating" an ambiguity. And thus the *Murphy* court's assertion that "[t]here is no contradiction here," *id.*, is simply wrong. Instead, the Seventh Circuit endorsed both textualism and contextualism in the very same sentence. But immediately thereafter, the opinion

Unfortunately, *Belnick* is atypical. Normally, contradictions regarding the governing standard are not made clearer by the court's application of the law.[270]

The second principal reason that it can be difficult to establish which interpretive approach a court is using is that cases frequently contain language that is too vague to classify as textualist or contextualist. Consider this quotation from *Porous Media Corporation v. Midland Brake, Inc.*, a decision of the Eighth Circuit:

> To interpret the terms of a contract under Minnesota law, a court must initially determine whether a contract term is ambiguous. A contract term is ambiguous if it is reasonably susceptible to more than one interpretation. The meaning of an unambiguous contract is a matter of law for the court, however, the meaning of an ambiguous contract term is a fact question for the jury.[271]

Such language does not identify the process for assessing whether a contract is ambiguous. Is the ambiguity determination limited to the four corners of the contract, or may the judge review extrinsic evidence? Note that the application of the law in this case does not aid in answering that question because the court of appeals deferred to the trial judge's conclusion that the contract was reasonably susceptible to more than one meaning rather than assessing ambiguity itself.[272] One might suggest that reading the decision in the context of Minnesota interpretation law would improve the clarity of the opinion. Unfortunately, that is not the case. The contract in *Porous Media* was governed by the U.C.C.,[273] which is generally contextualist in nature.[274] That supports the conclusion that the Eighth Circuit was referring to contextualism. But the common law of Minnesota is substantially textualist.[275]

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indicated that the confused quotation is just the *Murphy* court's sloppy way of explaining that partial contextualism is the governing standard rather than full contextualism: "The party claiming that a contract is ambiguous must first convince the judge that this is the case, and must produce *objective facts, not subjective and self-serving testimony*, to show that a contract which looks clear on its face is actually ambiguous." *Id.* (emphasis added and citations omitted). And the court did consider objective extrinsic evidence in construing the contract. *See id.* at 567–68 (also distinguishing between the objective and subjective extrinsic evidence offered by the parties). Accordingly, *Murphy* ultimately embraces a form of contextualism.

270 For some examples, see most the authorities cited *supra* in note 265.

271 220 F.3d 954, 959 (8th Cir. 2000) (citations omitted).

272 *Id.* at 960.

273 *Id.*

274 *See* Silverstein, *supra* note 106, at 1061–82.

275 *See, e.g.*, Hous. & Redevelopment Auth. v. Norman, 686 N.W.2d 329, 337 (Minn. 2005); *see also* Silverstein, *supra* note 13, at 286 (explaining that Minnesota follows textualism based on the author's analysis of the caselaw in that state).

Cases in textualist states often apply the four-corners rule to contracts governed by the Code.[276] And Minnesota follows this pattern.[277] That bolsters the conclusion that the court of appeals was referring to textualism.[278]

The troublesome wording from *Porous Media* was three sentences in length.[279] But shorter passages can be vague as well. For example, in *Employment Television Enterprises, LLC v. Barocas*, one of the parties presented trade usage evidence to the trial judge in support of its claim that a word in the contract possessed a special industry meaning different from the standard meaning.[280] On appeal, the appellate court was unable to decipher whether the judge below considered the evidence in reaching its determination that the contract was unambiguous because of vagueness in the lower court's ruling:

> The record reflects that the trial court reviewed this proffer [of trade usage evidence], but concluded the "plain meaning and general usage" of the term to be paramount. We cannot ascertain from this ruling whether the trial court properly considered ETV's trade usage evidence but found it insufficient to establish ambiguity in light of the plain meaning, or whether the court considered the evidence to be irrelevant in light of the plain and unambiguous nature of the term.[281]

Corbin on Contracts identifies another manifestation of this problem in its discussion of trade usage: "When a court . . . says that proof of local or trade usage is inadmissible because the words of the contract are 'plain and clear,' the statement may be subject to several kinds of explanation."[282] On the one hand, the court may have "considered the evidence offered to prove the

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276 *See* Silverstein, *supra* note 106, at 1080–82 (collecting authorities).

277 *See id.* at 1081 & n.404 (collecting Minnesota authorities).

278 For a comparable case, see Feldman Co., Inc. v. Atwood Richards, Inc., 636 N.Y.S.2d 312 (N.Y. App. Div. 1996). There, the court stated that the contract was unambiguous without identifying the test for ambiguity or explaining how the determination was made in this case. *Id.* at 313. Like Minnesota, New York is generally textualist. *See, e.g.*, W.W.W. Assocs., Inc. v. Giancontieri, 566 N.E.2d 639, 642 (N.Y. 1990); *see also* Silverstein, *supra* note 13, at 286 (explaining that New York follows textualism based on the author's analysis of the caselaw in that state). But the contract in *Feldman* was governed by the U.C.C. because it concerned the sale of goods, *see* 636 N.Y.S.2d at 313, and thus *Feldman* suffers from the same problem as *Porous Media*.

279 For another example of an extended description of interpretation that is impossible to classify as describing textualism or contextualism, see First Nat'l Bank of Crossett v. Griffin, 832 S.W.2d 816, 818–20 (Ark. 1992).

280 100 P.3d 37, 42 (Colo. Ct. App. 2004).

281 *Id.* at 43.

282 KNIFFIN, 5 CORBIN ON CONTRACTS, *supra* note 32, § 24.13, at 119.

usage and found it too weak,"[283] consistent with contextualism. On the other hand, the court may have found the language of the agreement to be facially unambiguous and barred any consideration of the usage evidence, consistent with textualism. This merits some elaboration.

Above, I argued that contextualism can be conceptualized as permitting (1) the "consideration" of extrinsic evidence at the first stage during the ambiguity determination, and (2) the "admitting" of evidence at the second stage to resolve any ambiguity uncovered at stage 1.[284] But courts are not consistent in their use of the terms "consider" and "admit" when explaining the role of extrinsic evidence. They employ the words interchangeably when describing stages 1 and 2.[285] Accordingly, when a judge writes that extrinsic evidence is not "admissible" or may not be "admitted" unless a contract is ambiguous—and does so without elaboration[286]—the statement is consistent with both textualism and contextualism.

To explain, "admissible" can be used in a broad sense to refer to any relevant evidence.[287] And thus a *textualist* court might write that extrinsic evidence is not admissible (meaning relevant) unless a contract is ambiguous (meaning unclear on its face). But "admissible" can also be used in a narrow sense to refer to whether the evidence may be presented to the jury at trial. And therefore, a *contextualist* court might write that extrinsic evidence is not admissible (meaning useable at trial to resolve an ambiguity) unless a contract is ambiguous (meaning unclear after considering both the language of the agreement and extrinsic evidence at a preliminary stage).

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283 *Id.* at 119–20.

284 *See supra* text accompanying note 252.

285 *See, e.g.*, Sault Ste. Marie Tribe of Chippewa Indians v. Granholm, 475 F.3d 805, 812 (6th Cir. 2007) (using both words to explain both stages of the interpretive process); W.W.W. Assocs., Inc. v. Giancontieri, 566 N.E.2d 639, 642 (N.Y. 1990) (using both words to describe stage 1); Vitullo v. New York Cent. Mut. Fire Ins. Co., 51 N.Y.S.3d 768, 770 (N.Y. App. Div. 2017) (using "admissible" to explain stage 1); Cross v. O'Heir, 993 N.E.2d 1100, 1106 (Ill. App. Ct. 2013) (using both words to describe stage 2).

286 *See, e.g.*, Checkers Pub, Inc. v. Sofios, 71 N.E.3d 731, 737 (Ohio Ct. App. 2016) ("Accordingly, interpretation of a clear and unambiguous contract term is a matter of law, and a court should not admit extrinsic evidence to establish its meaning."). For a comparable example from a secondary source, see 12 WILLISTON, *supra* note 133, § 34:1, at 18–19 ("However, parol evidence of usage and custom will ordinarily not be admissible when the intent and meaning of the parties as expressed in the contract are clear and unambiguous.").

287 *See, e.g.*, Rosov v. Maryland State Bd. of Dental Exam'rs, 877 A.2d 1111, 1123 (Md. Ct. Spec. App. 2005) ("Admissible evidence is evidence relevant to the issues in the case and tends to either establish or disprove them.") (internal quotation marks omitted).

In sum, when a court sets forth a general principle such as "extrinsic evidence is admissible if a contract is ambiguous"[288] or reaches a conclusion such as "extrinsic evidence may not be admitted here because the contract is unambiguous,"[289] such statements standing alone leave open whether extrinsic evidence may be or was considered in deciding whether the agreement is ambiguous.[290]

My recommendation to address the problems discussed in this part is simply that judges, lawyers, and professors be careful in explaining and applying interpretation doctrine. Make every effort to avoid inconsistent and vague descriptions of the governing legal rules. And describe in full whether, how, and why extrinsic evidence was used in construing the agreement at issue.

One technique that might assist in achieving these goals would be to standardize the use of the words "consider" and "admit" in interpretation cases. "Consider" should be limited to stages 1 and 2A of textualism and stage 1 of contextualism. "Admit" should be limited to stage 2B of textualism and stage 2 of contextualism.

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288 Or that "extrinsic evidence is *in*admissible if a contract is *un*ambiguous."

289 Or that "extrinsic evidence may be admitted here because the contract is ambiguous."

290 *See* Admiral Builders Sav. and Loan Ass'n v. S. River Landing, Inc., 502 A.2d 1096, 1100 (Md. Ct. Spec. App. 1986) ("When extrinsic evidence is admitted, it is often difficult to ascertain whether it is coming in *after* the primary determination of ambiguity (in order to explain the ambiguity) or if consideration of the evidence aided in the preliminary determination of ambiguity *vel non*.") (emphasis in original).

Note that when a court states that extrinsic evidence is "admissible" even though a contract is "*un*ambiguous," this necessarily constitutes contextualism. *See, e.g.*, Feinberg v. Federated Dept. Stores, Inc. 832 N.Y.S.2d 760, 763 (N.Y. Super. Ct. 2007) ("The statute's express language renders evidence of the parties' course of performance and dealing for more than a decade admissible. Such evidence is relevant to the interpretation of the contract(s), without regard to any contractual ambiguity.") (referring to U.C.C. § 2-202). The essence of contextualism is the rejection of facial ambiguity as the lynchpin for examining extrinsic evidence. Language like that in *Feinberg* accomplishes this.

Note further that the word "consider" probably does not raise the same concerns as the words "admitted" and "admissible." Thus, for example, when a court states that extrinsic evidence may not be "considered" unless a contract is ambiguous, it is generally safe to conclude that the court is referencing textualism. *See, e.g.*, Caldas v. Affordable Granite & Stone, Inc., 820 N.W.2d 826, 832 (Minn. 2012) ("When the language of a contract is clear and unambiguous, we enforce the agreement of the parties as expressed in the contract. But if the language is ambiguous—that is, susceptible to more than one reasonable interpretation—parol evidence may be *considered* to determine the intent of the parties.") (emphasis added and citation omitted); James L. Gang & Assocs., Inc. v. Abbott Labs, Inc., 198 S.W.3d 434, 437–38 (Tex. Ct. App. 2006) ("When a contract is unambiguous, a court does not *consider* course of dealing . . . . [Appellant]'s evidence relating to course of dealing between itself and [appellee] is not relevant in the face of an unambiguous contract.") (emphasis added).

The two interpretive approaches are described as follows when employing the terms in my recommended way. For textualism, at stage 1, the judge may not *consider* extrinsic evidence in conducting the ambiguity determination. At stage 2A, the judge must *consider* relevant extrinsic evidence in deciding whether resolution of the ambiguity is a question of law or fact. And at stage 2B, the judge must *admit* relevant extrinsic evidence for use by the jury in resolving the ambiguity. For contextualism, at stage 1, the judge must *consider* relevant extrinsic evidence in determining whether the contract is ambiguous (i.e., whether there is a jury question). And at stage 2 the judge must *admit* relevant extrinsic evidence for use by the jury in resolving the ambiguity.

Just as courts will probably not jettison the phrase "parol evidence" despite my recommendation,[291] inconsistent and vague judicial opinions regarding contract interpretation are almost certainly going to be with us for the foreseeable future. But unlike with parol evidence, here I have no secondary recommendation. There is little judges, lawyers, professors, and law students can do other than muddle through confusing cases on the construction of agreements.

Two final notes are in order. First, this part focused on the challenges associated with determining whether a single judicial opinion is using or endorsing textualism or contextualism. Most importantly, I explained that courts regularly set forth contradictory rules and analysis within the same decision.[292] This problem must be distinguished from a more prevalent concern in the caselaw: inconsistent statements regarding the standards governing contract interpretation *across opinions* from a given jurisdiction. Such inconsistency is essentially universal in the United States. This is my fourth article addressing contract interpretation. In conducting research for these four papers, *every* state I investigated contained both textualist and contextualist authorities.[293] However, that problem is largely beyond the scope of this piece.

Second, Part VI established that when courts try to explain the *law* of contract interpretation in judicial opinions, what they write is frequently incoherent. But in my experience, when courts

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291 *See supra* the last four paragraphs of Part IV.

292 *See supra* notes 253–270 and accompanying text.

293 For some examples, see Silverstein, *supra* note 106, at 1082–84; *see also* the authorities cited *supra* in note 7.

actually *interpret* contracts, what they write is normally quite logical. In other words, judges (and other lawyers) are generally good at construing agreements. Where they struggle is in explaining the legal rules that govern the interpretive process. *Taylor v. State Farm Mutual Automobile Insurance Company*, a leading contextualist decision, is illustrative.[294] The Arizona Supreme Court's discussion of the principles of interpretation in that case is perplexing.[295] But the opinion's construction of the settlement agreement at the center of the dispute is particularly lucid and persuasive.[296] Thus, while the complexity and confusion in the interpretation jurisprudence certainly cause significant problems for judges, lawyers, and contracting parties,[297] the problems may not be quite as serious as they appear on the surface.[298]

VII. ISSUE 5: CONTEXTUALISM AND THE AMBIGUITY DETERMINATION

Most decisions in contextualist jurisdictions state that contextualism involves an "ambiguity" determination.[299]

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294 854 P.2d 1134 (Ariz. 1993).

295 *See id.* at 1138–41. For example, the court conflated interpretation and the parol evidence rule by referring to the "'plain meaning' view of the parol evidence rule." *Id.* at 1138. It described the rules of textualism as concerning "prior negotiations" in one sentence, but then in the very next sentence stated that the rules govern "extrinsic evidence of any nature." *Id.* And the court attempted to distinguish between assessing "ambiguity" and assessing whether language is "reasonably susceptible" to an asserted meaning, *id.* at 1140, despite the fact that those are identical inquiries, *see infra* notes 413–432 and accompanying text.

296 *See Taylor*, 854 P.2d at 1141–45. It is not possible to concisely summarize the court's analysis or provide useful examples the way I did with the court's confusion regarding the law in the prior footnote. Accordingly, readers interested in more detail should review the pages cited at the beginning of this footnote.

297 *See* Kniffin, *supra* note 11, at 86 ("A central theme of this Article is that a clear distinction between the parol evidence rule and interpretation does exist but that in a significant proportion of cases, courts have indeed found themselves confused, have thereby ignored the distinction, and have thus reached unjust conclusions concerning admission or exclusion of evidence."); *id.* at 110–20 (collecting examples).

298 *Cf.* 11 WILLISTON, *supra* note 7, § 31:1, at 354 ("However, it has been said that common sense and good faith are the principal characteristics underlying the interpretation or construction of contracts, and that the construction of a contract as to its operation and effect should depend less on artificial rules than on the application of good sense and sound equity to the object and spirit of the contract in a given case."); FARNSWORTH, *supra* note 17, § 7.11, at 456 (explaining that the use of interpretive rules "in judicial opinions is often more ceremonial (as being decorative rationalizations of decisions already reached on other grounds) than persuasive (as moving the court toward a decision not yet reached)").

299 *See, e.g.*, RSD AAP, LLC v. Alyeska Ocean, Inc., 358 P.3d 483, 488–89 (Wash. Ct. App. 2015); Chopin v. Chopin, 232 P.3d 99, 101–02 (Ariz. Ct. App. 2010); Hervey v. Mercury Cas. Co., 110 Cal. Rptr. 3d 890, 895 (Cal. Ct. App. 2010).

Commentators generally concur.[300] But there is a powerful argument that contextualism dispenses with the assessment of ambiguity. At the very least, contextualist authorities are deeply schizophrenic on the role of ambiguity in the interpretive process. In this part, I discuss the role of ambiguity in contextualist interpretation.

Let me begin with a basic recap of contextualism, as qualified by the material in Parts III and V. Under full contextualism, at stage 1, the judge assesses whether the contract is "ambiguous" based on the language of the contract and all relevant extrinsic evidence. If the agreement is unambiguous—i.e., if the textual and extrinsic evidence overwhelmingly supports one party—then the judge rules for the party asserting the unambiguous meaning. If the agreement is ambiguous—i.e., if the textual and extrinsic evidence does not overwhelmingly support one party—then the case proceeds to stage 2. During the second stage, the jury resolves the ambiguity at trial based on the same evidence that the judge considered at stage 1.[301]

Under partial contextualism, at stage 1, the judge analyzes whether the contract is ambiguous based on the language of the contract and a subset of the relevant extrinsic evidence. If the agreement is unambiguous—i.e., if the textual evidence and the subset of extrinsic evidence overwhelmingly support one party—then the judge rules for the party asserting the unambiguous meaning. If the agreement is ambiguous—i.e., if the textual and extrinsic evidence does not overwhelmingly support one party—then, in theory, the case proceeds to stage 2A. At that stage, the judge assesses whether the text and *all* of the relevant extrinsic evidence overwhelmingly supports one side. If the answer is yes, then the judge resolves the ambiguity in favor of the party whom the evidence supports. If the answer is no, then the lawsuit continues to stage 2B. There, the jury resolves the ambiguity based on the same evidence that the judge considered at stage 2A. However, in practice, cases proceed directly from stage 1 to stage 2B under partial contextualism.[302]

Contextualism permits the judge to review some or all of the relevant extrinsic evidence at stage 1 because this approach

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300 *See* the authorities cited *supra* in note 51.

301 *See supra* Part V.B.1.; Chart 1 (located *supra* at note 238).

302 *See supra* Part V.B.2.; Chart 1 (located *supra* at note 238). This summary does not perfectly fit partial contextualism under the U.C.C. when a court is located in a state with textualist common law. *See supra* notes 229–234 and accompanying text.

allows for non-standard-meaning latent ambiguities. Under both versions of contextualism, during the first stage of the interpretive process, parties are permitted to submit evidence indicating that language contained in the contract possesses a non-standard or special meaning—a meaning that is different from the standard or ordinary meaning of the words used.[303]

Next, recall the definition of ambiguity endorsed by virtually all courts—textualist and contextualist alike: Language in a contract is ambiguous when it is reasonably susceptible to more than one meaning.[304] The essence of "reasonably susceptible" is that language is not infinitely flexible. Instead, the words in a contract impose genuine limits on the scope of possible constructions. Accordingly, at some point, a proposed reading of a contract crosses over from interpretation to modification. A century ago, Judge Learned Hand explained this idea in the following way: "[T]here is a critical breaking point . . . beyond which no language can be forced."[305] Here is Professor Allan Farnsworth's comparable statement: "But even though a court may look at all the circumstances in the process of interpreting contract language, the language itself imposes a limit on how far the court will go in that process."[306]

This understanding of ambiguity presents no issue for textualism because that approach is committed to the limiting power of language. Textualism follows the four-corners rule, under which a court may not consider extrinsic evidence unless the words on the face of the agreement are reasonably susceptible to the meanings asserted by both parties.[307] This entails that the language of a contract, by itself, can rule out a construction advanced by one of the litigants, prohibiting the party from presenting any extrinsic evidence in favor of its reading.[308] And textualist decisions regularly explain that courts must not twist or distort contractual wording to create ambiguity or modify an agreement,[309] propositions that inherently embrace

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303 *See supra* notes 129–139 and accompanying text.

304 *See supra* note 35 and accompanying text.

305 Eustis Mining Co. v. Beer, Sondheimer & Co., 239 F. 976, 982 (S.D.N.Y. 1917).

306 FARNSWORTH, *supra* note 17, § 7.10, at 455; *see also* Ricks, *supra* note 18, at 788–89 (explaining that the "reasonably susceptible" standard "is an objective standard and as such must depend . . . on something public").

307 *See supra* notes 32–42 and accompanying text.

308 Once again, set aside the possibility of a subject-matter latent ambiguity.

309 *See, e.g.*, Davenport v. Dickson, 507 P.2d 301, 306 (Kan. 1973) ("Construction of the terms of a written agreement does not authorize modification beyond the meaning expressed by the language used by the parties. A court may not make a new contract or rewrite the same under the guise of construction."); Nat'l City Bank v. Engler, 777

the idea that language possesses a limited spectrum of potential meanings.

Contextualism has a much more ambivalent relationship with ambiguity as "reasonable susceptibility."[310] On the one hand, many opinions from contextualist jurisdictions set forth legal principles that appear to endorse the notion that contractual wording can only be stretched so far.[311] In particular, contextualist cases regularly explain that extrinsic evidence may be used to "interpret" or "construe" a contract—including to assist in determining whether it is ambiguous—but not to "contradict," "alter," "vary," or "modify" an agreement.[312] Such

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N.W.2d 762, 765 (Minn. Ct. App. 2010) ("When a contractual provision is clear and unambiguous, based on the plain language of the contract, courts may not rewrite, modify, or limit the effect of the contract by 'strained construction.'"); Woods of Somerset, LLC v. Devs, Sur. and Indem. Co., 422 S.W.3d 330, 335 (Mo. Ct. App. 2013) ("[C]ourts may not create ambiguity by distorting contractual language that may otherwise be reasonably interpreted."); Vermont Teddy Bear Co., Inc. v. 538 Madison Realty Co., 807 N.E.2d 876, 879 (N.Y. 2004) ("[C]ourts may not by construction add or excise terms, nor distort the meaning of those used and thereby make a new contract for the parties under the guise of interpreting the writing.") (internal quotation marks omitted); *see also* Country Club of the Ozarks, LLC v. CCO Inv., LLC, 338 S.W.3d 325, 333 (Mo. Ct. App. 2011) ("Parol evidence is permissible to aid in interpreting an ambiguous contract when it does not contradict, alter, or vary the contractual terms."); Rodolitz v. Neptune Paper Prods., Inc., 239 N.E.2d 628, 630 (N.Y. 1968) ("[A] court may not, under the guise of interpretation, make a new contract for the parties or change the words of a written contract so as to make it express the real intention of the parties if to do so would contradict the clearly expressed language of the contract."); 11 WILLISTON, *supra* note 7, § 31:5 (collecting numerous authorities).

310 I use the phrases "reasonably susceptible" and "reasonable susceptibility" synonymously.

311 *See, e.g.*, Tigg Corp. v. Dow Corning Corp., 822 F.2d 358, 363 (3d. Cir. 1987) (applying Michigan law) ("Any evidence which cannot be read as consistent with the express terms of the contract is simply irrelevant because of the principle that a contract will not be given an interpretation that is in conflict with its express language."); ACL Techs., Inc. v. Northbrook Prop. & Cas. Ins. Co., 22 Cal. Rptr. 2d 206, 214 (Cal. Ct. App. 1993) (criticizing the interpretive approach of another court because "it strains the word accidental, wrenching the word from its natural embrace of the concept of unexpectedness . . . contrary to . . . common sense"); *id.* at 217 ("'Unlike the deconstructionists at the forefront of modern literary criticism, the courts still recognize the possibility of an unambiguous text.'") (quoting Ideal Mut. Ins. Co. v. Last Days Evangelical Ass'n, 783 F.2d 1234, 1238) (5th Circ. 1986)); *id.* at 219 ("With all due respect to the critics of *Pacific Gas*, the case is not an endorsement of linguistic nihilism.").

312 *See, e.g.*, Taylor v. State Farm Mut. Auto. Ins. Co., 854 P.2d 1134, 1138–39 (Ariz. 1993) (explaining that "the court can admit evidence for *interpretation* but must stop short of *contradiction*") (emphasis in original); Hervey v. Mercury Cas. Co., 110 Cal. Rptr. 3d 890, 895 (Cal. Ct. App. 2010) ("Although parol evidence may be admissible to determine whether the terms of a contract are ambiguous, it is not admissible if it contradicts a clear and explicit policy provision.") (citations omitted); Renfro v. Kaur, 235 P.3d 800, 803 (Wash. Ct. App. 2010) ("[E]xtrinsic evidence is admissible to aid in ascertaining the parties' intent where the evidence gives meaning to words used in the contract. And we recently reiterated, [e]xtrinsic evidence may be considered regardless of whether the contract terms are ambiguous. But extrinsic evidence may not be used . . . to

statements support the theory that contextualism preserves the ambiguity determination.

On the other hand, contextualism recognizes non-standard-meaning latent ambiguities: Parties are permitted to introduce extrinsic evidence during stage 1 to advance the argument that they used a word or phrase in a non-standard or special way.[313] But this means that contextualism allows parties to submit interpretive evidence that *contradicts* the ordinary meaning of an agreement. That is because the non-standard definition of a word necessarily conflicts with the standard definition. After all, it is a *different definition*. And this supports the theory that contextualism eliminates the ambiguity determination.

Both of these perspectives on contextualism merit elaboration, which is set forth in the next two sub-parts.

A. Arguments that Contextualism Eliminates the Ambiguity Determination

The thesis that contextualism eliminates the ambiguity determination is grounded on the fact that contextualism recognizes non-standard-meaning latent ambiguities. Recall the case of *Western States Construction Co. v. United States*,[314] discussed above in Part III.[315] There, the court held that it was permissible to consider trade usage evidence that the contractual phrase "metallic pipe" does not include pipe made of cast iron even though iron is "metallic" according to the standard definition of that word.[316] Next, here are three illustrations from the *Restatement (Second) of Contracts*—which endorses full contextualism[317]—two of which are based on actual cases.

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vary, contradict, or modify the written word.") (alterations in original; citations and internal quotation marks omitted).

313 *See supra* notes 129–139 and accompanying text.

314 26 Cl. Ct. 818 (1992).

315 *See supra* text accompanying notes 134–136.

316 *See* W. States, 26 Cl. Ct. at 820, 826.

317 *See* RESTATEMENT (SECOND) OF CONTRACTS § 202(1) (AM. L. INST. 1981) ("Words and other conduct are interpreted in light of all the circumstances . . . ."); *id.* § 202 cmt. b ("The circumstances for this purpose include the entire situation, as it appeared to the parties. . . ."); *id.* § 202 cmt. a ("The rules in this section . . . do not depend upon any determination that there is an ambiguity . . . ."); *id.* § 212(1) ("The interpretation of an integrated agreement is directed to the meaning of the terms of the writing or writings in the light of the circumstances, in accordance with the rules stated in this Chapter."); *id.* § 212 cmt. b ("It is sometimes said that extrinsic evidence cannot change the plain meaning of a writing, but meaning can almost never be plain except in a context. Accordingly, the rule stated in Subsection (1) is not limited to cases where it is determined that the language used is ambiguous. Any determination of meaning or

> [§ 220, illus. 8] A leases a rabbit warren to B. The written lease contains a covenant that at the end of the term A will buy and B will sell the rabbits at "60 Pounds Sterling per thousand." The parties contract with reference to a local usage that 1,000 rabbits means 100 dozen. The usage is part of the contract.[318]
>
> [§ 222, illus. 6] A and B enter into a contract for the purchase and sale of "No. 1 heavy book paper guaranteed free from ground wood." Usage in the paper trade may show that this means paper not containing over 3% ground wood.[319]
>
> [§212, illus. 4] A and B are engaged in buying and selling shares of stock from each other, and agree orally to conceal the nature of their dealings by using the word "sell" to mean "buy" and using the word "buy" to mean "sell." A sends a written offer to B to "sell" certain shares, and B accepts. The parties are bound in accordance with the oral agreement.[320]

In each of these four examples, a party was allowed to submit interpretive extrinsic evidence that contradicts the express terms of the agreement. *Western States* permitted evidence that "metallic" does not include a type of metal (iron). Section 220, illustration 8 permitted evidence that 1000 means 1200. Section 222, illustration 6 permitted evidence that "free from ground wood" means containing up to 3% ground wood rather than no ground wood. And section 212, illustration 4 permitted evidence that "sell" means "buy."

Cases of this type—which are emblematic of contextualist contract interpretation[321]—stand for the proposition that an

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ambiguity should only be made in the light of the relevant evidence of the situation and relations of the parties, the subject matter of the transaction, preliminary negotiations and statements made therein, usages of trade, and the course of dealing between the parties."); *id.* § 214 cmt. b ("Even though words seem on their face to have only a single possible meaning, other meanings often appear when the circumstances are disclosed.").

318 RESTATEMENT (SECOND) OF CONTRACTS § 220 illus. 8 (based upon Smith v. Wilson, 3 B. & Ad. 728, 110 E.R. 266, 1832 WL 4162 (K.B. 1832)); *see also* 12 WILLISTON, *supra* note 133, § 34:6, at 67–68 ("The word 'thousand,' as commonly used, has a very specific meaning, denoting 10 hundreds, but the language of the various trades and localities has given it quite a different meaning.") (collecting authorities).

319 RESTATEMENT (SECOND) OF CONTRACTS § 222 illus. 6 (based upon Gumbinsky Bros. Co. v. Smalley, 197 N.Y. Supp. 530 (N.Y. App. Div. 1922), *aff'd* 139 N.E. 758 (N.Y. 1923)); *see also* 12 WILLISTON, *supra* note 133, § 34:6, at 62–63 & n.43 ("Usage, for example, may allow a seller to furnish goods containing a small amount of impurities although the contract specifies that they shall be 'free from' impurities, when to [sic] those dealing with goods of the kind understand that the term means only that they be commercially pure.") (collecting authorities).

320 RESTATEMENT (SECOND) OF CONTRACTS § 212 illus. 4.

321 For sources collecting many comparable authorities, see Hurst v. W.J. Lake & Co., 16 P.2d 627, 629 (Or. 1932); M.C. Dransfield, *Admissibility of Extrinsic Evidence of Custom or Usage to Show That Words Employed in a Contract Unambiguous on Their Face Have a Special Trade Significance*, 89 A.L.R. 1228 (1934); KNIFFIN, 5 CORBIN ON

asserted construction supported by relevant extrinsic evidence need not fit the language of the parties' agreement, as that language is generally understood. Rather, parties are allowed to submit evidence that the express terms of their agreement possess a non-standard meaning *inconsistent* with the standard meaning of those terms. Put another way, if a party contends that a special industry dialect or even a private code—rather than ordinary English—was employed when writing the contract, the court must receive evidence to that effect.[322] And it is

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CONTRACTS, *supra* note 32, §§ 24.8, 24.13, 24.16, 24.17; 11 WILLISTON, *supra* note 7, § 32:4; 12 WILLISTON, *supra* note 133, § 34:1, 34:5, 34:6. The *Corbin* treatise specifically notes that "[i]n numberless well-considered cases, proof of local or trade usage, custom, and other circumstances has been allowed to establish a meaning that the written words of the contract would never have been given in the absence of such proof." KNIFFIN, 5 CORBIN ON CONTRACTS, *supra*, § 24.13, at 119. And *Williston* concurs: "[N]umerous cases have been decided in which words with a clear normal meaning were shown by usage to bear a meaning which was not suggested by the ordinary language used."). 12 WILLISTON, *supra*, § 34:5, at 45.

For some additional instructive examples, see Mass. Muni. Wholesale Elec. Co. v. Town of Danvers, 577 N.E2d 283, 295 (Mass. 1991) (holding that contracting parties properly adopted an alternative definition of "default," under which lack of payment for any reason—including because the underlying contract was ruled legally invalid—constituted a default, rather than using the standard definition, under which only a failure to pay a legal debt constitutes a default); H. Molsen & Co., Inc. v. Raines, 534 S.W.2d 146, 149–50 (Tex. Civ. App. 1975) (upholding the admission of extrinsic evidence showing that 3.5 had a technical trade meaning of a range from 3.5 to 4.9 "even though the writing is perfectly intelligible without" the extrinsic evidence; ultimately concluding that the evidence as a whole supported the conclusion that the parties used "3.5" in the ordinary sense); Modine Mfg. Co. v. N. E. Indep. Sch. Dist., 503 S.W.2d 833, 837–41 (Tex. Civ. App. 1973) (holding that the trial court improperly excluded trade usage evidence that a contract provision providing that the cooling "capacit[y] shall not be less than indicated" allowed for reasonable variation in cooling capacity); RESTATEMENT (SECOND) OF CONTRACTS § 222 illus. 3 ("A promises to act as B's agent in a certain business, and B promises to pay a certain commission for each 'order.' By a local usage in that business, 'order' means only an order on which the purchaser has paid a certain price. Unless otherwise agreed, the usage is part of the contract."); *id.* § 220, Reporter's Note, cmt. d ("[T]wo-by-four boards are considerably smaller than two inches by four inches in dimension; psychiatrists' hours are forty-five minutes long. To hold that a contract specifying two-by-fours or a psychiatrist's hours was so unambiguous as to prevent proof of an industry-wide standard would be foolish, and none of the courts would be likely to do so despite their dicta.").

322 Regarding trade usage, see the authorities cited in note 321 *supra*; *see also* CALAMARI AND PERILLO, *supra* note 7, § 3.17, 145 ("Under some views, a trade usage (or a course of dealing) may be shown to contradict the plain meaning of the language."); KNIFFIN, 5 CORBIN ON CONTRACTS, *supra* note 32, § 24.13, at 118 ("Because trade usage supplies a particular meaning that is used by members of the trade, this meaning will often differ from the meaning assigned by the general public."); *id.* at 119 ("As can be seen from the illustrations just described, such evidence often establishes a special and unusual meaning definitely in conflict with the more common and ordinary usages.").
Regarding private codes, see Helen Hadjiyannakis, *The Parol Evidence Rule and Implied Terms: The Sounds of Silence*, 54 FORDHAM L. REV. 35, 59–60 n.134 (1985) (explaining that the *Restatement (Second) of Contracts*—specifically § 212 and its supporting comments and illustrations—endorses the view that parties may adopt a "private code" to be used in interpreting their agreement, under which words can mean the exact opposite

reversible error to reject a proposed non-standard meaning based solely on the judge's reading of the text within the four-corners of the agreement.[323]

This logically flows from the theory of language use in contract drafting that underlies the *Restatement* specifically and contextualism generally. Recall the *Restatement*'s hypothesis, previously quoted in Part III,[324] that parties often use non-standard meanings when writing agreements:

> Parties to an agreement often use the vocabulary of a particular place, vocation or trade, in which new words are coined and common words are assigned new meanings. . . . Moreover, the same word may have a variety of technical and other meanings. "Mules" may mean animals, shoes or machines; a "ram" may mean an animal or a hydraulic ram; "zebra" may refer to a mammal, a butterfly, a lizard, a fish, a type of plant, tree or wood, or merely to the letter "Z."[325]

If "zebra" can mean "a mammal, a butterfly, a lizard, a fish, a type of plant, tree or wood, or merely . . . the letter 'Z,'"[326] then it can mean anything, including a hippopotamus, the Parthenon, Godzilla, or "500 railroad cars full of watermelons."[327] Contractual language, on this view, is infinitely flexible,[328] which destroys the concept of "reasonably susceptible" under which language possesses the capacity to constrain the spectrum of permissible interpretations.[329] It follows that parties must be

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of their meaning under standard usage); KNIFFIN, 5 CORBIN ON CONTRACTS, *supra* note 32, § 24.8, at 54–59 (making the same point regarding the *Restatement* and discussing private codes generally).

323 Hervey v. Mercury Cas. Co., 110 Cal. Rptr. 3d 890, 896 (Cal. Ct. App. 2010) (explaining that when a plaintiff argues that contractual terms have a "special meaning . . . the court cannot grant a demurrer but must permit the admission of extrinsic evidence regarding the meaning of the document intended by the parties") (internal quotation marks omitted); Wolf v. Superior Court, 8 Cal. Rptr. 3d 649, 655—56 (Cal. Ct. App. 2004) ("Indeed, it is reversible error for a trial court to refuse to consider such extrinsic evidence on the basis of the trial court's own conclusion that the language of the contract appears to be clear and unambiguous on its face.").

324 *See supra* note 131 and accompanying text.

325 RESTATEMENT (SECOND) OF CONTRACTS § 202 cmt. f (AM. L. INST. 1981); *accord id.* § 201 cmt. a.

326 *Id.* § 202 cmt. f.

327 *See* TKO Equip. Co. v. C & G Coal Co., 863 F.2d 541, 545 (7th Cir. 1988) (Easterbrook, J.) ("Under the prevailing will theory of contract, parties, like Humpty Dumpty, may use words as they please. If they wish the symbols 'one Caterpillar D9G tractor' to mean '500 railroad cars full of watermelons,' that's fine—provided parties share this weird meaning.").

328 *See* Ricks, *supra* note 18, at 795 (explaining that certain leading contextualist decisions endorse the view "that words do not have objective meaning").

329 *See id.* at 788–89 & n.106 (explaining that the theory of language set forth Pac. Gas & Elec. Co. v. G.W. Thomas Drayage & Rigging Co., 442 P.2d 641 (Cal. 1968), is inconsistent with the idea that language sets limits on the scope of potential interpretations).

entitled to introduce extrinsic evidence of special meanings even though such meanings directly contradict the ordinary meaning of written contract terms. And the *Restatement* explicitly acknowledges in multiple places that contextualist interpretation grants precisely this privilege. Comment d to section 220 is illustrative:

> There is no requirement that an ambiguity be shown before usage can be shown, and no prohibition against showing that language or conduct have a *different meaning* in the light of usage from the meaning they might have apart from the usage. *The normal effect of a usage on a written contract is to vary its meaning from the meaning it would otherwise have.*[330]

As is comment b to section 222: "There is no requirement that an agreement be ambiguous before evidence of a usage of trade can be shown, nor is it required that the usage of trade be *consistent* with the meaning the agreement would have apart from the usage."[331]

If contextualism allows extrinsic evidence to establish a special meaning that contradicts the ordinary meaning of the express terms of an agreement, then contextualism has eliminated the ambiguity determination; it has eliminated the requirement that contractual language be "reasonably susceptible" to the interpretation argued for by the parties.[332]

Professor Steven Burton endorses this conclusion as to the *Restatement (Second)*. Starting with the "buy"-equals-"sell" illustration discussed above, he explains that "[c]ertainly the word *buy* is not ambiguous in that its array of reasonable meanings includes sell. Under the *Restatement*, this does not matter. Extrinsic evidence of the private agreement is admissible to give meaning to the express agreement."[333] Said another way, by permitting evidence that "buy" means "sell," the *Restatement* allows for the introduction of extrinsic evidence even when the words of the contract are not reasonably susceptible to the supported construction. And if "buy" can mean "sell" when the

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330 RESTATEMENT (SECOND) OF CONTRACTS § 220 cmt. d (emphasis added).

331 *Id.* § 222 cmt. b (emphasis added); *accord id.* § 202 cmt. h ("But the parties may have agreed to displace normal meanings . . . ."); *id.* § 220, Reporter's Note, cmt. d ("The cases supporting the Illustrations below make clear that no matter how plain a meaning may be to a layman, it may turn out to have a different and perhaps even contradictory meaning when a special usage is proven.").

332 Note that while the line between consistency and contradiction is blurry on the margins, 12 WILLISTON, *supra* note 133, § 34:7, at 78–79, here we are dealing with clear cases of contradiction.

333 BURTON, *supra* note 1, § 4.5.2, at 140.

extrinsic evidence is sufficiently strong, then any language is "reasonably susceptible" to any meaning. In addition, the *Restatement* provides that usage and course of dealing may "qualify" a contract.[334] Professor Burton argues that this too constitutes a rejection of the ambiguity requirement: "This means that . . . a term need not be ambiguous in order for evidence of these elements to be admissible. Even a partial contradiction entails that a meaning is being given to the express term that is not within its array of reasonable meanings."[335]

Various scholars contend that there are multiple types of contextualism—extreme versions that eliminate the ambiguity determination and moderate versions that do not.[336] Some cases draw the same distinction.[337] As a result, secondary sources and judicial opinions often struggle with whether a particular contextualist case or jurisdiction endorses an assessment of ambiguity at stage 1 of the interpretive process.[338] My argument here is that these commentators and judges are mistaken: Contextualism in all of its forms eliminates the ambiguity determination; contextualist interpretation does not require that a reading of an agreement satisfy the reasonable susceptibility standard. Instead, the contextualist authorities discussed in this sub-part stand for the proposition that as long as the relevant extrinsic evidence sufficiently establishes that the parties adopted a special understanding of their contract terms, any language can possess any meaning. The Arizona Supreme Court explained this point in the leading case of *Taylor v. State Farm Mutual Automobile Insurance Company*: "If, for example, parties

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334 *See* RESTATEMENT (SECOND) OF CONTRACTS §§ 222(3), 223(2) (AM. L. INST. 1981). The U.C.C. is in accord. *See* U.C.C. § 1-303(d).

335 BURTON, *supra* note 1, § 4.5.2, at 140. Professor Burton also argues that the U.C.C. eliminates the ambiguity determination on substantially similar grounds. *See id.* § 4.5.3, at 140–43; *see also* Roger W. Kirst, *Usage of Trade and Course of Dealing: Subversion of the U.C.C. Theory*, 1977 U. Ill. L.F. 811, 815 ("If the usage of trade or course of dealing affects the outcome, extrinsic evidence will seem to modify or contradict the plain meaning of the written agreement.").

336 *See, e.g.*, BURTON, *supra* note 1, § 4.2.2, at 115, 117 (identifying one textualist and two contextualist approaches that preserve the ambiguity determination, and one contextualist approach that eliminates it); *id.* § 4.3.3, at 128–34 (distinguishing between contextualist cases that preserve the ambiguity determination and contextualist cases that dispense with it); KNIFFIN, 5 CORBIN ON CONTRACTS, *supra* note 32, § 24.7, at 39–43, 51–52 (same); *id.* § 24.9, at 61 (same); Kniffin, *supra* note 11, at 98–102 (same); LINZER, 6 CORBIN ON CONTRACTS, *supra* note 8, § 25.15[E] (This section is entitled "Establishing Ambiguity Through Extrinsic Evidence."); *id.* § 25.17 (This section is entitled "Dispensing With Ambiguity.").

337 *See, e.g.*, Nautilus Marine Enters., Inc. v. Exxon Mobile Corp., 305 P.3d 309, 316–17 (Alaska 2013).

338 *See, e.g.*, LINZER, 6 CORBIN ON CONTRACTS, *supra* note 8, § 25.16[A], at 215.

use language that is mutually intended to have a special meaning, and that meaning is proved by credible evidence, a court is obligated to enforce the agreement according to the parties' intent, even if the language ordinarily might mean something different."[339]

Since contextualism has jettisoned the ambiguity determination, what are courts doing when they purport to address whether a contract is "ambiguous" in a case where one side asserts a non-standard meaning? As indicated late in the prior paragraph, they are assessing the *weight* of the evidence: the judge is deciding whether there is sufficient evidence that the parties used a non-standard meaning in executing the agreement to warrant advancing the case to the next stage of the litigation.[340] Typically, this means that the judge is analyzing whether a reasonable jury could believe that the parties in fact intended to contract by reference to a special meaning.[341] Once again, the Arizona Supreme Court explains, quoting Professor Arthur Corbin: "At what point a judge stops 'listening to testimony that white is black and a dollar is fifty

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339 854 P.2d 1134, 1139 (Ariz. 1993) (citing, *inter alia*, RESTATEMENT (SECOND) OF CONTRACTS § 212 illus. 4, which is one of the examples I used *supra* at note 320 to explain contextualism's elimination of the ambiguity determination); *accord* Trident Ctr. v. Connecticut Gen. Life Ins. Co., 847 F.2d 564, 569 (9th Cir. 1988) ("Under *Pacific Gas*, . . . the contract cannot be rendered impervious to attack by parol evidence. If one side is willing to claim that the parties intended one thing but the agreement provides for another, the court must consider extrinsic evidence of possible ambiguity. If that evidence raises the specter of ambiguity where there was none before, the contract language is displaced. . . ."); Individual Healthcare Specialists, Inc. v. Bluecross Blueshield of Tenn., Inc., 566 S.W.3d 671, 692 (Tenn. 2019) ("Under the *Pacific Gas* approach, if extrinsic evidence shows that the contractual language does not comport with the parties' 'actual' intent, the court may override the written words if doing so is necessary to 'correct' the written agreement."); Gilson et al., *supra* note 6, at 36 ("Under this [contextualist] regime, interpretive doctrines such as the parol evidence rule are treated merely as prima facie guidance, which courts can (and should) override by considering additional evidence of the context of the transaction if they believe that doing so is necessary to substantially 'correct' or complete the parties' written contract by realigning it with its 'true' meaning.").

340 *See* KNIFFIN, 5 CORBIN ON CONTRACTS, *supra* note 32, § 24.9, at 61 (explaining that when courts "freely admit proffered extrinsic evidence without asking whether ambiguity exists, the ultimate question is still the weight of this evidence in convincing a court or jury of the parties' intended meanings at formation of the contract"); *see also id.* at 60–61 ("The question should be not the admissibility of relevant extrinsic evidence, but an assessment of the weight of such evidence, including its persuasive quality and cogency, which the court can accomplish only after viewing it. This is true despite the fact that courts have often disposed of flimsy and untrustworthy evidence by labeling it as inadmissible.").

341 *See supra* notes 202–205, 213–214, 217–222, and accompanying text; *see also infra* Part VIII.

cents is a matter for sound judicial discretion and common sense.'"[342]

Contextualism does require that judges and juries grant significant weight to the text of the contract and its ordinary meaning. In fact, the *Restatement* provides that "the words of an integrated agreement remain the most important evidence of intent."[343] As a result, arguments made before contextualist courts that the parties used a non-standard meaning will often not reach the jury for lack of sufficient evidentiary support. Likewise, juries will reject many such arguments that they do hear.[344] This entails that language possesses a type of constraining force, even if it does not restrict the spectrum of possible meanings. In particular, the greater the conflict between

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342 *Taylor*, 854 P.2d at 1139 (quoting ARTHUR L CORBIN, 3 CORBIN ON CONTRACTS § 579, at 420 (1960)); *accord* FPI Dev., Inc. v. Nakashima, 282 Cal. Rptr. 508, 521 n.10 (Cal. Ct. App. 1991) (claiming that the contextualist approach "does not embody the unconstrained view of language that some ascribe to it," but then explaining this concept by reference to the weight of the evidence: the court elaborated that judges are "justified in saying that words are too plain and clear to justify" an interpretation "far removed from common and ordinary usage" when the party advancing such a reading does so "without producing *any substantial evidence* that the other party . . . gave the unusual meaning to the language or had any reason to suppose that the first party did so") (emphasis added); Emp. Television Enters., LLC v. Barocas, 100 P.3d 37, 43 (Colo. Ct. App. 2004) ("In deciding whether usage of trade evidence makes a term ambiguous, a court should first consider any evidence of trade usage that proposes an alternative definition. Thus, trade usage evidence is admissible even if the language is plain and unambiguous on its face, *as long as the evidence is sufficient to suggest an alternative meaning*.") (emphasis added); *see also* RESTATEMENT (SECOND) OF CONTRACTS § 220 illus. 9 ("In an integrated contract, A promises to sell and B to buy a certain quantity of 'white arsenic' for a stated price. The parties contract with reference to a usage of trade that 'white arsenic' includes arsenic colored with lamp black. The usage is part of the contract."). Of course, sometimes courts purporting to apply contextualism are actually using textualism or a hybrid interpretive approach that does in fact preserve the ambiguity determination. *See, e.g.*, Jones-Hamilton Co. v. Beazer Materials & Serv., Inc., 973 F.2d 688, 692–93 (9th Cir. 1992) (explaining that *Pac. Gas & Elec. Co. v. G.W. Thomas Drayage & Rigging Co.*, 442 P.2d 641 (Cal. 1968), sets forth the governing standard under California law and requires the consideration of extrinsic evidence at stage 1 of the interpretive process, but relying exclusively on the text of the contract in adopting one party's reading of an indemnity provision, and affirming the trial court's refusal to consider the other party's extrinsic evidence); *see also supra* Part VI (discussing cases where it is impossible to determine whether the court is using textualism or contextualism); *infra* notes 373–397 and accompanying text (discussing a hybrid interpretive approach).

343 RESTATEMENT (SECOND) OF CONTRACTS § 212 cmt. b.

344 *See* Stefan Vogenauer, *Interpretation of Contracts: Concluding Comparative Observations*, *in* CONTRACT TERMS 123, 135 (Andrew Burrows & Edwin Peel, eds., 2007) ("Admitting interpretative material from outside the four corners of the document, however, does not necessarily entail that such material has to be controlling. It is important not to confuse *admissibility* and *weight*. Whilst no barriers as to admissibility are erected, external factors will not usually carry much weight if they conflict with the text of the instrument.").

the express terms and the extrinsic evidence, the stronger the latter will need to be to override the standard meaning of the text.[345] But when the extrinsic evidence is sufficiently powerful, it governs rather than the standard meaning under contextualism.

B. Arguments that Contextualism Preserves the Ambiguity Determination

The last section set forth the thesis that contextualism eliminates the ambiguity determination. This part considers (and rejects) several counterarguments supporting the conclusion that contextualism preserves the ambiguity determination.

The first counterargument focuses on the fact that contextualist judges must address whether a contract has more than one potential meaning during stage 1 of the interpretive process, just like their textualist counterparts. To illustrate, suppose the agreement at issue is neither patently ambiguous nor suffers from a subject-matter latent ambiguity. At summary judgment (which is generally the first stage under contextualism), one party asserts that the court should adopt the standard meaning of the contract's terms based on the text alone, and the other party asserts that the court should adopt a non-standard meaning derived from extrinsic evidence. In such a dispute, the judge is obligated to decide whether (1) only the standard meaning is plausible, justifying a grant of summary judgment, or (2) both asserted meanings are plausible, justifying submission of the interpretation issue to a jury.[346] Put simply, the judge must assess whether the contract has more than one potential meaning. But addressing whether the agreement has more than one potential meaning, this argument continues, *just is* an ambiguity determination. And if the judge concludes that both asserted meanings are plausible, then the contract is fairly characterized as "ambiguous" as between those two meanings. Accordingly, contextualism retains an assessment of ambiguity.

This argument fails because it is based upon the wrong definition of "ambiguous." The word "ambiguous" can be understood in a broad sense to apply when language possesses

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345 *See* CORBIN, 3 CORBIN ON CONTRACTS, *supra* note 342, § 579, at 127 ("The more bizarre and unusual an asserted interpretation is, the more convincing must be the testimony that supports it.").

346 Set aside for now option (3), which is that only the non-standard meaning is plausible because the extrinsic evidence is so strong that no reasonable jury could rule in favor of the party asserting the standard meaning. This possibility is covered in Part VIII.C *infra*.

more than one meaning *of any kind*—for example, a standard meaning and a special meaning.[347] Or the term can be understood in a narrow sense to apply solely when the language at issue has more than one *standard* meaning. Only the latter definition incorporates the reasonably susceptible standard under which language restricts the scope of possible interpretations. The former definition allows words to have a non-standard meaning, which is incompatible with reasonable susceptibility, as I explained above.[348] Ambiguity-as-reasonable-susceptibility is the version of ambiguity at issue here.[349] And the point of the last section was to demonstrate that contextualism jettisons any assessment of *that* type of ambiguity.[350] Therefore, while contextualist interpretation does require judges to analyze whether a contract is "ambiguous" in the broad sense, it does not require judges to conduct an ambiguity determination in the narrow sense relevant to this discussion.

The second argument in favor of the proposition that contextualism preserves the ambiguity determination is that contextualism in fact still requires judges to apply the reasonably susceptible standard during the first stage of interpretation. The difference between textualism and contextualism is that the former asks whether *the language of the contract* is "reasonably susceptible" to more than one meaning, whereas the latter asks whether *all* of the evidence submitted regarding the transactional context—*textual and extrinsic together*—is "reasonably susceptible" to more than one meaning.[351]

This position does not work for reasons that are similar to those that defeated the first argument: it employs the wrong understanding of "reasonably susceptible." Contractual language can possess the pertinent form of constraining force only if the

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347 *See, e.g.*, W. States Constr. Co. v. United States, 26 Cl. Ct. 818, 822 (1992) ("Ambiguity must still be demonstrated, but it exists when there are competing interpretations, one of which is a specialized trade meaning.").

348 In particular, see the text accompanying notes 324–335 *supra*.

349 See the text accompanying notes 304–306 *supra*.

350 In particular, see the text accompanying notes 336–339 *supra*.

351 One source that hints at this argument is Harry G. Prince, *Contract Interpretation in California: Plain Meaning, Parol Evidence and Use of the "Just Result" Principle*, 31 LOY. L.A. L. REV. 557 (1998). There, Professor Prince explained that California's ambiguity determination involves asking whether the language of the contract is reasonably susceptible to the meaning asserted by both parties "given the transactional context." *Id.* at 586–87; *see also* RESTATEMENT (SECOND) OF CONTRACTS § 212 cmt. a. (AM. L. INST. 1981) ("Even so, the operative meaning is found *in the transaction and its context* rather than in the law or in the usages of people other than the parties."). In addition, multiple contracts professors have pressed this argument in private discussions with me over the years.

reasonable susceptibility test is applied to the language itself, not to both the language and extrinsic evidence. That is because there is no limit to the potential features of the context surrounding the execution of an agreement. For example, during preliminary negotiations, the parties can adopt any conceivable understanding about language use. And different fields of trade can embrace an infinite variety of vocabularies. Accordingly, mandating that an interpretation be consistent with the text *and* the broader context is not a genuine limitation on the spectrum of potential meanings: as long as the extrinsic evidence sufficiently demonstrates that the parties employed special terminology when executing their agreement, the words of the contract can mean anything.[352] Thus, since applying the reasonably susceptible standard to both the text and the context does not actually restrict the possible meanings of the express terms, contextualism lacks the requisite type of ambiguity determination—one in which the words of the contract can only be stretched so far.[353]

Note that when applying the reasonable susceptibility standard to the express terms and the broader context together, the evidence *in a specific case* will limit the scope of potential meanings. In other words, only some constructions of the agreement will fit the available combination of textual and extrinsic facts before the court. But the critical point here is that contractual language *standing alone* does not restrict the spectrum of possible readings under contextualism. And it is only when the express terms possess such limiting force as a general matter that an interpretive approach can be said to preserve the ambiguity determination.

The third argument concedes that full contextualism eliminates the ambiguity determination but maintains that partial contextualism preserves it. Recall that partial contextualism permits the use of only certain types of extrinsic

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352 Professors Robert Scott and Jody Kraus essentially make the same point in their casebook. They argue that the only basis for analyzing whether a contractual term is "reasonably susceptible" to an asserted meaning is "whether that meaning would be consistent with the court's view of the *plain and unambiguous meaning* of the term." ROBERT E. SCOTT & JODY KRAUS, CONTRACT LAW AND THEORY, 592 (4th ed. 2007) (emphasis added). In other words, the reasonably susceptible standard is inherently tied to the ordinary meaning of express terms. Disconnecting the standard from ordinary meaning entails that "there is no meaning to which terms . . . are not reasonably susceptible," eviscerating the limiting effect of the reasonable susceptibility standard. *Id.* at 593.

353 *See* the text accompanying notes 304–306 *supra*.

evidence to establish that a contract is "ambiguous." For example, under one version of partial contextualism, the assessment of ambiguity is limited to the contractual text and "objective" extrinsic evidence.[354] The theory behind this approach is that objective evidence possesses greater reliability than subjective evidence because it is more difficult to fabricate.[355] The U.C.C. implements another version of partial contextualism, according to some courts, under which the ambiguity determination is restricted to the words of the agreement and the incorporation tools—course of performance, course of dealing, and usage of trade.[356] Some authorities defend this approach on the same ground as the courts adopting objective partial contextualism: evidence of course of performance, course of dealing, and trade usage is more reliable than other types of extrinsic evidence.[357] In addition, the U.C.C. itself articulates justifications for granting special privileges to the incorporation tools. First, the Code states that course of performance evidence is "the best indication of what [the parties] intended" a contract to mean.[358] Second, the Code presumes "that the course of prior dealings . . . and the usages of trade were taken for granted when the [contract] was phrased."[359]

A few decisions applying partial contextualism contend that this approach does not permit interpretive extrinsic evidence to contradict a written agreement. For example, in *Chase Manhattan Bank v. First Marion Bank*, the Fifth Circuit endorsed the incorporation-tools version of partial contextualism under the U.C.C.[360] It thus ruled that the trial judge should have considered course of dealing and trade usage evidence that a subordination agreement with an express duration of eighteen months was actually intended to last beyond eighteen months.[361] Among other points, the court argued that reviewing course-of-dealing and trade-usage evidence does not violate, or constitute an exception to, the parol evidence rule's prohibition on contradicting the

354 *See supra* note 192 and accompanying text.

355 *See* AM Int'l, Inc. v. Graphic Mgmt. Assocs., Inc., 44 F.3d 572, 575 (7th Cir. 1995); *In re* Envirodyne Indust., Inc., 29 F.3d 301, 305 (7th Cir. 1994); BURTON, *supra* note 1, § 4.2.2, at 115.

356 *See supra* note 193, 226–232, and accompanying text.

357 *See, e.g.*, Carter Baron Drilling v. Badger Oil Corp., 581 F. Supp. 592, 598 (D. Colo. 1984).

358 U.C.C. § 2-202 cmt. 2.

359 *Id.*

360 437 F.2d 1040, 1046–48 (5th Cir. 1971) (applying New York law).

361 *Id.*

express terms of a contract, even when the extrinsic evidence appears to conflict with those terms:

> Certainly the parol evidence rule does not preclude evidence of course of dealing or usage of trade, for such evidence merely delineates a commercial backdrop for intelligent interpretation of the agreement. . . . Evidence to explain ambiguity, establish a custom, or show the meaning of technical terms, and the like, is not regarded as an exception to the general rule because it does not contradict or vary the written instrument, but simply places the court in the position of the parties when they made the contract, and enables it to appreciate the force of the words they used in reducing it to writing.[362]

In responding to the reasoning in *Chase*, I want to set aside the parol evidence rule. As I will discuss in Part IX, contextualism preserves the parol evidence rule even though it allows the use of extrinsic evidence for purposes of establishing a special meaning that contradicts the standard meaning of contractual language. But the Fifth Circuit's analysis went beyond the parol evidence rule; the court concluded that using the incorporation tools to construe an agreement in the manner described in *Chase* "does not contradict or vary the written instrument."[363] That is not true. Employing extrinsic evidence to establish a non-standard meaning is a form of contradicting the writing because a non-standard meaning is *different* from the ordinary meaning of an agreement's language. And different meanings are necessarily conflicting.[364] Indeed, the Fifth Circuit essentially ordered the trial judge to receive evidence that "eighteen months" actually means longer than eighteen months. Such evidence plainly contradicts the standard meaning of the express terms.

Partial contextualism permits parties to use extrinsic evidence to assert a special meaning that is inconsistent with the ordinary meaning of the written words. Because this type of contradiction is authorized, partial contextualism sanctions the advancing of interpretations that do not satisfy the reasonably susceptible standard. Accordingly, both full contextualism and

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362 *Id.* at 1046, 1048; *see also* RESTATEMENT (SECOND) OF CONTRACTS § 220 cmt. d (AM. L. INST. 1981) ("Language and conduct are in general given meaning by usage rather than by the law, and ambiguity and contradiction likewise depend upon usage. Hence usage relevant to interpretation is treated as part of the context of an agreement in determining whether there is ambiguity or contradiction as well as in resolving ambiguity or contradiction.").

363 *Chase*, 437 F.2d at 1048.

364 *See supra* text accompanying note 313 (articulating the same point); *see also supra* notes 330–331 and accompanying text (explaining the *Restatement's* acknowledgement that contextualist interpretation involves contradiction).

partial contextualism eliminate the ambiguity determination in precisely the same manner.[365]

One type of partial contextualism warrants further discussion. Suppose we are dealing with a narrow version of partial contextualism under which only *trade usage* evidence can be used to establish a non-standard-meaning latent ambiguity. One could plausibly assert that this approach preserves the ambiguity determination. To explain, systems of industry terminology can be thought of as alternate languages.[366] At stage 1 of the interpretive process, the question is whether the parties used standard English or a technical industry dialect in drafting their agreement. Such an inquiry can be analogized to whether the parties used English or French when writing the contract.[367] If permitting extrinsic evidence on the latter question (English versus French) does not result in contradiction of the agreement, one might conclude that the same is true for extrinsic evidence regarding the former question (English versus an industry dialect).[368]

I am unpersuaded by this justification for the third counterargument because it does not address my central

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365 While I stated that I want to set aside the parol evidence rule here, it is worth noting that some cases have described contextualist interpretation as an exception to the parol evidence rule. For example, in *Stryker Corp.*, the Sixth Circuit explained that allowing extrinsic evidence to establish a non-standard-meaning latent ambiguity constitutes a "[b]reaking from the parol evidence rule," but is nevertheless "justified because it 'enabl[es] courts to ascertain and carry into effect the intention of the contracting parties.'" Stryker Corp. v. Nat'l Union Fire Ins. Co. of Pittsburgh, 842 F.3d 422, 427 (6th Cir. 2016) (quoting Ives v. Kimball, 1 Mich. 308, 313 (1849)) (applying Michigan law). Characterizing this use of extrinsic evidence as an "exception" to the parol evidence rule constitutes a recognition of the fact that contextualism permits a party to introduce interpretive evidence that contradicts a written agreement.

366 *In re* Envirodyne Indus., Inc., 29 F.3d 301, 305 (7th Cir. 1994) (describing trade usage evidence as "in the nature of specialized dictionaries"); Ricks, *supra* note 18, at 799 n.169 ("For instance, individuals within a trade may employ certain language quite differently than those outside the trade. As a result, '[t]he "plain meaning" of a particular phrase might be quite different in a particular industry sub-community than it is in normal everyday speech.'" (quoting BRIAN BIX, LAW, LANGUAGE, AND LEGAL DETERMINACY 75 (1993))); *see also* Goldstein, *supra* note 32, at 115 ("Evidence of trade usage . . . allows parties to supplement dictionary definitions and the judge's understanding of common usage with evidence of other particular public usages of a term among particular groups . . . .").

367 *See* KNIFFIN, 5 CORBIN ON CONTRACTS, *supra* note 32, § 24.13, at 111 ("Just as a court would interpret according to the French language a contract written in French by two French speakers, a court will interpret according to trade usage a contract written by two parties familiar with a term common in that trade."); Goldstein, *supra* note 32, at 116 (analogizing trade usage to British English).

368 *See* Anchor Sav. Bank, FSB v. United States, 121 Fed. Cl. 296, 311 (2015) ("The use of extrinsic evidence to construe trade terms is best viewed as analogous to the lexicography rule for dictionaries rather than as an actual exception to the rule prohibiting extrinsic evidence for unambiguous contract provisions.").

conceptual claim: Under all types of partial contextualism, language can possess any meaning, just as it can under full contextualism. And that is so even when every piece of textual evidence within the four corners of an agreement supports the conclusion that the parties employed standard English when preparing the instrument. Therefore, since the words of a contract do not restrict the scope of potential interpretations, partial contextualism dispenses with the reasonably susceptible standard.

There is an additional problem with basing the third counterargument on a version of partial contextualism that restricts the ambiguity determination to the text of an agreement and trade usage: Little authority supports such an interpretive system. While my research was not exhaustive, most cases that I found embracing partial contextualism permit at least some categories of extrinsic evidence that are specific to the parties to play a role at stage 1—such as course of dealing and course of performance. This type of evidence can be employed to establish a meaning exclusive to the parties.[369] If such a meaning is possible, then the alternate language theory no longer applies to partial contextualism because private codes specific to contracting persons cannot plausibly be understood as distinct languages in the way French or an industry dialect can be.[370] Accordingly, partial contextualism, at least as generally used in the real world, eliminates the ambiguity determination.[371]

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369 *See* Pac. Gas & Elec. Co. v. G.W. Thomas Drayage & Rigging Co., 442 P.2d 641, 645 (Cal. 1968) ("The fact that the terms of an instrument appear clear to a judge does not preclude the possibility that the parties chose the language of the instrument to express different terms. That possibility is not limited to contracts whose terms have acquired a particular meaning by trade usage but exists whenever the parties' understanding of the words used may have differed from the judge's understanding.") (footnote omitted).

370 *Cf.* Ricks, *supra* note 18, at 788–89 (explaining that the "reasonably susceptible" standard "is an objective standard and as such must depend . . . on something *public*") (emphasis added).

371 Some additional explanation is in order. Based on my review, the bulk of the cases applying partial contextualism are decided under the U.C.C. And the Code's version of partial contextualism requires judges to consider course of performance and course of dealing, as well as usage of trade, when assessing ambiguity. *See supra* notes 193, 226–237, 356–359, and accompanying text. Likewise, common law opinions that are (or at least appear to be) employing partial contextualism often allow course of performance evidence at stage 1 of the interpretive process. *See, e.g.*, United Fire & Cas. Co. v. Arkwright Mut. Ins. Co., 53 F. Supp. 2d 632, 640–41 (S.D.N.Y. 1999); Time Warner Cable of N.Y.C. v. City of New York, 943 F. Supp. 1357, 1390 (S.D.N.Y. 1996); Eskimo Pie Corp. v. Whitelawn Dairies, Inc., 284 F. Supp. 987, 989–90, 992, 995 (S.D.N.Y. 1968); Stephens v. Radium Petrol. Co., Inc., 550 N.W.2d 39, 43 (Neb. 1996). Note further that courts endorsing "objective" evidence partial contextualism, *see supra* notes 192, 354–355, and accompanying text, typically permit parties to submit evidence beyond trade usage during the ambiguity determination. *See, e.g.*, Stryker Corp. v. Nat'l Union Fire Ins. Co. of

The most that can be said for partial contextualism is that this interpretive approach makes it harder than full contextualism for a party to establish that a contract is "ambiguous." It does so by limiting the types of evidence that possess the capacity to create an ambiguity. This mitigates the harm some might see in allowing all forms of extrinsic evidence—including self-serving testimony regarding preliminary negotiations—to establish that the parties may have used a non-standard meaning, thereby advancing the case to the next stage of the interpretive process.[372]

Pittsburgh, 842 F.3d 422, 428 (6th Cir. 2016) ("But in the ordinary course, a latent ambiguity must be revealed by objective means—for instance, an admission, uncontested evidence, or the testimony of a disinterested third party."). And even the cases holding that only extrinsic evidence provided by neutral third parties may establish a non-standard-meaning latent ambiguity, *see, e.g.*, *In re Envirodyne Indus., Inc.*, 29 F.3d 301, 305 (7th Cir. 1994), should not be read to restrict stage 1 to the text and industry practice. Third parties can testify regarding (1) other surrounding commercial circumstances, and (2) understandings specific to the contracting parties, though they probably will not have the latter type of information in most cases.

To be sure, many decisions provide that judges may review trade usage when assessing ambiguity without mentioning other types of extrinsic evidence. *See, e.g.*, *In re* Tech. for Energy Corp., 140 B.R. 214, 229 (Bankr. E.D. Tenn. 1992). But I came across no opinion expressly stating that trade usage is the *only* category of extrinsic evidence a party may present during the ambiguity determination. *Compare* Cheaves v. United States, 108 Fed. Cl. 406, 409 (2013) ("Although review of an unambiguous contract is generally limited to the contract itself, there are exceptions to the rule. *One* such exception is where trade practice and custom may inform the meaning of an otherwise unambiguous term.") (emphasis added). The closest I found to that type of case are authorities *suggesting* that stage 1 must be limited to the four corners and trade usage. For example, a line of federal decisions applying New York law endorses the following principle: "[A]n ambiguity exists where a contract term could suggest more than one meaning when viewed objectively by a reasonably intelligent person who has examined the context of the entire integrated agreement and who is cognizant of the customs, practices, usages and terminology as generally understood in the particular trade or business." World Trade Ctr. Props., L.L.C. v. Hartford Fire Ins. Co., 345 F.3d 154, 184 (2d Cir. 2003) (internal quotation marks omitted); *accord* Seiden Assocs., Inc. v. ANC Holdings, Inc., 959 F.2d 425, 428 (2d Cir. 1992); Random House, Inc. v. Rosetta Books LLC, 150 F. Supp. 2d 613, 618 (S.D.N.Y. 2001); *see also* Goldstein, *supra* note 32, at 76–79, 112–13, 126–27 (proposing an interpretive system that essentially restricts the ambiguity determination to the text of the contract and trade usage).

372 Note that in cases where the parties offer no extrinsic evidence of the type allowed at stage 1 under partial (or full) contextualism, the court must assess ambiguity by analyzing only the text within the four-corners of the agreement. In other words, partial and full contextualism operate just like textualism when the parties do not present any qualifying extrinsic evidence at stage 1. But it does not follow that either form of contextualism preserves the ambiguity determination in the relevant sense. The issue here is whether language imposes an absolute limit on the spectrum of possible meanings. *See supra* notes 304–306 and accompanying text. If language does not have that capacity, then the ambiguity determination has been eliminated. *See supra* notes 328–329, 332, and accompanying text. And under both partial and full contextualism, language can indeed possess any meaning if the permissible extrinsic evidence is strong enough. *See supra* text accompanying note 365. *See also infra* notes 398–399 and accompanying text (explaining that contextualist courts carefully analyze the ordinary meaning of language within the four corners of a contract even though such language does not have the limiting power it possesses under textualism).

The fourth argument is that some contextualist authorities preserve the ambiguity determination because they only permit extrinsic evidence to qualify the express terms of a contract. Such evidence may not be used to completely override express terms. To explain this distinction, consider the case of *Nanakuli Paving and Rock Company v. Shell Oil Company*.[373] Nanakuli, an asphaltic paving contractor, and Shell entered into a contract under which Shell was to supply asphalt to Nanakuli at "Shell's posted price at the time of delivery."[374] Nanakuli argued that the contract obligated Shell to provide Nanakuli with "price protection."[375] This means that after Shell raised its asphalt price, it was required to continue charging Nanakuli the old price for quantities Nanakuli needed to fulfill its obligations under construction contracts for which Nanakuli had made its bid using Shell's original price.[376] When Shell failed to provide such protection after a price increase, Nanakuli sued for breach.[377] At trial, Nanakuli submitted both course of performance and trade usage evidence that price protection was a component of the parties' contract, which the trial court admitted.[378]

On appeal, Shell argued that price protection could not be construed as reasonably consistent with the express term providing for sales at Shell's posted price.[379] The Ninth Circuit disagreed, explaining that incorporation tools evidence is admissible when it does not "totally negate" an express term but instead merely qualifies the term.[380] An example of total negation would be using extrinsic evidence to establish that Nanakuli rather than Shell was entitled to set the price for asphalt under the contract.[381] That would entirely override the provision stating asphalt was to be sold at "*Shell's* posted price at the time of delivery." But including price protection in the agreement only created a limited exception to the express provision that Nanakuli must pay Shell's posted price.[382] Most of Shell's asphalt was indeed sold at "Shell's posted price." Price protection merely requires that Shell sell to Nanakuli at the *old* posted price rather

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373 664 F.2d 772 (9th Cir. 1981).
374 *Id.* at 777–78.
375 *Id.* at 777.
376 *Id.*
377 *Id.*
378 *Id.* at 778.
379 *Id.* at 779.
380 *Id.* at 780, 805.
381 *Id.* at 805.
382 *Id.* at 780, 805.

than the current one for brief periods after a price increase. Thus, price protection only qualifies or "cuts down" the posted price term; it does not completely negate it.[383] In sum, *Nanakuli* stands for the proposition that interpretive extrinsic evidence can support a *partial* contradiction of express terms, but not a *complete* contradiction.[384]

Many cases decided under the U.C.C. are in accord with *Nanakuli*.[385] As are some common law authorities.[386] Does this

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383 *Id.*

384 *Id.* It might be better to conceptualize the price protection evidence in *Nanakuli* as supporting the existence of a distinct contractual term rather than as assisting in construing the phrase "Shell's posted price." But either way, *Nanakuli* is particularly useful for explaining the distinction between a partial contradiction and a complete contradiction.

385 *See* Lisa Bernstein, *Custom in the Courts*, 110 NW. U. L. REV. 63, 69–70, 82, 84–85 (2015) (concluding that the *Nanakuli* approach is the majority rule under the U.C.C.); *but cf.* Silverstein, *supra* note 106, at 1080–81 n.399 (collecting authorities finding that other approaches are the majority view under the Code). For another helpful example, see State *ex rel.* Nichols v. Safeco Ins. Co. of Am., 671 P.2d 1151, 1154–55 (N.M. Ct. App. 1983) ("Evidence as to usage of trade is admissible in construing a written contract . . . to add to, subtract from or qualify the terms of the agreement or to explain their meaning, even if contradictory to the words therein. Parol evidence is not admissible, however, when it would *change the basic meaning* of the contract and produce an agreement *wholly different* from, *wholly inconsistent* with the written agreement and which tends to distort the expressly stated written understanding of the parties." (emphasis added and citations omitted)) (holding that the trial court correctly refused to consider one party's proffer of trade usage evidence that leased equipment could be returned early for a rent deduction because the evidence was inconsistent with the express terms of the contract which specified a rental price and a rental period of eight months).

386 *See, e.g.*, Bohler-Uddeholm Am. Inc. v. Ellwood Grp., Inc., 247 F.3d 79, 95 n.4 (3d Cir. 2001) ("In our analysis, we differentiated between using extrinsic evidence to support an alternative interpretation of a term that sharpened its meaning (legitimate) and an interpretation that completely changed the meaning (illegitimate): 'extrinsic evidence may be used to show that "Ten Dollars paid on January 5, 1980," meant ten Canadian dollars, but it would not be allowed to show the parties meant twenty dollars.'") (referring to and quoting from Mellon Bank, N.A. v. Aetna Bus. Credit, Inc., 619 F.2d 1001, 1013 (3d Cir. 1980)); *id.* at 93 ("Furthermore, the alternative meaning that a party seeks to ascribe to the specific term in the contract must be reasonable; courts must resist twisting the language of the contract beyond recognition."); *In re* Tobacco Cases I, 111 Cal. Rptr. 3d 313, 320–21 (Cal. Ct. App. 2010) ("The reason underlying the rule [allowing evidence of course of performance] is that it is the duty of the court to give effect to the intention of the parties where it is not *wholly at variance* with the correct legal interpretation of the terms of the contract, and a practical construction placed by the parties upon the instrument is the best evidence of their intention. . . . Here, as discussed, the [master settlement agreement's] definition of the term 'cartoon' is not susceptible to the interpretation Reynolds urges. Accordingly, we do not consider course of performance evidence.") (emphasis added and citations and internal quotation marks omitted); Winet v. Price, 6 Cal. Rptr. 2d 554, 558–60 (Cal. Ct. App. 1992) ("Further, parol evidence is admissible only to prove a meaning to which the language is 'reasonably susceptible,' *not to flatly contradict the express terms of the agreement*. Winet's evidence violates this tenet, because it seeks to prove that a release of unknown or unsuspected claims was *not* intended to include unknown or unsuspected claims.") (first emphasis added and citations omitted); Gerdlund v. Elec. Dispensers Int'l, 235 Cal. Rptr. 279, 283–84 (Cal. Ct. App.

interpretive approach—under which extrinsic evidence may only support an interpretation that *partially* contradicts the language of a contract—preserve the ambiguity determination? Professor Steven Burton believes that the answer is no. He reasons that "[e]ven a partial contradiction entails that a meaning is being given to the express term that is not within its array of reasonable meanings."[387] In other words, Professor Burton maintains that any type of contradiction, partial or complete, violates the reasonably susceptible standard. And in a prior article, I articulated a similar view.[388]

But if complete contradictions are ruled out by the *Nanakuli* approach, then the language of an agreement, by itself, imposes genuine limits on the spectrum of possible meanings the agreement may possess. Contractual language is not infinitely flexible under this approach. The express terms of a contract bar the parties from advancing certain readings no matter how strong the extrinsic evidence. As a result, contract language possesses "a critical breaking point,"[389] as required by the reasonable susceptibility standard.

The question thus appears to be this: What is essential to the concept of reasonable susceptibility? Is it enough that language, standing alone, places *some* objective limits on the interpretive process, such as the restriction on complete contradiction adopted by *Nanakuli*? Or must the limits be more robust as Professor Burton asserts, restricting contract interpretation to readings that do not *in any way* contradict the express terms? I do not have an answer here. In part, that is because the concept of "reasonably susceptible" is not sufficiently delineated in the

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1987) (explaining that a provision permitting termination of the contract at will cannot be interpreted to permit termination only for good cause because the two interpretations are "totally inconsistent" and "[t]estimony of intention which is contrary to a contract's express terms . . . does not give meaning to the contract: rather it seeks to substitute a different meaning. It follows under [*Pacific Gas*] that such evidence must be excluded."); *see also* Stryker Corp. v. Nat'l Union Fire Ins. Co. of Pittsburgh, 842 F.3d 422, 427–28 (6th Cir. 2016) (applying Michigan law) (endorsing a form of partial contextualism but holding that extrinsic evidence could not be used to show that an insurance policy covering claims settled "with the written consent" of the insurer actually meant that no consent was required if a claim was settled for under the coverage limits in the policy).

387 BURTON, *supra* note 1, § 4.5.2, at 140.

388 *See* Silverstein, *supra* note 106, at 1079 ("[Textualism] requires the judge to determine whether the language contained within the four corners of a written agreement is reasonably susceptible to the interpretations asserted by both parties. But that simply means that the judge must decide whether one of the parties is trying to contradict rather than construe the contractual language with its alleged understanding of the agreement.").

389 *See supra* note 305 and accompanying text.

caselaw to arbitrate between Professor Burton's view and the alternative. But more importantly, the answer does not matter. That is because the *Nanakuli* method of contract interpretation is not actually a form of contextualism. Instead, it is a hybrid approach that falls between contextualism and textualism.

Recall the essence of contextualist interpretation: The parties are entitled to submit extrinsic evidence during the first stage of the interpretive process.[390] In fact, it is reversible error when a trial judge refuses to consider extrinsic evidence in deciding whether a contract is "ambiguous."[391] Accordingly, the ambiguity determination must take place after discovery under contextualism—i.e., after the pleadings stage[392]—except in special circumstances.[393]

The essence of textualism is the four-corners rule: the first stage of the interpretive process is restricted to the language falling within the four corners of the contract.[394] Because the court is prohibited from considering extrinsic evidence during the ambiguity determination, that determination can occur at the pleading stage under textualism.[395]

The *Nanakuli* approach operates like contextualism in some cases and like textualism in other cases. That decision and comparable authorities provide that a judge may consider extrinsic evidence during the first stage of the interpretive process if the evidence is used to advance a construction that *partly* contradicts the agreement. If one of the parties advances a reading that *completely negates* an express provision, however, then the court should adjudicate the matter solely via reference to the terms of the contract. Thus, for example, had Nanakuli argued that "Shell's posted price" actually meant "Nanakuli's posted price," the court would have granted a motion to dismiss by Shell based solely on the complaint and the contract. This makes the *Nanakuli* approach a hybrid school of interpretation: (1) Contextualism virtually always permits extrinsic evidence at stage 1; (2) textualism never does;[396] and (3) *Nanakuli* allows extrinsic evidence at stage 1 *some* of the time. Under the *Nanakuli*

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390 *See supra* text accompanying notes 52–53, 60–61, 199, 209, and 213.

391 *See supra* note 323 and accompanying text.

392 *See supra* text accompanying notes 199–200, 213, and 218; see also *supra* the text early in the paragraph after note 240 and *supra* Chart 1 in Part V.B (located at note 238).

393 *See supra* text accompanying notes 241–244.

394 *See supra* text accompanying notes 37 and 58–59.

395 *See supra* text accompanying notes 169 and 178; *see also supra* Chart 1 in Part V.B (located at note 238).

396 Once again, set aside subject-matter latent ambiguities.

framework, some cases will address ambiguity at the pleading stage based solely on the four corners of the contract (as with textualism), whereas in others the judge will conduct the ambiguity determination at summary judgment based on the text of the agreement and extrinsic evidence (as under contextualism).[397]

Since *Nanakuli* is a hybrid method of interpretation, "quasi-ambiguity determination" is the most logical way to describe the first stage of that approach. *Nanakuli* permits some level of contradiction. Professor Burton is thus correct that this approach does not fully embrace the "reasonably susceptible" standard. However, because language places absolute limits on the spectrum of contractual meaning under *Nanakuli*, the case does embrace the reasonably susceptible standard to at least some degree. Hence my proposal that we use the phrase "*quasi*-ambiguity determination."

The issue addressed in this section is whether *contextualism* preserves the ambiguity determination. The *Nanakuli* approach is not actually a type of contextualism. The structure of that approach is thus ultimately irrelevant to resolving the central issue here.

All of the counterarguments challenging my conclusion that contextualism eliminates the assessment of ambiguity are invalid. Therefore, contextualist interpretation does indeed dispense with the requirement that the proffered readings of a contract satisfy the reasonably susceptible standard.

C. Further Points Regarding Contextualism and the Ambiguity Determination

Several additional points regarding contextualism and ambiguity are worth noting. First, when I state that contextualism "eliminates" the ambiguity determination, I mean to convey only that contextualism jettisons the mandate that the construction of a contract satisfy the reasonably susceptible standard. As noted at the end of Part VII.A,[398] the express terms of an agreement remain the most significant evidence of intent in contextualist interpretation. The level of clarity within the four

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397 Note that in a prior article, I stated that the *Nanakuli* approach "can fairly be labeled as contextualist." *See* Silverstein, *supra* note 106, at 1081; *id.* at 1076–77 (describing the *Nanakuli* approach). However, that was for the purposes of a potential empirical study, not for an article regarding "conceptual clarification."

398 *See supra* notes 343–344 and accompanying text.

corners of a contract is thus relevant at both stages of the interpretive process even if contractual language places no absolute restriction on the scope of potential meanings. Accordingly, courts in contextualist jurisdictions do in fact assess whether a patent ambiguity exists—i.e., they carefully analyze the ordinary meaning of contract language.[399] Additional detail regarding the impact of a patent ambiguity under contextualism is presented in Part VIII.

Second, assuming contextualism eliminates the assessment of ambiguity, what effect does that have on the parol evidence rule? By dispensing with the ambiguity determination, contextualist interpretation permits the use of interpretive extrinsic evidence to contradict the written terms of a contract.[400] Does this entail that contextualism also eliminates the contradiction prong of the parol evidence rule?[401] Some authorities have suggested that conclusion.[402] This issue is covered in Part IX.

Third, contextualist courts might find certain "extreme" contradictions to be intolerable even if they generally permit extrinsic evidence to completely override the ordinary meaning of an express term. Recall the *Restatement* illustration in which "thousand" meant 1200.[403] Or consider *Columbia Nitrogen Corporation v. Royster Company*, where the court ruled that extrinsic evidence that express price and quantity terms in a contract were only projections rather than binding obligations should have been submitted to the jury.[404] Contextualist judges willing to endorse these examples might balk at the following hypothetical.

Suppose a written contract provides that "A shall sell his 2010 Toyota Camry to B for $5,000." After a dispute erupts, B sues A asserting that the contract language just quoted actually requires that A purchase B's house for $250,000 pursuant to the private code adopted orally by the parties during preliminary negotiations, and that A is in breach for not paying the $250,000. A moves to dismiss

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399 *See, e.g.*, Wolf v. Superior Court, 8 Cal. Rptr. 3d 649, 656–62 (Cal. Ct. App. 2004) (discussing thoroughly both the text of the disputed contract and the proffered extrinsic evidence in deciding whether the agreement was ambiguous).

400 *See supra* notes 321–331 and accompanying text.

401 The contradiction prong of the parol evidence rule is discussed *supra* in the text accompanying notes 71–72.

402 *See infra* notes 537–540 and accompanying text.

403 RESTATEMENT (SECOND) OF CONTRACTS § 220 illus. 8 (AM. L. INST. 1981).

404 451 F.2d 3, 6–11 (4th Cir. 1971); *accord* Am. Mach. & Tool Co., v. Strite-Anderson Mfg. Co., 353 N.W.2d 592, 596–98 (Minn. Ct. App. 1984).

B's complaint. I suspect that at least some contextualist courts would find that extrinsic evidence can *never* be strong enough to support the interpretation advanced by B—even if the evidence included the testimony of "twenty bishops."[405] And thus these courts would grant A's motion to dismiss. Such an example arguably goes beyond the "complete negation" of a term. Instead, it wholly reworks the entire contract. If any contextualist authorities would resolve such a case on the pleadings, then those courts also arguably embrace the reasonable susceptibility standard to at least some degree.[406]

However, my example here is so farfetched that I do not think it should influence how we label interpretive approaches. Accordingly, it is proper to classify the *Columbia Nitrogen* court and the *Restatement* as "contextualist" even though, in theory, some interpretations might be so bizarre that these authorities would not permit extrinsic evidence on the matter, much like the courts applying the hybrid system of *Nanakuli* or textualism.

Fourth, recall the discussion in Part VI regarding how it is often difficult or impossible to establish whether a court is using textualism or contextualism. The same problem arises with respect to whether a court is using one of those two approaches or the hybrid approach of *Nanakuli*. *ACL Technologies, Inc. v. Northbrook Property & Casualty Insurance Company* is illustrative.[407]

In that case, the California Court of Appeal appeared to endorse the hybrid approach in two ways. First, it said that extrinsic evidence cannot be used to completely negate an express term: "Indeed, if there is a key word in California's statement of the parol evidence rule it is 'contradict.' Whatever

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405 Hotchkiss v. Nat'l City Bank of N.Y.C., 200 F. 287, 293 (S.D.N.Y. 1911) (Hand, J.) ("If, however, it were proved by twenty bishops that either party, when he used the words, intended something else than the usual meaning which the law imposes upon them, he would still be held, unless there were some mutual mistake, or something else of the sort.").

406 *See, e.g.*, Taylor v. State Farm Mut. Auto. Ins. Co., 854 P.2d 1134, 1139 (Ariz. 1993) ("[T]he judge may properly decide not to consider certain offered evidence because it does not aid in interpretation but, instead, varies or contradicts the written words. This might occur when the court decides that the asserted meaning of the contract language is so unreasonable or extraordinary that it is improbable that the parties actually subscribed to the interpretation asserted by the proponent of the extrinsic evidence.") (citations omitted); Consol. World Invs., Inc. v. Lido Preferred Ltd., 11 Cal. Rptr. 2d 524, 527 (Cal. Ct. App. 1992) ("Thus if the contract calls for the plaintiff to deliver to defendant 100 pencils by July 21, 1992, parol evidence is not admissible to show that when the parties said 'pencils' they really meant 'car batteries' or that when they said 'July 21, 1992' they really meant 'May 13, 2001'.").

407 22 Cal. Rptr. 2d 206 (Cal. Ct. App. 1993).

else extrinsic evidence may be used for, it may not be used to show that words in contracts mean the *exact opposite* of their ordinary meaning."[408] Second, the court stated that language constrains the scope of possible interpretations: "'Unlike the deconstructionists at the forefront of modern literary criticism, the courts still recognize the possibility of an unambiguous text.'"[409] "With all due respect to the critics of *Pacific Gas,* the case is not an endorsement of linguistic nihilism."[410] But immediately after the last quotation, the California Court of Appeal reversed course and endorsed full-blown contextualism by explaining that extrinsic evidence may demonstrate that a word in a contract holds a special meaning that is indeed the exact opposite of its ordinary meaning:

> Despite what might be called [*Pacific Gas*'s] "deconstructionist" dictum, the actual holding of the case is a fairly modest one: courts should allow parol evidence to explain *special* meanings which the individual parties to a contract may have given certain words. No such evidence, of course, was ever offered in the case before us. There is nothing to indicate, for example, that an agent of Northbrook told an officer of ACL that, despite the ordinary meaning of "sudden" as "not gradual," Northbrook would agree to give the word a special meaning in the particular policy it was about to issue so that it would mean "gradual." *That* is the sort of thing contemplated by *Pacific Gas.*[411]

"Gradual" is the exact opposite of "sudden." If "sudden" can mean "gradual" when the extrinsic evidence is strong enough, then total negation is allowed and language places no genuine limits on the spectrum of possible interpretations.[412]

Fifth, part of the reason that the contextualist and hybrid-approach jurisprudence is so confused regarding the roles of ambiguity and contradiction in the interpretive process is that contextualism is built upon a fundamental conceptual mistake. While it was not the first case to adopt contextualist

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408 *Id.* at 217 (emphasis added and citation and footnote omitted).

409 *Id.* (quoting Ideal Mut. Ins. Co. v. Last Days Evangelical Ass'n, 783 F.2d 1234, 1238 (5th Cir. 1986)).

410 *Id.* at 219.

411 *Id.* (emphasis in original and footnote omitted); *id.* at 217–19 (explaining further that no valid extrinsic evidence was presented that the parties adopted a special meaning under which the word "sudden" included the concept "gradual").

412 For other decisions applying California law where it is impossible to determine which interpretive approach the court is using, see *RLI Ins. Co. v. City of Visalia*, 297 F. Supp. 3d 1038, 1048–51 (E.D. Cal. 2018), and *BHC Interim Funding II, L.P. v. FDIC*, 851 F. Supp. 2d 131, 139–41 (D.D.C. 2012).

interpretation,[413] *Pacific Gas and Electric Company v. G. W. Thomas Drayage and Rigging Company*[414] is the watershed decision that paved the way for modern acceptance of contextualism.[415] There, Chief Justice Roger Traynor, on behalf of the California Supreme Court, wrote the following when rejecting the four-corners rule:

> The test of admissibility of extrinsic evidence to explain the meaning of a written instrument is not whether it appears to the court to be plain and unambiguous on its face, but whether the offered evidence is relevant to prove a meaning to which the language of the instrument is reasonably susceptible.[416]

In the years since *Pacific Gas* was decided, numerous contextualist authorities have quoted or paraphrased this language in setting forth the operation of stage 1 of the interpretive process.[417] But Chief Justice Traynor's statement is confused.

Again, here is what he wrote: "The test . . . is not whether [the instrument] appears . . . *unambiguous* on its face, but whether the offered evidence is relevant to prove a meaning to which the language of the instrument is *reasonably susceptible*."[418] That is internally inconsistent. Chief Justice Traynor is saying the test is not ambiguity; it is reasonable susceptibility. But ambiguity and reasonable susceptibility are the same thing. Language *just is* ambiguous when it is reasonably susceptible to more than one meaning.[419] Distinguishing between "ambiguity" and "reasonable susceptibility" is like distinguishing between "bachelors" and "unmarried males."[420]

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413 *See, e.g.*, Atl. N. Airlines v. Schwimmer, 96 A.2d 652, 656 (N.J. 1953).

414 442 P.2d 641 (1968).

415 Silverstein, *supra* note 13, at 275; *accord* Carlton J. Snow, *Contract Interpretation: The Plain Meaning Rule in Labor Arbitration*, 55 FORDHAM L. REV. 681, 690 (1987) (recognizing *Pacific Gas* as initiating the "frontal attack on the plain meaning rule").

416 *Pacific Gas*, 442 P.2d at 644.

417 *See, e.g.*, Halicki Films, LLC v. Sanderson Sales and Mktg., 547 F.3d 1213, 1223 (9th Cir. 2008) (applying California law); Pennzoil Co. v. Fed. Energy Regul. Comm'n, 645 F.2d 360, 388 (5th Cir. 1981) (applying federal common law); Taylor v. State Farm Mut. Auto. Ins. Co., 854 P.2d 1134, 1141 (Ariz. 1993); Winet v. Price, 6 Cal. Rptr. 2d 554, 557 (Cal. Ct. App. 1992); Harrigan v. Mason & Winograd, Inc., 397 A.2d 514, 516 (R.I. 1979).

418 *Pacific Gas*, 442 P.2d at 644 (emphasis added).

419 *See* BURTON, *supra* note 1, § 1.3.3, at 32 (explaining that the *Pacific Gas* reasonably susceptible test "is the same as a requirement that the language be ambiguous—that it reasonably bear more than one meaning").

420 Admittedly, Chief Justice Traynor wrote that the improper test is whether an agreement "is . . . unambiguous *on its face*," *Pacific Gas*, 442 P.2d at 644 (emphasis

It is puzzling why Chief Justice Traynor attempted to create such a distinction. By the time of *Pacific Gas*, it was well established that a contract is ambiguous when it is reasonably susceptible to more than one meaning. Numerous cases recognized this definition,[421] including some in California.[422] As did contracts treatises[423] and general legal encyclopedias.[424]

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added), whereas he later said that reasonable susceptibility is judged based on the contract *and* extrinsic evidence, *id.* Thus, while Traynor was clearly using the traditional definition of ambiguity, see *supra* notes 347–350 and accompanying text (describing two definitions of ambiguity), it is possible that he was employing a non-traditional understanding of "reasonably susceptible," such as the broader notion discussed *supra* at the text accompanying notes 351–353. But because Traynor did not elaborate further, we cannot know for certain precisely what he meant. Moreover, it was illogical for the judge to juxtapose "ambiguity" in its *traditional* sense with "reasonably susceptible" in its *non*-traditional sense when authorities had long considered the two concepts to be synonymous. *See infra* notes 421–423 and accompanying text. In any event, Traynor's words have created much confusion, see, e.g., *Hayter Trucking, Inc. v. Shell W. E&P, Inc.*, 22 Cal. Rptr. 2d 229, 238 (Cal. Ct. App. 1993) ("Thus, parol evidence may be admitted to explain the meaning of a writing when the meaning urged is one to which the written contract term is reasonably susceptible *or* when the contract is ambiguous.") (emphasis added), including among contracts professors, see, e.g., Kniffin, *supra* note 11, at 100 n.130 (attempting to distinguish between "ambiguity" and "reasonably susceptible").

421 *See, e.g.*, Zehnder v. Michaud, 145 F.2d 713, 714 (8th Cir. 1944) ("A contract is ambiguous when it is susceptible of two different meanings."); Friedman v. Va. Metal Prod. Corp., 56 So. 2d 515, 517 (Fla. 1952) ("A word or phrase in a contract is 'ambiguous' only when it is of uncertain meaning, and may be fairly understood in more ways than one. The term 'ambiguous' means susceptible of more than one meaning.") (citation omitted); Blevins v. Riedling, 158 S.W.2d 646, 648 (Ky. 1942) ("A contract is ambiguous when its language is reasonably susceptible of different constructions."); Emps. Liab. Assur. Corp. v. Morse, 111 N.W.2d 620, 624 (Minn. 1961) ("A contract is ambiguous if it is reasonably susceptible to more than one construction."). Courts sometimes articulated the same substantive definition using slightly different terminology. *See, e.g.*, United Packinghouse Workers v. Maurer-Neuer, Inc., 272 F.2d 647, 649 (10th Cir. 1959) ("Usually an ambiguity is said to exist when from a consideration of the entire instrument the meaning of the controverted words is capable of more than one conclusion.") (citing *Ambiguity*, BLACK'S LAW DICTIONARY 105 (4th ed. 1951)); Gardner v. Spurlock, 339 P.2d 65, 69 (Kan. 1959) ("Ambiguity in a written instrument does not appear until application of pertinent rules of interpretation to the face of the instrument leaves it genuinely uncertain which one of two or more meanings is the proper meaning.") (internal quotation marks omitted).

422 *See, e.g.*, Holtham v. Savory, 238 P. 136, 138 (Cal. Ct. App. 1925) ("The rule contended for by appellant is only applicable where the language used in the contract is ambiguous, or fairly susceptible of either one of two interpretations contended for by the parties, in which event parol evidence is always admissible for the purpose of construing the contract according to the true intent of the parties at the time of its execution."); *see also* Susan J. Martin-Davidson, *Yes, Judge Kozinski, There Is a Parol Evidence Rule in California—The Lessons of a Pyrrhic Victory*, 25 SW. U. L. REV. 1, 50 (1995) (explaining that the reasonable susceptibility test articulated by Chief Justice Traynor in *Pacific Gas* "was not new in California law").

423 *See, e.g.*, 2 WILLIAM F. ELLIOTT, COMMENTARIES ON THE LAW OF CONTRACTS § 1517, at 791–92 (1913) (explaining that a contract is ambiguous when it is "susceptible of more than one construction"); 4 WILLIAM HERBERT PAGE, THE LAW OF CONTRACTS § 2036, at 3518 (2d ed. 1920) ("If a promise is so ambiguous as to be susceptible of more than one interpretation. . . ."); LAURENCE P. SIMPSON, HANDBOOK OF THE LAW OF

Professor Val Ricks identifies another way in which *Pacific Gas* is internally inconsistent.[425] In his opinion, Chief Justice Traynor endorsed the infinite flexibility of language:

> Words, however, do not have absolute and constant referents. A word is a symbol of thought but has no arbitrary and fixed meaning like a symbol of algebra or chemistry. The meaning of particular words or groups of words varies with the verbal context and surrounding circumstances and purposes in view of the linguistic education and experience of their users and their hearers or readers (not excluding judges). A word has no meaning apart from these factors; much less does it have an objective meaning, one true meaning.[426]

But Chief Justice Traynor also embraced the principle that an interpretation of a contract is valid only if the language of the agreement is reasonably susceptible to the proposed reading.[427] This standard presumes that language can confine the spectrum of possible meanings—i.e., that language is *not* infinitely flexible.

Given the incoherence flowing through the fountainhead of contextualism, it should not be surprising that subsequent authorities using that approach to interpretation—or the hybrid approach—are riddled with confusion. Indeed, the *Restatement (Second) of Contracts* suffers from this problem. As noted above, the *Restatement* adopts a theory of language use in contracting under which the express terms of an agreement can possess any meaning.[428] And the *Restatement* expressly provides that interpretive extrinsic evidence can be used to vary the meaning of a contract—to contradict it.[429] But the *Restatement* also states in two places that extrinsic evidence may only be used to support an interpretation if the language of the parties' contract is "reasonably susceptible" to the asserted reading.[430] And

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CONTRACTS § 66, at 239 (1954) ("The words may be on their face ambiguous and susceptible of different meanings.").

424 *See, e.g.*, 12 AM. JUR. *Contracts* § 229, at 752 (1938) ("It has been said that it is only where the language of a contract is ambiguous and uncertain and susceptible of more than one construction that a court may, under the well-established rules of construction, interfere to reach a proper construction and make certain that which in itself is uncertain."); 13 C.J. *Contracts* § 514, at 542 (1917) ("In arriving at the intention of the parties, where the language of a contract is susceptible of more than one construction it should be construed in the light of the circumstances surrounding them at the time it is made . . . .").

425 Ricks, *supra* note 18, at 788–89, 789 n.106.

426 Pac. Gas & Elec. Co. v. G.W. Thomas Drayage & Rigging Co., 442 P.2d 641, 644–45 (Cal. 1968) (internal quotation marks and citations omitted).

427 *Id.* at 644.

428 *See supra* notes 317–335 and accompanying text.

429 *See supra* notes 330–331 and accompanying text.

430 *See* RESTATEMENT (SECOND) OF CONTRACTS § 213 cmt. b (AM. L. INST. 1981)

elsewhere it contains additional material implying that the language of a contract restricts the scope of potential interpretations.[431] Accordingly, like Chief Justice Traynor in *Pacific Gas*, the *Restatement* tries to have it both ways.[432] If even the *Restatement* could not get the rules of interpretation straight, it should not be surprising that generations of judges, lawyers, and law students have struggled with contract interpretation and the parol evidence rule.

Sixth, and last, it is worth considering whether the analysis in this section justifies adopting further changes to the nomenclature of contract interpretation. In Part III, I described textualism as recognizing patent ambiguities and subject-matter latent ambiguities, whereas contextualism recognizes both of these plus non-standard-meaning latent ambiguities.[433] Does my conclusion here that contextualism jettisons the ambiguity determination warrant a change to that taxonomy?

To assist in answering this question, here is an alternative way of describing contextualism: Contextualism allows a judge to consider extrinsic evidence when there is a patent ambiguity, to establish a subject-matter latent ambiguity, or to establish a special meaning. This delineation substitutes "special meaning" for "non-standard-meaning latent ambiguity." Moreover, since there is only one type of latent ambiguity under this new conceptual scheme, the description can be simplified further by shortening "subject-matter latent ambiguity" to just "latent ambiguity": Contextualism recognizes patent ambiguities, latent ambiguities, and special meanings.

("[B]ut the integrated agreement must be given a meaning to which its language is reasonably susceptible when read in the light of all the circumstances."); *id.* § 215 cmt. b ("But the asserted meaning must be one to which the language of the writing, read in context, is reasonably susceptible.").

431 *See, e.g.*, *id.* § 202 cmt. g ("But such 'practical construction' is not conclusive of meaning. Conduct must be weighed in the light of the terms of the agreement and *their possible meanings*.") (emphasis added); *see also* LINZER, 6 CORBIN ON CONTRACTS, *supra* note 8, § 25.16[D], at 226 ("Actually, it is the reasonably susceptible language of [*Pacific Gas*] that has given proponents of a stricter parol evidence rule a weapon. That formula is widely used. Even the Restatement (Second) of Contracts . . . says that the asserted meaning of extrinsic evidence 'must be one to which the language of the writing, read in context, is reasonably susceptible.'").

432 In fairness, it is possible that the *Restatement* is using a different understanding of "reasonably susceptible," such as the broader notion discussed *supra* at the text accompanying notes 351–353. *See* RESTATEMENT (SECOND) OF CONTRACTS § 215 cmt. b ("But the asserted meaning must be one to which the language of the writing, *read in context*, is reasonably susceptible.") (emphasis added). I suggested the same with respect to Chief Justice Traynor's *Pacific Gas* opinion in note 420 *supra*.

433 *See supra* text accompanying notes 150–151.

Support for this revised framework can be found in the fact that ambiguity is generally understood as reasonable susceptibility, under which language has a breaking point. Patent ambiguities directly implicate the reasonably susceptible standard, and subject-matter latent ambiguities are consistent with it. But non-standard-meaning latent ambiguities violate the standard because allowing for special meanings constitutes a rejection of the limiting power of language. Thus, there is logic in avoiding the term "ambiguity" when describing the use of extrinsic evidence to establish a special meaning. Put another way, since non-standard-meaning latent ambiguities do not actually concern ambiguity as reasonable susceptibility, it is better to simply refer to "special meanings" without the word "ambiguity." And some cases in fact distinguish between assessing whether there is an ambiguity and assessing whether a special meaning exists.[434]

Recall, however, that "ambiguity" can also be understood in a broader sense to encompass uncertainty about the intended meaning of a word on grounds that are distinct from the reasonably susceptible standard, such as where a word has both an ordinary meaning and a special meaning.[435] This alternative conception of ambiguity constitutes a basis for retaining the phrase "non-standard-meaning latent ambiguity." As does the fact that use of the term "latent ambiguity" in the context of special meanings is strongly embedded in the interpretation caselaw.[436] The principal problem with continuing to employ the locution I proposed in Part III is that the word "ambiguity" holds one meaning in the phrase

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434 *See, e.g.*, Pepcol Mfg. Co. v. Denver Union Corp., 687 P.2d 1310, 1314 (Colo. 1984) ("It is only where the terms of an agreement are ambiguous or are used in some special or technical sense not apparent from the contractual document itself that the court may look beyond the four corners of the agreement in order to determine the meaning intended by the parties."); State *ex rel.* Petro v. R.J. Reynolds Tobacco Co., 820 N.E.2d 910, 915 (Ohio 2004) ("Courts resort to extrinsic evidence of the parties' intent only where the language is unclear or ambiguous, or where the circumstances surrounding the agreement invest the language of the contract with a special meaning.") (internal quotation marks omitted).

435 *See supra* text accompanying notes 347–350.

436 *See, e.g.*, Stryker Corp. v. Nat'l Union Fire Ins. Co. of Pittsburgh, 842 F.3d 422, 427 (6th Cir. 2016); Sault Ste. Marie Tribe of Chippewa Indians v. Granholm, 475 F.3d 805, 814 (6th Cir. 2007); Kerin v. U.S. Postal Serv., 116 F.3d 988, 992 n.2 (2d Cir. 1997); Nationwide Agribusiness Ins. v. George Perry & Sons, Inc., 338 F. Supp. 3d 1063, 1073 (E.D. Cal. 2018); Roosevelt Irrigation Dist. v. United States, No. CV-15-00448-PHX-JJT, 2017 WL 4364108, at *11 (D. Ariz. Sept. 30, 2017); Artesian Water Co. v. Chester Water Auth., No. 10-7453, 2012 WL 3029689, at *4–5 (E.D. Pa. July 24, 2012); Orth v. Wis. State Emps. Union Council 24, 500 F. Supp. 2d 1130, 1137 (E.D. Wis. 2007); Paris v. USI of S. Cal. Ins. Servs., Inc., No. B200225, 2008 WL 4182428, at *8–9 (Cal. Ct. App. Sept. 12, 2008); Wolf v. Superior Court, 8 Cal. Rptr. 3d 649, 655–56, 661 (Cal. Ct. App. 2004); Mind & Motion Utah Invs., LLC v. Celtic Bank Corp., 367 P.3d 994, 1004–05 (Utah 2016).

"patent ambiguity" (reasonable susceptibility) and another meaning in the phrase "non-standard-meaning latent ambiguity" (ordinary meaning versus special meaning). But this concern is likely not fatal because the "patent" and "non-standard-meaning latent" lead-ins convey that "ambiguity" is operating in two different contexts, and thus possesses two different meanings.

Since there are plausible bases for using either "non-standard-meaning latent ambiguity" or "special meaning" when describing the operation of contextualism, both terms are appropriate. I have a slight preference for "non-standard-meaning latent ambiguity," and that is the phrasing I emphasize when teaching contract interpretation to my students and throughout the rest of this Article. But I could easily see switching to "special meaning" in class at some point in the future.

VIII. ISSUE 6: WHEN DOES CONTRACT INTERPRETATION RAISE A JURY QUESTION?

Part V discussed the stages of interpretation. There, I explained that stage 2A of textualism concerns whether a contractual ambiguity can be resolved by the judge as a matter of law or must instead be resolved by a jury as a matter of fact, and that summary judgment is the primary procedural vehicle for addressing that issue.[437] Similarly, I concluded that stage 1 of both full contextualism and partial contextualism—the "ambiguity determination"—also concerns whether a jury question exists and generally takes place at summary judgment. In other words, a judge applying contextualism may adjudicate an interpretive dispute via summary judgment if the contract is "unambiguous," but must send the case to the jury for resolution as a question of fact if the agreement is "ambiguous."[438]

Part VII established that contextualism eliminates the ambiguity determination. As a result, when contextualist courts purport to address whether a contract is "ambiguous," they are actually assessing the general weight of the evidence; they are deciding whether the textual and extrinsic evidence justifies

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437 *See supra* notes 171–180 and accompanying text; Chart 1 (located *supra* at note 238).

438 Regarding full contextualism, see *supra* Part V.B.1. The most helpful material is contained in the text accompanying notes 202–205 *supra,* and in Chart 1 (located *supra* at note 238). Regarding partial contextualism, see *supra* Part V.B.2. The most helpful material is contained in the text accompanying notes 213–214 and 217–222, in the small paragraph between notes 225 and 226 *supra*, and in Chart 1 (located supra at note 238). See also the final paragraph of Part V.C. *supra*, which summarizes my labelling practices with respect to both versions of contextualism.

advancing the case to the next stage of the interpretive process—a jury trial. The courts are not analyzing whether the express terms of the agreement are reasonably susceptible to more than one meaning.[439]

This part addresses the circumstances in which interpretation raises a jury question under textualism and contextualism in light of my revised description of those approaches. Professor Steven Burton has observed that little authority exists regarding how contextualism distinguishes an unambiguous contract from an ambiguous one[440]—i.e., what separates disputes that raise a question of law for the judge from those that raise a question of fact for the jury.[441] And based on my own research, the decisions that do address this matter regularly conflict with each other or are internally inconsistent.[442] Accordingly, there is a particular need for guidance on the judge/jury issue with respect to contextualism.

The rest of Part VIII focuses on a series of nine hypothetical cases that are designed to provide direction regarding which types of interpretation lawsuits raise a jury question under textualism, full contextualism, and partial contextualism. The nine examples represent paradigms of disputes over contractual meaning. Note that Part VIII is not intended to serve as a comprehensive treatment of the circumstances in which interpretive matters are presented to a jury. That would require an independent article. Instead, my purpose here is less ambitious: It is to identify and analyze a variety of specific issues that together fall under the broad heading of "judge or jury as decision-maker" in contract interpretation.

Let me begin with several general points about the hypotheticals and my related analysis. First, all nine of the examples involve relevant extrinsic evidence. If the parties do not submit such evidence, the near-universal rule for all interpretative approaches is that contract construction is a

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439 *See supra* notes 340–342 and accompanying text.

440 *See* BURTON, *supra* note 1, § 4.3.3, at 128 ("Little authority explains just how this question of reasonable susceptibility should be answered under this contextual approach.").

441 *See id.* § 6.1.2.1, at 204–05 ("To elaborate, having identified a contract's terms, a court must decide upon motion—to dismiss, for summary judgment; to exclude evidence; or for a directed verdict—whether a term or the contract is ambiguous in the contested respect. *If there is no such ambiguity, there is nothing for a fact-finder to decide*.") (emphasis added).

442 For an example of the latter problem, see *W. States Constr. Co. v. United States*, 26 Cl. Ct. 818, 824–25 (1992).

question of law for the judge.[443] That is so even if the agreement is patently ambiguous and thus a reasonable jury could, in theory, adopt either reading of the instrument.[444] Accordingly, there is no need to address situations where the parties fail to proffer extrinsic evidence.

Second, throughout this Article, I have articulated the standard for deciding whether an interpretive dispute involving extrinsic evidence must be resolved by a judge or a jury as follows: Under textualism and contextualism, interpretation is a question of law if the interpretive evidence so heavily favors one side that there is no genuine issue of material fact—i.e., a reasonable jury could rule for only one party. If there is a genuine issue of material fact—i.e., a reasonable jury could rule for either side based on the evidence—then interpretation is a question of fact.[445] From here, I will refer to this version of the judge/jury standard as the "reasonable jury rule." And note that this rule is identical to the general standard for summary judgment under the rules of civil procedure.[446]

Third, the nine hypotheticals vary across two dimensions: (1) the content on the face of the agreement—i.e., is the contractual language clear or ambiguous; and (2) the nature of the extrinsic evidence—for example, does it overwhelmingly favor one side or is the evidence divided as between the interpretations asserted by the parties.

Fourth, six of the hypotheticals concern an alleged non-standard-meaning latent ambiguity. In these examples, the contract is clear on its face; the ordinary meaning of the

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443 *See supra* notes 49–50, 172–173, 241–244, and accompanying text.

444 *See* Pamado, Inc. v. Hedinger Brands, LLC, 785 F. Supp. 2d 698, 706–07 (N.D. Ill. 2011) (applying Illinois's textualist law); Wolf v. Superior Court, 8 Cal. Rptr. 3d 649, 656 (Cal. Ct. App. 2004) (applying California's contextualist law); BURTON, *supra* note 1, § 5.1.1, at 153.

445 *See supra* notes 49–50, 173–174, 202–208, 210 and accompanying text; *see also, e.g.*, ConocoPhillips Co. v. Lyons, 299 P.3d 844, 849 (N.M. 2012) ("Courts will grant summary judgment and interpret the meaning as a matter of law when the evidence presented is so plain that it is only reasonably open to one interpretation. If, however, a court determines that the contract is reasonably and fairly open to multiple constructions, then an ambiguity exists, summary judgment should be denied, and the jury should resolve all factual issues presented by the ambiguity.") (internal quotation marks and citations omitted).

446 *See* FED. R. CIV. P. 56(a) ("The court shall grant summary judgment if the movant shows that there is no genuine dispute as to any material fact and the movant is entitled to judgment as a matter of law."); Carman v. Tinkes, 762 F.3d 565, 566 (7th Cir. 2014) ("Summary judgment is appropriate when no material fact is disputed and the moving parties are entitled to judgment as a matter of law, meaning that no reasonable jury could find for the other party based on the evidence in the record.").

contested language is indisputable. But one side asserts that the parties intended that language to hold a special meaning. Textualism does not recognize non-standard-meaning latent ambiguities.[447] As a result, in these six cases, a judge applying textualism is barred from considering extrinsic evidence. Instead, the judge must, as a matter of law, adopt the standard meaning of the language contained within the four-corners of the agreement, and preferably at the pleading stage.[448] Since there is no cause for a judge in a textualist state to receive extrinsic evidence when a contract is facially unambiguous, the results in the examples below that involve that type of agreement only apply to contextualism.

The other three hypotheticals concern a patently ambiguous agreement. When such an ambiguity exists, a textualist court is obligated to consider extrinsic evidence.[449] Thus, the results in the remaining examples are relevant to both contextualism and textualism.

Fifth, the only difference between full contextualism and partial contextualism is the type of evidence that a court may consider in deciding whether an agreement is "ambiguous." The essence of stage 1—is there sufficient evidence such that a reasonable jury could rule for either side—is the same for both approaches.[450] Accordingly, I treat full and partial contextualism as a single position throughout the rest of this section.

Sixth, when a contract is patently ambiguous, the distinction between textualism and full contextualism evaporates.[451] As I explained in Part V, these two approaches follow the same process in deciding whether an interpretive dispute raises a jury question once the matter has moved past the pleading stage.[452] Thus, there is no need to distinguish between the textualist result and the contextualist result in the hypotheticals that involve a patent ambiguity; the results for the two approaches are identical in such cases.[453]

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447 *See supra* notes 150–151, and accompanying text.

448 *See supra* notes 167–170, 177–178, and accompanying text.

449 *See supra* notes 48, 56, 171 and accompanying text.

450 *See supra* Part V.B.

451 *See* Schwartz & Scott, *supra* note 4, at 963 n.94 ("But what if there is a genuine ambiguity in the written agreement? In such a case, the divide between formalist and antiformalist positions essentially disappears: a court will consider extrinsic evidence to resolve the ambiguity.").

452 *See supra* notes 202–208 and accompanying text.

453 As I noted in point four above, see *supra* text accompanying notes 447–449, the differences between textualism and contextualism *are* relevant in the six examples that

Pulling together points four, five, and six, if a hypothetical concerns a patent ambiguity, the resolution set forth below applies to textualism and both versions of contextualism. If a hypothetical concerns a non-standard-meaning latent ambiguity, the resolution below applies only to both versions of contextualism.[454]

Seventh, none of the hypotheticals involve a subject-matter latent ambiguity. That is because subject-matter latent ambiguities and patent ambiguities are essentially indistinguishable for purposes of deciding whether an interpretive dispute raises a question of law or fact. When an agreement suffers from either form of ambiguity, the express terms cannot in principle conclusively arbitrate between the readings advanced by the parties.[455] This means that the existence of a jury question in a case involving a patent ambiguity or a subject-matter latent ambiguity will generally turn on the balance of the extrinsic evidence. Thus, if the patent ambiguities in the hypotheticals below were changed to subject-matter latent ambiguities, the results in the examples would be the same.

Eighth, the nine hypotheticals fall into three categories: (1) cases where there is no jury question and thus the judge must adjudicate the dispute as a matter of law at summary judgment (four hypos); (2) cases where there is a jury question and thus the judge must deny any motions for summary judgment (three hypos); and (3) cases where it is debatable whether there is a jury question (two hypos). To better distinguish among the examples, I use a different set of labels for each category: letters early in the alphabet for the first category (which is one extreme); letters late in the alphabet for the second category (which is the other extreme); and letters near the middle of the alphabet for the third category (which is the area of uncertainty in between the two extremes).

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address a non-standard-meaning latent ambiguity because textualism does not recognize that type of ambiguity, whereas contextualism does.

454 Note that there is no need to separately discuss the *Nanakuli* hybrid approach, presented *supra* in Part VII.B, because that approach always operates like either textualism or contextualism. If a contract is patently ambiguous, all of the interpretive frameworks function in the same way. *See supra* notes 451–453 and accompanying text. If a contract is facially unambiguous and a party is attempting to establish a special meaning, then the hybrid approach operates like textualism when the party is trying to completely override one or more express terms and like contextualism when the party is trying to qualify the express terms of the agreement.

455 *See supra* text accompanying note 119.

Ninth, the resolutions to the seven hypotheticals in the first and second categories are primarily derived from the material set forth in prior sections of this Article and the logical implications of that material. However, I also cite to some authority in the footnotes that further supports my conclusions. For the two hypotheticals where I am unsure of the correct answer, my analysis turns on both the material above and the significant additional caselaw and secondary sources presented below.

Now we can turn to the hypotheticals.

A. Cases Where Interpretation Is for the Judge

The first category is cases where there is no jury question. For textualism, this means that the court ought to resolve the patent ambiguity at stage 2A as matter of law.[456] For contextualism, this means that the court ought to find that the contract is "unambiguous" at stage 1.[457] Both of these rulings are justified when the interpretive evidence so heavily favors one party that a reasonable jury would necessarily find in favor of that side.[458] This category contains four examples—Cases A through D.

Case A involves a facially unambiguous contract and extrinsic evidence that overwhelmingly or exclusively favors the same interpretation as the text of the agreement. In this type of lawsuit, there is no genuine issue of material fact and thus the judge should grant summary judgment to the party asserting the meaning supported by the text and the extrinsic evidence. For example, suppose Buyer and Seller enter into a contract providing that Seller will deliver lumber to Buyer on "December 15." After a dispute develops, Buyer argues for the standard meaning of "December 15" and Seller argues for a special meaning under which "December 15" means any time before January 1. At summary judgment,[459] all of the relevant extrinsic evidence supports the conclusion that the parties intended to adopt the standard meaning of "December 15." In this case, under contextualism, the judge should rule for Buyer as a matter of law because the textual and extrinsic evidence do not raise a jury question as to the meaning of the contract.[460]

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456 *See supra* notes 49–50 and accompanying text.

457 *See supra* text accompanying note 438.

458 *See supra* text accompanying notes 445–446.

459 Note that under textualism, this type of case can be addressed on the pleadings because there is no need for the judge to consider extrinsic evidence.

460 For an action that matches the structure of Case A, see *Columbia Gas*

Case B involves a facially unambiguous contract and extrinsic evidence that (1) is divided as between the readings advanced by the two parties, and (2) is weak. In this type of lawsuit, there is no genuine issue of material fact and thus the judge should grant summary judgment to the party asserting the meaning supported by the text. To illustrate, assume the same basic facts as those in Case A—a contract for delivery on "December 15" where Buyer argues for the standard meaning and Seller argues for a special meaning (delivery before January 1). This time, at summary judgment, there is extrinsic evidence supporting both parties' interpretations. But the evidence is weak: a single admission during discovery regarding the preliminary negotiations mildly supports Buyer and a single document from the preliminary negotiations mildly supports Seller. Here, under contextualism, the judge should rule for Buyer as a matter of law because the evidence does not raise a jury question as to the meaning of the contract. Divided, weak extrinsic evidence cannot create an issue for the finder of fact when the text of a contract unambiguously supports one side.

Case C involves a facially unambiguous contract and extrinsic evidence that (1) overwhelmingly or exclusively supports an interpretation that conflicts with the text of the agreement, and (2) is weak. In this type of lawsuit, there is no genuine issue of material fact and thus the judge should grant summary judgment to the party asserting the meaning supported by the text. For example, assume again the same basic facts as Case A—a contract for delivery on "December 15" where Buyer argues for the standard meaning and Seller argues for the special meaning. This time, all of the relevant extrinsic evidence favors the Seller. But the evidence is weak: a single document from the preliminary negotiations mildly supports Seller's construction. Here, under contextualism, the judge should rule for Buyer as a matter of law because the evidence does not raise a jury question as to the meaning of the contract. Weak extrinsic evidence

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Transmission Corp. v. New Ulm Gas, Ltd., 940 S.W.2d 587 (Tex. 1996). There, the parties disputed the meaning of a complex pricing provision in a contract for the sale of gas. *Id.* at 588–90. Both sides moved for summary judgment, but the trial court found the contract to be ambiguous, denied both motions, and submitted the matter to a jury, which ruled for the seller. *Id.* at 589. On appeal, the Texas Supreme Court found the agreement to unambiguously possess the meaning advanced by the buyer. *Id.* at 589, 592. All of the relevant contractual text supported the buyer, *id.* at 590–92, as did all of the permissible extrinsic evidence, *id.* at 591 & n.2. Accordingly, "the only reasonable interpretation of this contract" was buyer's, *id.* at 591, and "the parties' intent should not have been submitted to the jury," *id.* at 592.

favoring a special meaning cannot create an issue for the finder of fact when the text of a contract is unambiguous, even when there is no extrinsic evidence backing the ordinary meaning.[461]

Case D involves a facially ambiguous contract and extrinsic evidence that (1) overwhelmingly or exclusively favors one side's interpretation, and (2) is strong or moderate. In this type of lawsuit, there is no genuine issue of material fact and thus the judge should grant summary judgment to the party asserting the meaning supported by the extrinsic evidence. For example, assume this time that the contract between Buyer and Seller provides that Seller must deliver the lumber in "early December." In court, Buyer asserts that this phrase means by December 5, whereas Seller asserts that the phrase means by December 15. The words "early December" are reasonably susceptible to the meanings advanced by both parties. Thus, the agreement is patently ambiguous.[462] Assume further, however, that all of the

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461 For a decision that probably fits the structure of Case C, see *BNC Mortgage, Inc. v. Tax Pros, Inc.*, 46 P.3d 812 (Wash. Ct. App. 2002), *overruled on other grounds by* Columbia Cmty. Bank v. Newman Park, LLC, 304 P.3d 472, 479 (Wash. 2013). The contract there stated that Tax Pros subordinated a judgment that had already been entered. *Id.* at 821. However, an attorney for Tax Pros admitted to a contradictory interpretation in an affidavit. *Id.* at 820. The affidavit provided that the agreement was intended to subordinate all of Tax Pros' claims, which would also include a judgment entered into after execution of the contract. *Id.* BNC asserted that the affidavit created an ambiguity as to whether the agreement subordinated only the first judgment (as Tax Pros claimed) or both judgments (as BNC claimed). *Id.* The Washington Court of Appeals rejected BNC's argument, holding that the "affidavit is not by itself sufficient to take the case to a jury." *Id.* at 821. I stated that *BNC Mortgage* only "probably" mirrors Case C at the start of this footnote because the court may have based its holding in part on extrinsic evidence that favored Tax Pros' construction rather than on just the subordination contract and the affidavit. *See id.* at 820. But I think the better reading of the decision is that the critical ruling was driven solely by the contract and the affidavit. And if I am correct, then *BNC Mortgage* does indeed constitute an example of Case C. For another instructive lawsuit that mirrors Case C, see *Alexander v. Buckeye Pipe Line Co.*, 374 N.E.2d 146, 151 (Ohio 1978) (affirming summary judgment for the party asserting the ordinary meaning of the words "oil" and "gas" in a contract because the other side's trade usage evidence that the parties intended a special, narrower meaning of those terms—a single affidavit—was not sufficient to create a question of fact); *see also* Barris Indus., Inc. v. Worldvision Enters., Inc., 875 F.2d 1446, 1450 (9th Cir. 1989) (applying California law) ("Further, the mere existence of extrinsic evidence supporting an alternative meaning does not foreclose summary judgment where the extrinsic evidence is insufficient to render the contract susceptible to the non-movant's proffered interpretation.").

Note that if weak evidence that *contradicts* the ordinary meaning of an agreement's express terms cannot create an ambiguity (Case C), then, as a matter of logic, neither can weak *divided* evidence (Case B), nor evidence that is *consistent* with the ordinary meaning (Case A). Thus, authority that fits the structure of Cases A and B was unnecessary. However, I did find multiple decisions that nicely mirror Case A, and I included one in the relevant location above. *See supra* note 460 and accompanying text.

462 Because there is patent ambiguity, Case D would reach summary judgment under both contextualism and textualism. This type of case generally cannot be adjudicated on the pleadings.

relevant extrinsic evidence presented at summary judgment favors Buyer and is strong: preliminary negotiations documents, the course of performance, the course of dealing, and usages of trade all support Buyer's construction and no extrinsic evidence supports Seller's reading. Here, under both contextualism and textualism, the judge should rule for Buyer as a matter of law because the evidence does not raise a jury question as to the meaning of the contract. The same would be true if the extrinsic evidence exclusively favoring Buyer's interpretation, rather than being strong, was moderate in nature, such as just (1) documentation from the preliminary negotiations, or (2) several rounds of action by the parties that constitute a course of performance.[463]

B. Cases Where Interpretation Is for the Jury

The second category is cases where there is a jury question. For textualism, this means that the court ought to conclude at stage 2A that resolution of a patent ambiguity is for the trier of fact.[464] For contextualism, this means that the court ought to hold that the contract is "ambiguous" at stage 1.[465] Both of these rulings are justified when a reasonable jury could find for either party given the interpretive evidence.[466] This category contains three examples—Cases X through Z.

Case X involves a facially ambiguous contract and extrinsic evidence that is divided between the readings advanced by the two parties. In this type of lawsuit, there is a genuine issue of material fact and thus the judge should deny motions for

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463 *Gastar Expl. Inc. v. Rine*, 806 S.E.2d 448 (W. Va. 2017), is an excellent illustration of Case D. There, the language of the agreement was reasonably susceptible to three interpretations: the grantors of a piece of land intended to convey (1) all of their oil and gas rights (as the grantees argued), (2) none of their oil and gas rights (as the grantors argued), or (3) half of their oil and gas rights. *Id.* at 457. The court thus turned to extrinsic evidence, which demonstrated that after execution of the deed, the grantors stopped paying any taxes on the oil and gas rights at issue and the grantees began paying taxes on all of those rights. *Id.* at 452–53, 457. This supported the grantees' claim that the deed had conveyed all of the grantors' oil and gas rights. *Id.* And no extrinsic evidence supported either of the other readings of the agreement. *Id.* The weight of the evidence, combined with the principle that ambiguous deeds are construed in favor of the grantee, led the court to conclude that "there is no doubt that the [grantors] intended to convey the oil and gas interest to [the grantees]." *Id.* at 457. Accordingly, the court ruled that the trial judge erred in not granting summary judgment for the grantees. *Id.* at 458. *See also* Ames v. County of Monroe, 80 N.Y.S.3d 774, 777–78 (N.Y. App. Div. 2018) (resolving ambiguity as a matter of law because the only extrinsic evidence was "decades" of course of performance evidence that exclusively favored one party).

464 *See supra* notes 49–50, and accompanying text.

465 *See supra* text accompanying note 438.

466 *See supra* text accompanying notes 445–446.

summary judgment submitted by either party. For example, assume again the facts of Case D—a contract for delivery in "early December" where Buyer argues that Seller must deliver by December 5 and Seller argues that it must deliver by December 15. As before, the agreement is patently ambiguous. But this time, assume that the relevant extrinsic evidence is divided: preliminary negotiations and course of dealing evidence support Buyer while course of performance and trade usage evidence support Seller. Here, under both contextualism and textualism, the judge should deny any motion for summary judgment. Split textual and extrinsic evidence is the archetype of a dispute that must be decided by the finder of fact because a reasonable jury clearly can rule for either side in these circumstances.[467]

Case Y involves a facially unambiguous contract and extrinsic evidence that (1) overwhelmingly or exclusively favors an interpretation that conflicts with the text of the agreement, and (2) is moderate in weight. In this type of lawsuit, there is a genuine issue of material fact and thus the judge should deny motions for summary judgment submitted by either party. For example, assume again the same basic facts as Case A—a contract for delivery on "December 15" where Buyer argues for the standard meaning and Seller argues for the special meaning (delivery before January 1). In this example, all of the extrinsic evidence favors the Seller. And the evidence is moderate in weight: an established trade usage supports Seller's construction, but there is no other extrinsic evidence. Here, the judge should deny any motion for summary judgment. A split between textual evidence which supports the ordinary meaning and substantial extrinsic evidence that supports the conclusion that the parties

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467 *See* BURTON, *supra* note 1, § 5.1.1, at 153. For a case that fits the structure of Case X, see *Lion Oil Trading & Transp., Inc. v. Statoil Mktg. and Trading (US) Inc.*, 728 F. Supp. 2d 531 (S.D.N.Y. 2010). There, a contract for the sale of oil provided that the price was to be determined by market information "for the calendar month of delivery." *Id.* at 532. A dispute arose as to whether the language referred to the month intended at the time an order was made or to the actual month the oil was delivered. *Id.* at 531–32. At summary judgment, the court found that the agreement was facially ambiguous after analyzing several aspects of the text. *Id.* at 536. In addition, the parties submitted a great deal of extrinsic evidence with their motion papers. *Id.* at 537. But the evidence did not decisively support either side's interpretation. *Id.* at 536–37. To illustrate, one party proffered trade usage evidence in support of its construction, while the other presented course of dealing evidence favoring its reading. *Id.* at 537. The judge thus ruled that the interpretive issue was not "amenable to summary judgment" and instead constituted "a paradigmatic jury question." *Id.* For other helpful examples that follows this pattern, see *Swift & Co. v. Elias Farms, Inc.*, 539 F.3d 849, 851–55 (8th Cir. 2008), and *RCJV Holdings, Inc. v. Collado Ryerson, S.A. de C.V.*, 18 F. Supp. 3d 534, 541–48 (S.D.N.Y. 2014).

intended a non-standard meaning is the classic example of a lawsuit that raises a question of fact under contextualism (but not under textualism).[468]

Note that Case Y mirrors Case C in every respect but one: In Case C, the extrinsic evidence of a special meaning was weak and therefore not sufficient to create a jury question; in Case Y, it is moderate and therefore sufficient to create a jury question.

Case Z involves a facially unambiguous contract and extrinsic evidence that (1) is divided as between the readings advanced by the two parties, and (2) is strong or moderate. In this type of lawsuit, there is *probably* a genuine issue of material fact and thus the judge should deny motions for summary judgment submitted by either side.[469] For example, return once again to the facts of Case A—a contract for delivery on "December 15" where Buyer argues for the standard meaning and Seller argues for the special meaning. Assume this time that significant, relevant extrinsic evidence is presented at summary judgment, but the evidence is split: preliminary negotiations and course of dealing evidence support Buyer's argument for the ordinary meaning, while course of performance and trade usage evidence support Seller's argument for the special meaning. Here, under contextualism, the judge should deny any motion for summary judgment. While the textual evidence clearly favors Buyer, considerable extrinsic evidence supports both parties. Therefore, the textual and extrinsic evidence *as a whole* is substantially divided, and that warrants sending the interpretive issue to the jury for resolution as a question of fact. The same would be true if Buyer and Seller presented a moderate level of extrinsic evidence in favor of their constructions of the agreement, such as only Buyer's preliminary negotiations evidence and only Seller's trade usage evidence.[470]

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468 *W. States Constr. Co. v. United States*, 26 Cl. Ct. 818 (1992), discussed *supra* in the text accompanying notes 134–136, and 138, is a perfect illustration of Case Y. There, the government moved for summary judgment based solely on the ordinary meaning of the text of the parties' facially unambiguous contract. *Id.* at 818–20. Western States responded with trade usage evidence in support of a special meaning. *Id.* at 820–21. After an extended discussion of contract interpretation caselaw, during which the Claims Court endorsed a version of contextualism, *id.* at 821–26, the court held that Western States' trade usage evidence created a question of fact and denied the government's motion for summary judgment, *id*. at 826.

469 I am using the word "probably" because for this hypothetical I am not one-hundred percent certain of the correct answer.

470 *Heggblade-Marguleas-Tenneco, Inc. v. Sunshine Biscuit, Inc.*, 131 Cal. Rptr. 183 (Cal. Ct. App. 1976), parallels the moderate version of Case Z discussed in the body text. There, the parties entered into two contracts for the sale of potatoes. *Id.* at 185. The

Note that Case Z mirrors Case B in every respect but one: In Case B, the divided extrinsic evidence was weak and therefore it was not sufficient to create a jury question. In Case Z, the divided extrinsic evidence is either moderate or strong, both of which are sufficient to create a question of fact because in these situations a reasonable jury could rule for either party.

C. Cases that are Unclear

The third category is cases where it is debatable whether there is a jury question. This category contains two examples—Cases P and Q. Note that I do not offer an ultimate resolution for those two hypotheticals in this section. Instead, the analysis here is intended to clarify various features of the caselaw and to complete my taxonomy of paradigmatic interpretive disputes.

Case P involves a facially ambiguous contract and extrinsic evidence that (1) exclusively favors an interpretation of one of the parties, and (2) is weak. In this type of lawsuit, it is unclear whether there is a jury question. For example, return to the facts of Cases D and X—a contract for delivery by "early December" where Buyer argues that Seller must deliver by December 5 and Seller argues that it must deliver by December 15. This agreement is patently ambiguous. Assume further that all of the relevant extrinsic evidence presented at summary judgment favors Buyer, but the evidence is weak: a single admission during discovery regarding the preliminary negotiations mildly supports Buyer's understanding of the contract. (Because the extrinsic evidence is an admission by Seller, there are no credibility issues with respect to the evidence. The same would be true if the evidence was an affidavit from Buyer, the veracity of which was

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contracts identified precise quantities that the buyer would purchase. *Id.* When the buyer only received and paid for a lesser amount, the seller sued for breach. *Id.* The seller argued that the contract was facially unambiguous in setting forth the quantities the buyer was obligated to purchase. *Id.* at 187. The seller also presented preliminary negotiations evidence favoring its construction that the quantity terms in the agreements were binding. *Id.* at 188. The buyer countered primarily with trade usage evidence that in the potato processing industry, quantities listed in contracts are understood to be merely estimates. *Id.* at 185, 187. And the court ruled that the buyer was entitled to present such evidence under the U.C.C. in order to "explain the meaning of the quantity figures." *Id.* at 188. In addition, some preliminary negotiations and contract drafting evidence favored the buyer's construction. *Id.* The court held that the division in the evidence created a question of fact for a jury. *Id.* at 188–89. *Carter Baron Drilling v. Badger Oil Corp.*, 581 F. Supp. 592 (D. Colo. 1984), is also on point. In that case, the court denied a motion for summary judgment that was grounded upon the facially unambiguous text of the contract in dispute and some trade usage evidence, because the non-moving party presented other trade usage evidence and evidence regarding the surrounding commercial circumstances. *Id.* at 599–600.

not challenged by Seller.) On these facts, I do not know whether the judge should grant a motion for summary judgment submitted by Buyer under textualism and contextualism.

To further set up the issue, it is helpful to compare Case P to Case D, where there was no jury question,[471] and to Case X, where there was a jury question.[472] Both Case D and Case P involve a patently ambiguous agreement where the extrinsic evidence clearly or exclusively favors one side. However, in Case D, the extrinsic evidence is strong or moderate. In Case P, by contrast, the extrinsic evidence is weak. Next, both Case X and Case P involve a patently ambiguous agreement where the interpretive evidence as a whole is divided. However, in Case X, there is textual and extrinsic evidence supporting both parties. In Case P, by contrast, the textual evidence is split, but the extrinsic evidence solely favors one side. Which example does Case P better resemble: Case D or Case X?

Classifying Case P might be rather easy if the reasonable jury rule was the only standard used by courts to decide whether an interpretive dispute concerning extrinsic evidence must be resolved by a judge or a jury. But while my research suggests that the reasonable jury rule is the most common framework for analyzing whether an interpretation issue raises a question of law or fact,[473] it is far from the only approach.[474] The leading alternative is what I will call the "disputed extrinsic evidence rule." Professor Steven Burton construes section 212(2) of the *Restatement (Second) of Contracts* as endorsing this version of the judge/jury standard.[475] Section 212(2) provides that interpretation is a question of fact only when "it depends on the *credibility* of *extrinsic* evidence or on a choice among *reasonable inferences* to be drawn from *extrinsic* evidence."[476] Many cases embrace this standard[477] and Professor Burton suggests that it is the majority rule.[478]

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471 *See supra* notes 462–463, and accompanying text.

472 *See supra* note 467 and accompanying text.

473 *See also* CALAMARI AND PERILLO, *supra* note 7, § 3.15 at 141–42 (implying the same conclusion); KNIFFIN, 5 CORBIN ON CONTRACTS, *supra* note 32, § 24.30, at 327 (same).

474 FARNSWORTH, *supra* note 17, § 7.14, at 477 ("This is another area where judicial attitudes differ, and it is possible to find a wide variety of statements about the proper role of judge and jury in the interpretation process."); *accord* BURTON, *supra* note 1, § 5.1, at 152, and § 5.1.1, at 152–54.

475 *See* BURTON, *supra* note 1, § 5.1.1, at 152–54.

476 RESTATEMENT (SECOND) OF CONTRACTS § 212(2) (AM. L. INST. 1981) (emphasis added).

477 *See, e.g.*, Baker v. Am.'s Mortg. Servicing, Inc., 58 F.3d 321, 326 (7th Cir. 1995)

I have yet to come across any authority that analyzes in detail the differences between the reasonable jury rule and the disputed extrinsic evidence rule. Part of the reason for this is likely that the two frameworks will reach the same result in the vast majority of lawsuits when a contract is patently ambiguous.[479] For example, if the reasonable jury rule is satisfied because the extrinsic evidence so heavily favors one side that there is no genuine issue of material fact, then it is also proper to describe the evidence as permitting only one reasonable inference under the disputed extrinsic evidence rule. Similarly, if the extrinsic evidence is undisputed as defined in the *Restatement*, then there will seldom be a genuine issue of material fact regarding the meaning of the agreement. Note further that some cases and scholars treat the reasonable jury rule and the disputed extrinsic evidence rule as the same standard.[480] And the *Restatement* itself arguably does so too.[481] As a result, there was

("Under Illinois law, if a contract is ambiguous, its interpretation is a question of law for the court as long as the extrinsic evidence bearing on the interpretation is undisputed."); Norville v. Carr-Gottstein Foods Co., 84 P.3d 996, 1000 n.1, 1004 (Alaska 2004) ("However, fact questions are created when the meaning of contract language is dependent on conflicting extrinsic evidence."); Ames v. County of Monroe, 80 N.Y.S.3d 774, 777 (N.Y. App. Div. 2018) ("Where, as here, a contract is ambiguous, its interpretation remains the exclusive function of the court unless determination of the intent of the parties depends on the credibility of extrinsic evidence or on a choice among reasonable inferences to be drawn from extrinsic evidence.") (internal quotation marks omitted); Fiallo v. Allstate Ins. Co., 51 A.3d 1193, 1203 (Conn. App. Ct. 2012) (same); Kofmehl v. Baseline Lake, LLC, 305 P.3d 230, 236 (Wash. 2013) (same).

478 *See* BURTON, *supra* note 1, § 5.1.1, at 152–53 ("As a general rule . . . the judge resolves relevant ambiguities in a written contract unless the resolution depends on disputed parol evidence.").

479 My focus in Case P is on patently ambiguous agreements. If a contract is clear on its face and a party is advancing a special meaning, the judge/jury standards function somewhat differently. For example, in Case Y, discussed *supra* in the text accompanying note 468, there was a conflict between contractual text and extrinsic evidence that is moderate in weight. In that situation, interpretation is a question of fact according to virtually all contextualist courts even though the *extrinsic* evidence is clearly "undisputed" and would be sufficient to warrant summary judgment if the agreement were ambiguous, as in Case D, discussed *supra* in the text accompanying notes 462–463.

480 *See, e.g.*, Mason v. Telefunken Semiconductors Am. LLC, 797 F.3d 33, 38 (1st Cir. 2015) (applying California law) ("If the extrinsic evidence is so one-sided that no reasonable person could decide the contrary, the meaning of the language becomes evident and the erstwhile ambiguity will not preclude summary judgment. But if the extrinsic evidence bearing on the meaning of the relevant language is contested or contradictory, summary judgment will not lie.") (citations and internal quotation marks omitted); RCJV Holdings, Inc. v. Collado Ryerson, S.A. de C.V., 18 F. Supp. 3d 534, 541 (S.D.N.Y. 2014) (applying New York law) (same); ConocoPhillips Co. v. Lyons, 299 P.3d 844, 849 (N.M. 2012) (same); MURRAY, *supra* 38, § 87[A], at 448 (same).

481 Comment e to section 212 states that "a question of interpretation is not left to the trier of fact where the evidence is so clear that *no reasonable person would determine the issue in any way but one*. But if the issue depends on evidence outside the writing, and the possible inferences are conflicting, the choice is for the trier of fact." RESTATEMENT

no need for me to address any variation regarding the judge/jury standard before now.

However, there is caselaw implying that the reasonable jury rule and the disputed extrinsic evidence rule are distinct. In particular, some decisions state that ambiguity resolution is a question of law if *either* rule is satisfied. The following language from an opinion of the Maryland Court of Special Appeals applying Washington law is representative: "Accordingly, unless the extrinsic evidence is undisputed *or* only one reasonable meaning can be ascribed to the language when viewed in context, summary judgment is not appropriate in a case involving interpretation . . . ."[482] It is possible that such statements are not intended to identify two separate tests.[483] But either way, there are indeed important differences between the two principal approaches to the judge/jury standard, differences that are implicated by the facts of Case P.

Under the reasonable jury rule, interpretation is a question of fact when the evidence regarding the parties' intent fails to conclusively support one side's reading of the contract.[484] The

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(SECOND) OF CONTRACTS § 212 cmt. e (AM. L. INST. 1981) (emphasis added). The first quoted sentence sets forth the reasonable jury rule. And the comment as a whole treats (1) "no reasonable person would determine the issue in any way but one," and (2) "conflicting inferences" regarding extrinsic evidence, as two sides of the same coin, with the former identifying when interpretation is for the judge and the latter identifying when interpretation is for the jury. *See id.*

482 Lab. Ready, Inc. v. Abis, 767 A.2d 936, 944 (Md. Ct. Spec. App. 2001) (emphasis added); *accord* Compagnie Financiere de CIC et de L'Union Europeenne v. Merrill Lynch, 232 F.3d 153, 159 (2d Cir. 2000) ("This Court may resolve the ambiguity in the contractual language as a matter of law if there is no extrinsic evidence to support one party's interpretation of the ambiguous language *or* if the extrinsic evidence is so-one sided that no reasonable factfinder could decide contrary to one party's interpretation.") (emphasis added); Luitpold Pharm., Inc. v. Ed. Geistlich Sohne A.G. Fur Chemische Industrie, 784 F.3d 78, 88 (2d Cir. 2015) (applying New York law) (same).

483 For example, the "or" in these cases might mean "in other words" rather than "alternatively." *See* J.I. RODALE, THE SYNONYM FINDER 812 (Warner ed. 1986) (noting that "alternatively" and "in other words" are both synonyms for "or"); Synonyms for Or, THESAURUS, http://www.thesaurus.com/browse/or?s=t [http://perma.cc/KDG7-87UK] (last visited Oct. 24, 2019).

484 *See, e.g.*, Swift & Co. v. Elias Farms, Inc., 539 F.3d 849, 851 (8th Cir. 2008) (applying Minnesota law) ("If the contract is [patently] ambiguous, however, the meaning of the contract becomes a question of fact, and summary judgment is inappropriate unless the *evidence of the parties' intent is conclusive*.") (emphasis added); Wash. Metro. Area Transit Auth. v. Potomac Inv. Prop., Inc., 476 F.3d 231, 235 (4th Cir. 2007) (applying Maryland law) ("Therefore, summary judgment is appropriate when the contract in question is unambiguous or when an ambiguity can be *definitively* resolved by reference to extrinsic evidence.") (emphasis added); RCJV Holdings, Inc. v. Collado Ryerson, S.A. de C.V., 18 F. Supp. 3d 534, 541 (S.D.N.Y. 2014) ("[T]he Court must resolve the ambiguity as a matter of law . . . 'if the evidence presented about the parties' intended meaning [is] so one-sided that no reasonable person could decide the contrary.'" (second alteration in

agreement itself is evidence of intent even if it suffers from a patent ambiguity. Accordingly, the reasonable jury rule is best understood as requiring that courts assess the nature and weight of the extrinsic evidence *together with* the express terms in deciding whether an interpretive issue raises an issue of law or fact—in deciding whether a reasonable jury could find for either party.[485]

In Case P, the agreement is patently ambiguous. This means that the language is reasonably susceptible to the meanings asserted by both Buyer and Seller. In addition, while the extrinsic evidence exclusively favors Buyer, there is very little such evidence. Since the textual evidence is split and the extrinsic evidence provides only marginal support for one side, the evidence *as a whole* is almost evenly divided. When that is so, the evidence of intent is not conclusive; a reasonable jury can find for either party. Thus, the reasonable jury rule *should* result in the judge denying Buyer's motion for summary judgment in Case P. And in the only opinion I found that appears to match Case P on the facts, the court employed the reasonable jury rule to deny a request for summary judgment made by the party who submitted weak extrinsic evidence[486]—i.e., the party in the same position as Buyer in my hypothetical.

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original) (citation omitted) (quoting Compagnie Financiere de CIC et de L'Union Europeenne v. Merrill Lynch, Pierce, Fenner & Smith Inc., 232 F.3d 153, 158 (2d Cir. 2000)); Mulch Mfg., Inc. v. Advanced Polymer Sols., LLC, 947 F. Supp. 2d 841, 858 (S.D. Ohio 2013) ("Although the resolution of any ambiguity is a question of fact, if extrinsic evidence reveals only one reasonable interpretation, the Court may enter summary judgment.").

485 *See* Tigg Corp. v. Dow Corning Corp., 822 F.2d 358, 361, 363–64 (3d Cir. 1987) (applying Michigan law) (endorsing the reasonable jury rule and explaining that "[i]f there is any evidence in the record *from any source* from which a reasonable inference in the nonmoving party's favor may be drawn, the moving party cannot obtain a summary judgment") (emphasis added); Kenney v. Read, 997 P.2d 455, 460 (Wash. Ct. App. 2000) (analyzing both the text of a facially ambiguous contract and related extrinsic evidence in applying the reasonable jury rule; reversing the trial court's grant of summary judgment).

486 *See* United States *ex rel.* Keller Painting Corp. v. Torcon, Inc., 64 F. Supp. 3d 371 (E.D.N.Y. 2014) (applying New York law). There, the parties filed cross-motions for summary judgment. *Id.* at 373; 382–83. The court ruled that the contract was facially ambiguous. *Id.* at 382. It then denied the defendant's motion because the extrinsic evidence submitted by that party was "not particularly probative." *Id.*; *see also id.* at 380 (setting forth the reasonable jury rule). The court also denied the plaintiff's motion because the contract "is ambiguous." *Id.* at 382–83. Nowhere in the opinion did the judge identify any extrinsic evidence offered by the plaintiff. Thus, as I said, this lawsuit *appears* to match Case P. However, in denying the plaintiff's motion, the court cited to and quoted from a case in which both sides presented witnesses that endorsed their reading of the contract. *Id.* at 383. So, it is possible that the plaintiff in *Keller* did in fact proffer extrinsic evidence in support of its summary judgment motion, and the court simply failed to mention it in the opinion.

Under the disputed extrinsic evidence rule, if there is no challenge to the credibility of evidence, then interpretation is for the jury only when the *extrinsic* evidence is subject to more than one reasonable inference—i.e., when the evidence from outside the contract plausibly supports both parties.[487] In Case P, by hypothesis, the extrinsic evidence entirely cuts one way (and there are no issues with its credibility because the evidence is an admission). Accordingly, the disputed extrinsic evidence rule provides that the judge should grant Buyer's motion for summary judgment.[488] Indeed, a number of decisions hold that a patent ambiguity should be resolved at summary judgment in favor of the moving party if that party is the only one to submit relevant extrinsic evidence supporting its construction.[489] That is precisely the situation with Case P: Buyer is the moving party and presented weak extrinsic evidence favoring its reading; Seller is the non-moving party and is relying solely on the language of the contract.

In sum, Case P is the unusual situation where the *extrinsic* evidence is *undisputed*, but a reasonable jury could still rule for either side because the textual and extrinsic evidence *together* are not *conclusive*. And that leaves open whether the hypothetical raises a question of law for a judge or a question of fact for a jury.[490]

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487 *See supra* notes 475–476, and accompanying text.

488 *See* BURTON, *supra* note 1, § 5.1.1, at 152–53 ("As a general rule . . . the judge resolves relevant ambiguities in a written contract unless the resolution depends on disputed parol evidence. . . . A judge should resolve an ambiguity as a matter of law [when] . . . one party offers relevant extrinsic evidence, and a reasonable jury could credit it.") (citing RESTATEMENT (SECOND) OF CONTRACTS § 212(2) (AM. L. INST. 1981), among other authorities).

489 *See, e.g.*, Fed. Ins. Co. v. Am. Home Assur. Co., 639 F.3d 557, 567 (2d Cir. 2011) (applying New York Law) ("However, where language in a contract is ambiguous, summary judgment can be granted 'if the non-moving party fails to point to any relevant extrinsic evidence supporting that party's interpretation of the language.'") (quoting Compagnie Financiere de CIC et de L'Union Europeenne v. Merrill Lynch, Pierce, Fenner & Smith Inc., 232 F.3d 153, 158 (2nd Cir. 2000)); Berkowitz v. Delaire Country Club, Inc., 126 So. 3d 1215, 1219 (Fla. Dist. Ct. App. 2012) ("Normally, when a contract is ambiguous, summary judgment is improper. However, if a party moving for summary judgment presents competent evidence to supports its position, which the nonmoving party does not counter, then summary judgment may be granted.") (citations omitted); 1375 Equities Corp. v. Buildgreen Sols., LLC, 992 N.Y.S.2d 288, 289–90 (N.Y. App. Div. 2014) (setting forth the rule and granting summary judgment because the non-moving party failed to proffer any probative extrinsic evidence).

490 Note that there might be a way to reconcile the reasonable jury rule and the disputed extrinsic evidence rule given how the latter is articulated in the *Restatement (Second) of Contracts*. To see this, start with the language of the *Restatement*: Interpretation is a question of fact when "it depends on the credibility of extrinsic evidence or on a choice among *reasonable inferences* to be drawn from *extrinsic* evidence."

Remember also that there are other versions of the judge/jury standard. Consider two. First, a line of Minnesota cases endorses the following approach: "If the extrinsic evidence is conclusive *and* undisputed, the determination of the meaning of a contract is a function of the trial judge, but if the extrinsic evidence is inconclusive or disputed, the uncertainty and conflict

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RESTATEMENT (SECOND) OF CONTRACTS § 212(2) (AM. L. INST. 1981) (emphasis added). Up to this point, I have construed the italicized language to mean that a question of fact exists only when the extrinsic evidence *by itself* supports two different conclusions regarding the proper construction of the agreement. But there is another way to read section 212(2). It could mean that the extrinsic evidence must support more than one reasonable inference *given the language of the contract*. This understanding effectively collapses the line between the disputed extrinsic evidence rule and the reasonable jury rule because the latter asks whether both parties' interpretations find substantial support in the evidence *generally*—whether extrinsic or textual. *See supra* notes 484–485 and accompanying text.

Let me make the analysis more concrete. Under either construction of the *Restatement*, if (1) an agreement is patently ambiguous, (2) all of the extrinsic evidence favors one reading, and (3) the extrinsic evidence is *strong or moderate* (as in Case D), then the extrinsic evidence clearly supports only one reasonable inference even though the contractual text is consistent with the asserted meanings of both parties. *See supra* notes 462–463, and accompanying text. Case P is different: (1) the agreement is patently ambiguous, (2) all of the extrinsic evidence favors one reading, but (3) the extrinsic evidence is *weak*. Under the construction of the *Restatement* set forth in the body text, extrinsic evidence is effectively assessed in isolation. And that evidence, standing alone, supports only one reasonable inference because the evidence exclusively supports the Buyer's interpretation of the agreement. By contrast, under my revised construction of the *Restatement* set forth in the first paragraph of this footnote, the extrinsic evidence is assessed in relation to the express terms. And one could plausibly describe the *extrinsic evidence* in Case P as supporting more than one reasonable inference given the limited weight of that evidence *and the ambiguity in the text*. Remember, the textual evidence is split in Case P. Even if the extrinsic evidence entirely favors Buyer's interpretation, if that evidence is exceptionally modest, then isn't it *reasonable* to *infer* that the parties intended Seller's construction in light of the facial ambiguity of the parties' contract? I think the answer is "yes." Moreover, as I explained in note 481 *supra*, comment e to section 212 actually seems to treat the reasonable jury rule and the disputed extrinsic evidence rule as the same principle. As do some decisions and other secondary sources. *See supra* note 480; *see also* KNIFFIN, 5 CORBIN ON CONTRACTS, *supra* note 32, § 24.30, at 327, 332, 336 (appearing to equate the reasonable jury rule and section 212(2) of the *Restatement*). That lends further support to my proposed construction of the *Restatement*.

Unfortunately, there are two problems with my analysis here. First, it conflicts with Professor Burton's reading of the *Restatement*. *See supra* note 488. Second, and more importantly, even if I am correct about section 212(2), my understanding cannot be extended to the disputed extrinsic evidence rule generally because of the cases providing that summary judgment is warranted any time only the moving party submits extrinsic evidence in support of its interpretation of a patently ambiguous contract. *See supra* notes 488–489 and accompanying text. In addition, recall that some opinions appear to recognize that the reasonable jury rule and the disputed extrinsic evidence rule are different because they state that ambiguity resolution is a question of law if *either* rule is satisfied. *See supra* note 482 and accompanying text. Given all of this, I believe that the better conceptualization is that the disputed extrinsic evidence rule and the reasonable jury rule are two different approaches to the judge/jury standard for contract interpretation. *See also* KNIFFIN, 5 CORBIN ON CONTRACTS, *supra* note 32, § 24.30, at 327 (stating that even if extrinsic evidence is "in dispute," it can still so heavily favor one side that a reasonable jury could reach only one conclusion).

must be resolved at trial."[491] This language provides that neither "conclusive" extrinsic evidence nor "undisputed" extrinsic evidence is sufficient to warrant adjudicating an interpretive issue as a matter of law. To justify taking a case from the jury, the extrinsic evidence must be both. In essence, this "Minnesota rule" provides that a judge may resolve a patent ambiguity only when *both* the reasonable jury rule *and* the disputed extrinsic evidence rule so permit. In Case P, the extrinsic evidence is undisputed in that it exclusively favors one side and there are no credibility questions. But because the extrinsic evidence is weak, it is inconclusive. Accordingly, under the Minnesota rule, Case P raises a question of fact, just as it does under the reasonable jury rule.

Second, as I noted above,[492] some cases hold that interpretation is a question of law if the evidence is *either* undisputed *or* conclusive—meaning if either the disputed extrinsic evidence rule or the reasonable jury rule is satisfied. In Case P, while the evidence is not conclusive, it is undisputed. Therefore, under these decisions, Case P raises a question of law, just as it does under the disputed extrinsic evidence rule.

So now we have four different versions of the judge/jury standard, with the frameworks evenly divided over whether Case P should be resolved by a judge or a jury. And there are still other approaches in the jurisprudence, though my research suggests that the vast majority of cases in textualist and contextualist states employ one of the four judge/jury standards discussed above.[493]

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491 Deutz & Crow Co. v. Anderson, 354 N.W.2d 482, 486 (Minn. Ct. App. 1984) (emphasis added); *accord* Dawn Equip. Co. v. Micro-Trak Sys., Inc., 186 F.3d 981, 987 (7th Cir. 1999) (applying Minnesota law); Transp. Indem. Co. v. Dahlen Transp. Inc., 161 N.W.2d 546, 550 (Minn. 1968); Nat'l Farmers Union Prop. & Cas. Co., v. Anderson, 372 N.W.2d 71, 75 (Minn. Ct. App. 1985); *see also* Citadel Grp. Ltd. v. Wash. Reg'l Med. Ctr., 692 F.3d 580, 587 (7th Cir. 2012) (articulating the same rule but not applying Minnesota law).

492 *See supra* note 482 and accompanying text.

493 Some elaboration is in order. As noted in the body text, the reasonable jury rule and the disputed extrinsic evidence rule substantially overlap. *See supra* text accompanying notes 479–481. The other two approaches I address in this section—(1) the Minnesota rule, and (2) the undisputed or conclusive rule—are also similar in operation to the two main rules. Indeed, both are combinations of the reasonable jury and disputed extrinsic evidence rules. *See supra* note 491 and accompanying text (discussing the Minnesota rule); *supra* notes 482–483 and accompanying text (discussing the undisputed or conclusive rule); *supra* note 492 and accompanying text (further discussing the undisputed or conclusive rule). As a result, all four frameworks should send substantially similar ratios of interpretive matters to judges and juries. To be sure, there is some variation, as my analysis of Case P is intended to demonstrate. Here is another example of such a difference: Juries will resolve more interpretation issues under the Minnesota

rule than under the undisputed or conclusive rule. That is because a judge may decide a case under the former approach only when the extrinsic evidence is conclusive *and* undisputed, while under the latter the judge may decide an issue if the evidence is conclusive *or* undisputed. Here is how the four approaches are likely ranked (from highest to lowest) in terms of the percentage of interpretation cases they send to a jury: (1) the Minnesota rule (which can also be described as "the conclusive *and* undisputed rule"); (2) the reasonable jury rule (which can also be thought of as the "conclusive rule"); (3) the disputed extrinsic evidence rule (which can also be described as the "undisputed rule"); and (4) the conclusive *or* undisputed rule. But again, while these approaches differ on the margins, logic demands that they should lead to the same result in a large majority of lawsuits given the degree of overlap between the reasonable jury rule and the disputed extrinsic evidence rule.

As I explained in the body text, my research indicates that these four rules as a group dominate the caselaw. Professor Burton concurs. He found that "[m]ost jurisdictions, *by far*, [authorize juries to resolve ambiguities] when extrinsic evidence is admissible, introduced, and contested." BURTON, *supra* note 1, § 5.1, at 152 (emphasis added). Accordingly, I decided to exclusively focus on the four primary, overlapping approaches in my analysis of Case P in the body text. But there are other judge/jury standards that provide juries with a *significantly* reduced *or* increased role in ambiguity resolution. *See* BURTON, *supra*, §§ 5.1 & 5.1.1, at 152–54. In other words, there are alternative approaches that critically diverge from the four main rules.

For example, Professor Burton explains that some decisions require "a judge to draw any needed inferences from extrinsic evidence," *id.* § 5.1.1, at 153, which entails that the resolution of ambiguity is a question of law unless the issue turns on the credibility of extrinsic evidence. This appears to be the majority rule in California. *See, e.g.*, Hess v. Ford Motor Co., 41 P.3d 46, 53 (Cal. 2002); Garcia v. Truck Ins. Exch., 682 P.2d 1100, 1106 (Cal. 1984); Brown v. Goldstein, 246 Cal. Rprt. 3d 161, 172 (Cal. Ct. App. 2019); Jade Fashion & Co. v. Harkham Indust., Inc., 177 Cal. Rptr. 3d 184, 198 (Cal. Ct. App. 2014); Scheenstra v. Cal. Dairies, Inc., 153 Cal. Rptr. 3d 21, 39 (Cal. Ct. App. 2013); Wolf v. Walt Disney Pictures and Television, 76 Cal. Rptr. 3d 585, 602–03 (Cal. Ct. App. 2008); 14A CAL. JUR. 3D CONTRACTS §§ 211, 212 (Westlaw database updated August 2020). *But see, e.g.*, Lucas v. Elliot, 4 Cal. Rptr. 2d 746, 748 (Cal. Ct. App. 1992) (holding that interpretation is a question of law only when the extrinsic "evidence is without conflict and is not susceptible of conflicting inferences," which is essentially identical to the Minnesota rule); SCC Alameda Point LLC v. City of Alameda, 897 F. Supp. 2d 886, 893 (N.D. Cal. 2012) ("If the court concludes . . . that the parties' competing interpretations are equally plausible, it cannot grant summary judgment."). Under the "California rule," juries resolve ambiguities considerably less often than under the four primary approaches. The California rule provides that to get to a jury, it is not enough that (1) both parties introduced relevant extrinsic evidence, and (2) the weight of each side's evidence is such that the evidence is inconclusive—meaning a reasonable jury could rule for either side. Instead, there must be doubts as to the veracity of some of the extrinsic evidence—i.e., the *credibility* of some of the evidence must be contested. A few authorities go even further than the California rule by providing that "any ambiguity whatever must be resolved against the drafter, leaving no role for the jury at all." BURTON, *supra* note 1, § 5.1.1, at 153. On the other extreme, Professor Burton observes that a small number of cases "appear to give the jury a broad role, asking it to resolve all ambiguities as a matter of fact." *Id.* § 5.1, at 152. *See, e.g.*, Chadwick v. Chadwick, 260 S.W.3d 421, 425 (Mo. Ct. App. 2008) ("Summary judgment, therefore, is only appropriate in contract cases where there is no ambiguity and the apparent meaning of contract terms can be determined within the four corners of the document."); *see also* BURTON, *supra*, § 5.1.1, at 154 (further discussing frameworks that endorse a larger role for juries in ambiguity resolution). For an extended discussion of various approaches to the judge/jury standard, see LINZER, 6 CORBIN ON CONTRACTS, *supra* note 8, § 25.18, at 240–69.

As indicated in the second paragraph of this footnote, I left out of the body text any analysis of how Case P would be decided under the minority approaches that provide juries with greatly constricted or expanded authority to resolve ambiguities. That is

partly due to the fact that these alternatives are exceptionally easy to apply. To illustrate, if ambiguity resolution is always a question of fact, then obviously Case P goes to the jury. Likewise, if ambiguity resolution is never a question of fact, then Case P plainly must be decided by the judge. And if juries only resolve ambiguities when there are credibility issues regarding the extrinsic evidence, as mandated by the California rule, then again Case P must be decided by the court since the hypothetical raises no such issues.

However, there is one twist under the California rule. Up to this point in Part VIII, interpretive issues have been for the judge any time there is only one qualifying reading of the contract given the textual and extrinsic evidence and the governing version of the judge/jury standard. *See, e.g.*, *supra* Part VIII.A. Interpretation is for the jury any time both sides are pressing qualifying readings. *See, e.g.*, *supra* Part VIII.B. In other words, once a judge finds that a case must be decided as a matter of law, the judge has necessarily determined which party's construction of the agreement is controlling. The California rule breaks from this framework. Under that approach, judges are obligated to choose among reasonable inferences when there are no challenges to the credibility of the extrinsic evidence. This means that interpretation is often for the judge even when both parties present qualifying interpretations. Put another way, if a judge holds that an interpretive dispute must be decided as a question of law, the judge has *not* necessarily determined which party's construction of the agreement is controlling. Instead, both sides might still be eligible to win the lawsuit. Case P is illustrative of the distinction between the California rule and the other approaches to the judge/jury standard. The California rule requires that the judge resolve Case P. But it does not obligate the judge to decide for a particular party: Either Buyer or Seller can win the case at summary judgment. This contrasts with all of the other approaches, which provide that if Case P must be decided by the judge, then it must be decided in favor of a specific party: Buyer must win at summary judgment. *See, e.g.*, *supra* notes 487–489, 492 and accompanying text. In effect, the California rule asks the judge to act as a jury when the relevant extrinsic evidence is divided such that a reasonable jury could rule for either side, as long as there is no challenge to the credibility of any of the evidence.

There is a final complexity in the caselaw regarding the judge/jury standard that merits brief discussion: The phrase "disputed evidence" has multiple meanings. Recall that the *Restatement* provides that interpretation is a question of fact only when "it depends on the credibility of extrinsic evidence *or* on a choice among reasonable inferences to be drawn from extrinsic evidence." RESTATEMENT (SECOND) OF CONTRACTS § 212(2) (AM. L. INST. 1981) (emphasis added). Professor Burton considers extrinsic evidence to be "disputed" when either prong of the *Restatement* rule is implicated—there is a challenge to the credibility of evidence or unchallenged evidence supports multiple reasonable inferences. *See* BURTON, *supra* note 1, § 5.1.1, at 152–53. But "disputed evidence" can be understood more narrowly to apply only to the first prong in the *Restatement*—when evidence is challenged on grounds of credibility. In fact, that is essentially the definition used by the California cases listed above in this footnote. *See, e.g.*, *Wolf*, 76 Cal. Rptr. 3d at 602–03. For example, suppose the parties submit contradictory affidavits regarding what was said in a conversation that took place during the preliminary negotiations. In that event, each affidavit challenges the credibility of the other. Compare that with a lawsuit in which the plaintiff submits course of performance evidence that is unchallenged by the defendant and that favors the plaintiff's reading of the contract, and the defendant submits trade usage evidence that is unchallenged by the plaintiff and that favors the defendant's reading. In that situation, only the second prong of the *Restatement* is implicated: No one is questioning the credibility of any of the evidence, but since the evidence is in conflict, multiple reasonable inferences regarding the intent of the parties are supported. *See* LINZER, 6 CORBIN ON CONTRACTS § 25.18[D], at 268–69 (addressing this distinction by juxtaposing "conflicting testimony" with "conflicting inferences"). A third definition of "disputed evidence" is identified in two places in the body: Evidence is "disputed" when both sides' present at least some extrinsic evidence supporting their reading of the contract. *See supra* text accompanying notes 489, 491. That definition is different from the second prong of the *Restatement* because even if each party submits some extrinsic evidence favoring its position (and thus the evidence is

Given the varying approaches to the judge/jury standard, one might propose that the solution to Case P depends upon which framework is employed by the relevant jurisdiction. But I am hesitant to adopt this conclusion for several reasons. First, the caselaw in many states is divided over the governing articulation of the judge/jury standard.[494] Second, recall that some authorities treat the reasonable jury rule and the disputed extrinsic evidence rule as the same principle.[495] And third, I have seen no cases that analyze the alternative approaches. These points together strongly imply that few, if any, courts have consciously endorsed one formulation of the judge/jury standard over the others and that courts generally do not appreciate the differences among the various rules. Thus, I do not think we can accurately predict how courts will respond when faced with a lawsuit that implicates variations in the rules, such as Case P. In sum, the jurisprudence does not answer whether Case P raises a question of law or fact.

One possible explanation for this uncertainty is that situations like Case P may simply be too rare to justify courts (and commentators) working out the distinctions among the primary judge/jury standards. Once a court finds that a contract is patently ambiguous in a textualist state, both parties are strongly incentivized to locate and present extrinsic evidence supporting their preferred construction. As a result, there should be divided extrinsic evidence in most lawsuits that involve an ambiguous agreement in those jurisdictions.[496] And in matters

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"disputed" under this third definition), one side's evidence could be so overwhelming that only one reasonable inference is possible (and thus the evidence is "undisputed" under the second prong of the *Restatement*). *See* KNIFFIN, 5 CORBIN ON CONTRACTS, *supra* note 32, § 24.30, at 327 (stating that even if extrinsic evidence is "in dispute," it can still so heavily favor one side that a reasonable jury could reach only one conclusion). The third definition is also different from the first prong of the *Restatement* because both sides could present extrinsic evidence (and thus again the evidence is "disputed" under the third definition) without challenging the credibility of the other side's evidence (and thus the evidence is "undisputed" under the first prong of the *Restatement*). *See also* ConocoPhillips Co. v. Lyons, 299 P.3d 844, 849 (N.M. 2012) (appearing to treat this third definition as distinct from the first two). However, I leave any further analysis of this issue and other complexities regarding the judge/jury standard for another day.

494 New York is one such state. To see this, review the cases cited *supra* in notes 477, 484, and 489. So is Minnesota. *See supra* notes 484, 491, and accompanying text. California's authorities are also split. *See supra* note 493. As are Missouri's. *Compare* Chadwick v. Chadwick, 260 S.W.3d 421, 425 (Mo. Ct. App. 2008) (providing that juries resolve all patent ambiguities), *with* Girardeau Contractors, Inc. v. Mo. Highway & Transp. Com., 644 S.W.2d 360, 363 (Mo. Ct. App. 1982) (endorsing the reasonable jury rule).

495 *See supra* notes 480–481 and accompanying text.

496 *See* Luitpold Pharm., Inc. v. Ed. Geistlich Sohne A.G. Fur Chemische Industrie, 784 F.3d 78, 87–88 (2d Cir. 2015) ("Because facial ambiguity in a contract will require the factfinder to examine extrinsic evidence to determine the contract's effect, and because

where only one party submits materials from outside the contract, I suspect that the evidence will seldom be as weak as it is in Case P. Similar analysis applies to disputes in contextualist states. Any time an agreement suffers from a patent ambiguity, parties located in such jurisdictions should be highly motivated to exercise their right to introduce extrinsic evidence in order to maximize the strength of their position at summary judgment. Indeed, because contextualism permits courts to consider extrinsic evidence even when a contract is facially *un*ambiguous, presenting such evidence is probably the default practice for lawyers in states following that approach. Moreover, as noted above,[497] I found only one opinion dealing with facts that are identical or substantially similar to Case P (though my research was not exhaustive). These points together support the conclusion that very few litigated interpretive matters will mirror my hypothetical in either textualist or contextualist territories.[498] Accordingly, some of the problems with the interpretation doctrine identified by Case P might be more theoretical than real.

Case Q, which is the final hypothetical, involves a facially unambiguous contract and extrinsic evidence that (1) overwhelmingly or exclusively favors an interpretation that conflicts with the text of the agreement, and (2) is strong. In this type of lawsuit, it is unclear whether there is a jury question. For example, return yet again to the basic facts of Case A—a contract for delivery on "December 15," where Buyer argues for the standard meaning and Seller argues for the special meaning (delivery before January 1). In this hypothetical, assume that all of the relevant extrinsic evidence presented at summary judgment favors the Seller and is very strong: preliminary negotiations documents, the course of performance, the course of dealing, and usages of trade all support Seller's construction, and no extrinsic evidence supports Buyer's reading. On these facts, summary judgment would clearly be inappropriate for Buyer in a contextualist state. The critical question here, however, is whether summary judgment would be appropriate for *Seller*.

To elaborate, Case Q is identical to Cases C and Y in every respect but one. In Case C, the Seller's evidence of a special

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such extrinsic evidence is most often mixed, a court generally will not grant summary judgment on a contract claim when the operative language is ambiguous.").

497 *See supra* note 486 and accompanying text.

498 That explains why I did not conduct an exhaustive search for decisions that match Case P.

meaning is weak, and so the court must grant summary judgment for Buyer.[499] In Case Y, the Seller's evidence of a special meaning is modest, and so the court must deny a motion for summary judgment by either side.[500] In Case Q, the Seller's evidence of a special meaning is exceptionally strong. If Buyer—the party asserting the ordinary meaning based on the contractual text—is not entitled to summary judgment in Case Y, then Buyer is also clearly not entitled to summary judgment in Case Q because Seller's extrinsic evidence is actually stronger here than in Case Y. But again, the question Case Q raises is whether *Seller*—the party asserting the special meaning based on extrinsic evidence—is entitled to summary judgment.

Put another way, is Case Q just a version of Case Y, where extrinsic evidence of a special meaning creates a question of fact that requires the jury to decide between the standard meaning supported by the contractual text and the special meaning? Or is Case Q a separate type of interpretive dispute in which the extrinsic evidence of a non-standard meaning is so powerful that it overwhelms the text as a matter of law, requiring the judge to adopt the non-standard meaning at summary judgment?

Put still another way, must a lawsuit where textual evidence conflicts with extrinsic evidence *always* either be (i) sent to the jury for resolution as a question of fact (as in Case Y), or (ii) decided by the judge as a matter of law for the party asserting the *standard* meaning of the text (as in Case C)? Or is there a third possibility (iii), in which the lawsuit can be decided by the judge as a matter of law for the party asserting a *special* meaning grounded in extrinsic evidence (as I am suggesting with respect to Case Q)?

As I said, it is unclear whether Case Q raises a question of law or fact; it is unclear whether Case Q is distinct from Case Y for purposes of a motion for summary judgment. That is so for two reasons. First, I have found no decision or secondary source that directly addresses what should happen in situations like Case Q. Second, plausible arguments for both the law and fact positions can be constructed from general principles and language in the contextualist caselaw.

I will begin with the proposition that Case Q should be resolved by the court as a matter of law in favor of Seller, the

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499 *See supra* note 461 and accompanying text.
500 *See supra* note 468 and accompanying text.

party arguing for a non-standard meaning based on extrinsic evidence. On this view, Case Q is different from Case Y.

Recall the two most commonly employed judge/jury standards—the reasonable jury rule and the disputed extrinsic evidence rule. Those approaches dominate in virtually every contextualist jurisdiction.[501] My focus here is on the reasonable jury rule. That is because the disputed extrinsic evidence rule—to the extent it varies from the reasonable jury rule—does not logically fit situations where the textual and extrinsic evidence support competing readings of an agreement, as in Case Q. The disputed extrinsic evidence rule is principally designed for situations involving a patently ambiguous contract. If an agreement is unclear on its face, then whether the extrinsic evidence is disputed is central to whether the lawsuit should be resolved by a judge or a jury. For example, the disputed nature of the extrinsic evidence is what distinguishes Case X (question of fact) from Case D (question of law).[502] But if the contractual wording unambiguously favors one meaning, then whether the case raises a question of law or fact turns primarily on the *strength* of the extrinsic evidence that conflicts with the standard meaning of the express terms. To illustrate, Cases B and C (questions of law) are separated from Cases Y and Z (questions of fact) by the fact that the extrinsic evidence of a special meaning is weak in the first two hypotheticals and moderate or strong in the later two hypotheticals.[503] Accordingly, the disputed extrinsic evidence rule—again, to the extent it differs from the reasonable jury rule—provides little guidance in Case Q.

It is not difficult to imagine a fact pattern in which a straightforward application of the reasonable jury rule mandates summary judgment for the party arguing for a special meaning based on extrinsic evidence. To see this, consider a more detailed version of Case Q. First, four letters exchanged during the preliminary negotiations expressly state that "delivery before

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501 *See, e.g.*, Tigg Corp. v. Dow Corning Corp., 822 F.2d 358, 361, 363 (3d. Cir. 1987) (applying Michigan law) (endorsing the reasonable jury rule); Norville v. Carr-Gottstein Foods Co., 84 P.3d 996, 1000 n.1, 1004 (Alaska 2004) (endorsing the disputed extrinsic evidence rule); ConocoPhillips Co. v. Lyons, 299 P.3d 844, 849 (N.M. 2012) (endorsing both because the court treats the reasonable jury rule and the disputed extrinsic evidence rule as if they are the same standard); Kelly v. Tonda, 393 P.3d 824, 830 (Wash Ct. App. 2017) (endorsing the disputed extrinsic evidence rule).

502 *Compare supra* text accompanying notes 462–463 (Case D), *with supra* text accompanying note 467 (Case X); *see also infra* Chart 2 (located shortly after note 520).

503 *Compare supra* text accompanying notes 460–461 (Cases B and C), *with supra* text accompanying notes 468–470 (Cases Y and Z); *see also infra* Chart 2 (located shortly after note 520).

January 1 will be acceptable, as per our past transactions and the practice in the industry." Second, in all six of the prior sales under the current contract (i.e., course of performance), delivery of the lumber between the 16th and 31st of the month was either expressly approved of by Buyer or Buyer accepted the goods without objection even though delivery was specified in the agreement for the 15th. Third, under each of the prior contracts between the parties with a December 15 delivery date (i.e., course of dealing), goods were repeatedly accepted between December 16 and December 31, again with either express approval or no objection from Buyer. Fourth, multiple expert witnesses with significant experience in the lumber industry testified during depositions that the universal practice of industry participants (i.e., trade usage) is to treat delivery before January 1 as full performance when the contract specifies that the goods must arrive by December 15. Fifth, Buyer presented no extrinsic evidence in support of its position. In particular, Buyer was unable to identify a single example within the lumber industry (i.e., trade usage) where receipt of lumber after the 15th of the month and before the first of the following month was objected to or treated as a breach by the purchaser, when the agreement stated that the vendor must provide the goods by the 15th.

On those facts, no reasonable jury could deliver a verdict in favor of Buyer. As a result, summary judgment for Seller appears to be required under the reasonable jury rule; the judge must find as a matter of law that the contract permits delivery any time before January 1. Buyer's argument that the words "December 15" possess their standard meaning will not be heard by the jury. Accordingly, if the reasonable jury rule is the governing standard—and *if* it applies in a straightforward manner—then it is possible for a party advancing a special meaning to win at summary judgment. In other words, under my analysis here, Case Q is indeed distinct from Case Y. And thus there are three options when textual and extrinsic evidence support conflicting readings of an agreement: (i) the matter goes to the jury (as in Case Y); (ii) summary judgment for the party asserting the standard meaning (as in Case C); and (iii) summary judgment for the party asserting the non-standard meaning (as in Case Q).

However, there is language in contextualist decisions that supports the conclusion that a party advancing a special meaning based on extrinsic evidence can never win at summary judgment—i.e., that the reasonable jury rule does *not* apply in a straightforward manner to a dispute like Case Q. Consider the

following statement from the Colorado Supreme Court's opinion in *Pepcol Manufacturing Co. v. Denver Union Corporation*:

> In determining whether a contract is ambiguous, the court may conditionally admit extrinsic evidence on this issue. If the court, after considering the extrinsic evidence, determines that there is no ambiguity, then the extrinsic evidence must be stricken. . . . Once a contract is determined to be ambiguous, the meaning of its terms is generally an issue of fact to be determined in the same manner as other disputed factual issues.[504]

This quotation implies that there are only two possibilities under contextualism when a party contends that facially unambiguous language possesses a special meaning:[505] (i) the extrinsic evidence of the special meaning is strong enough to send the case to the jury for adjudication as a question of fact (as in Case Y); or (ii) the extrinsic evidence of the special meaning is not strong enough to send the case to the jury, and thus the party asserting the standard meaning based on the text is entitled to judgment as a matter of law (as in Case C). Option (iii)—adopting a special meaning as a matter of law because the extrinsic evidence overwhelms the text—appears to be prohibited by the language in *Pepcol*. And thus Case Q is simply another species of Case Y. Let me explain.

To start with, here again are the three possible results when a party submits extrinsic evidence in support of a special meaning in a contextualist state, but this time phrased in terms of ambiguity: (i) the agreement is *ambiguous* because the extrinsic evidence is sufficient to establish that the parties may have intended a special meaning rather than the ordinary meaning of the contractual text (as in Case Y); (ii) the agreement is *unambiguous* because the extrinsic evidence is insufficient as a matter of law to establish that the parties may have intended a special meaning rather than the ordinary meaning of the contractual text (as in Case C); and (iii) the contract is *unambiguous* because the extrinsic evidence is so powerful that it establishes as a matter of law that the parties intended a special

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504 687 P.2d 1310, 1314 & n.3 (Colo. 1984) (citations and internal quotation marks omitted).

505 The language from *Pepcol* cannot apply when a contract is patently ambiguous—when the express terms are reasonably susceptible to more than one *standard* meaning. That is because relevant extrinsic evidence is never stricken in such cases under contextualism or textualism. Instead, either (1) the extrinsic evidence conclusively establishes which standard meaning the parties intended, or (2) the jury decides between the two standard meanings based on the textual and extrinsic evidence. *See supra* notes 462–463 (Case D), 467 (Case X), 471–498 (Case P), and accompanying text.

meaning rather than the ordinary meaning of the contractual text (as I am suggesting with respect to Case Q). Under this schema, a contract can be "unambiguous" in two ways—in favor of the standard meaning or in favor of the special meaning. Crucially, the language from *Pepcol* appears to permit only the former.

The Colorado Supreme Court wrote that "[i]f the court . . . determines that there is no ambiguity, then the extrinsic evidence must be stricken."[506] In other words, if an agreement is unambiguous, extrinsic evidence is no longer relevant. That phrasing makes perfect sense in situations where the judge concludes that the extrinsic evidence is not sufficient to establish that a contract is ambiguous, which is option (ii)/Case C. There, the judge strikes the extrinsic evidence and adopts the unambiguous ordinary meaning of the agreement's express terms.

But the *Pepcol* phrasing does not fit a case in which a judge concludes that a contract unambiguously possesses a special meaning, which is option (iii)/Case Q. In that circumstance, extrinsic evidence supporting a non-standard meaning is the basis for the ruling that the agreement is unambiguous. According to *Pepcol*, however, extrinsic evidence is "stricken" whenever a trial judge determines that an agreement is unambiguous.[507] Stricken evidence obviously cannot justify a legal conclusion. Therefore, when a judge finds that a contract is "unambiguous," the ultimate meaning of the contract must be derived exclusively from within the four corners of the instrument. And this entails that the only type of unambiguous meaning that is possible under Colorado law is unambiguous *ordinary* meaning derived from the contractual text (option (ii)). Unambiguous *special* meaning (option (iii)), which necessarily flows from extrinsic evidence, is ruled out by the language from *Pepcol* because such evidence is stricken if an agreement is "unambiguous."[508] As a result, it appears that extrinsic evidence of a special meaning can, at most, establish the existence of a non-standard-meaning latent ambiguity; the most such evidence can do is create a question of fact for the jury, which is option (i)/Case Y. And thus Case Q must be treated as a variant of Case

506 *Pepcol*, 687 P.2d at 1315 n.3.

507 *Id.*

508 The Colorado Supreme Court has reaffirmed the *Pepcol* standard at least twice. *See* Lazy Dog Ranch v. Telluray Ranch Corp., 965 P.2d 1229, 1235–36 (Colo. 1998); O'Brien v. Vill. Land Co., 794 P.2d 246, 249 n.2 (Colo. 1990).

Y where the evidence that the agreement is "ambiguous" happens to be stronger than in the typical lawsuit.

Some decisions from other contextualist states contain language that closely parallels or is logically consistent with *Pepcol*.[509] And Professor Steven Burton employed comparable wording in describing the operation of contextualism generally.[510] But there are reasons to believe that the *Pepcol* quotation and similar statements in other opinions are not intended to prohibit summary judgment for a party asserting a non-standard meaning.

First, in many lawsuits involving a purported special meaning, only the party advancing that meaning (Seller in Case Q) submits extrinsic evidence during summary judgment. The side arguing for the standard meaning (Buyer in Case Q) relies exclusively on material within the four corners of the agreement at that stage in the litigation.[511] Second, my research suggests that the party asserting a non-standard meaning virtually never moves for summary judgment. Indeed, I have found just four

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509 *See, e.g.*, Ward v. Intermountain Farmers Ass'n, 907 P.2d 264, 268 (Utah 1995) (endorsing contextualism) ("Conversely, if after considering such [extrinsic] evidence, the court determines that the language of the contract is not ambiguous, then the parties' intentions must be determined solely from the language of the contract."); ConocoPhillips Co. v. Lyons, 299 P.3d 844, 849, 852 (N.M. 2012) (reaffirming that New Mexico follows contextualism) ("If a court concludes that there is no ambiguity, the words of the contract are to be given their ordinary and usual meaning.") (internal quotation marks and alterations omitted); Isbrandtsen v. N. Branch Corp., 556 A.2d 81, 84–85 (Vt. 1988) (endorsing contextualism) ("If, however, no ambiguity is found, then the language must be given effect in accordance with its plain, ordinary and popular sense.").

510 BURTON, *supra* note 1, § 4.3.3, at 128 ("However, in these [contextualist] jurisdictions, the court must decide after considering the extrinsic evidence whether the language of the contract document is reasonably susceptible to both meanings. If not, *the contract is unambiguous, the extrinsic evidence is excluded*, and the judge decides the interpretive question as a matter of law.") (emphasis added); *see also id.* § 4.2.3, at 118–19 ("According to *Pacific Gas & Electric Co.*, as indicated above, the trial court would admit the extrinsic evidence conditionally, reserving its ruling on admissibility or admitting it subject to a motion to strike. If the court then finds the contract to be ambiguous, the evidence stays in. *If the court finds the contract to be unambiguous, it rules the evidence out or grants a motion to strike and, in either event, gives the contract its unambiguous meaning as a matter of law*.") (citing Pac. Gas & Elec. Co. v. G.W. Thomas Drayage & Rigging Co., 442 P.2d 641, 645 n.7 (Cal. 1968)) (emphasis added).

511 *See* Schwartz & Scott, *supra* note 4, at 962 ("Contests over the meaning of contract terms thus follow a predictable pattern: one party claims that the words in a disputed term should be given their *standard dictionary meaning*, as read in light of the contract as a whole, the pleadings, and so forth. The counterparty argues either that the contract term in question is ambiguous and extrinsic evidence will resolve the ambiguity, or that extrinsic evidence will show that the parties intended the words to be given a *specialized or idiosyncratic meaning* that varies from the meaning in the standard language.") (emphasis added).

cases in which that happened.[512] Normally, it is the party alleging a standard meaning based on the contractual text who seeks summary judgment.[513] The side pressing a special meaning merely contends in response that the motion should be denied and the case should go to trial because the extrinsic evidence raises a question of fact over whether the parties used the standard meaning or a special meaning of the terms at issue. Given these two points, the *Pepcol* language might simply reflect how contextualism functions in the usual case.

To repeat, in the typical lawsuit, the party pressing the standard meaning moves for summary judgment based solely on the wording of the agreement, and the other side responds with extrinsic evidence purporting to show that the parties intended that wording to possess a special meaning and thus that construction of the contract raises a question of fact. In that situation, there are only two possibilities: Either (i) the extrinsic evidence is strong enough to defeat the motion, and the matter advances to trial for resolution by the jury, or (ii) the extrinsic evidence is not strong enough to defeat the motion and the court grants summary judgment to the party asserting the standard meaning.

The *Pepcol* language maps perfectly onto those two options. Remember, the Colorado Supreme Court stated that "[i]f the court, after considering the extrinsic evidence, determines that there is no ambiguity, then the extrinsic evidence must be stricken."[514] That fits situation (ii), where the non-movant's extrinsic evidence is too weak to establish the existence of a non-standard-meaning latent

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512 I found three lawsuits where both the party advancing a special meaning and the party advancing the standard meaning moved for summary judgment. *See* Valve Corp. v. Sierra Ent. Inc., 431 F. Supp. 2d 1091, 1093, 1096–1100 (W.D. Wash. 2004); Neal & Co., Inc. v. Ass'n of Vill. Council Presidents Reg'l Hous. Auth., 895 P.2d 497, 500, 502–05 (Alaska 1995); Madison Indus., Inc. v. Eastman Kodak Co., 581 A.2d 85, 88–90 (N.J. Super. Ct. App. Div. 1990); *see also* Hazen First State Bank v. Speight, 888 F.2d 574, 575–76, 578 (8th Cir. 1989) (while both parties moved for summary judgment, it is not clear whether the summary judgment motion of the party asserting a special meaning encompassed the interpretation issue). I also found one case where only the party asserting a special meaning moved for summary judgment. *See* Feinberg v. Federated Dep't Stores, Inc. 832 N.Y.S.2d 760, 761–64 (N.Y. Sup. Ct. 2007).

513 *See, e.g.*, Mylan Inc. v. SmithKline Beecham Corp., 723 F.3d 413, 417–20 (3d Cir. 2013); W. States Constr. Co. v. United States, 26 Cl. Ct. 818, 818–20 (1992); Carter Baron Drilling v. Badger Oil Corp., 581 F. Supp. 592, 594, 599 (D. Colo. 1984); Michael Schiavone & Sons, Inc. v. Securalloy Co., 312 F. Supp. 801, 802, 804 (D. Conn. 1970); Eskimo Pie Corp. v. Whitelawn Dairies, Inc., 284 F. Supp. 987, 990 (S.D.N.Y. 1968); C-Thru Container Corp. v. Midland Mfg. Co., 533 N.W.2d 542, 544–45 (Iowa 1995); Alexander v. Buckeye Pipe Line Co., 374 N.E.2d 146, 149, 151 (Ohio 1978).

514 Pepcol Mfg. Co. v. Denver Union Corp., 687 P.2d 1310, 1314 n.3 (Colo. 1984).

ambiguity. In that case, the judge grants summary judgment to the side pressing the standard meaning derived from the contractual text. The extrinsic evidence of a non-standard meaning is effectively "stricken" because the judge ultimately does not rely on that evidence in construing the agreement. Instead, the court adopts the standard meaning based exclusively on the words within the four corners of the instrument. The Colorado high court also wrote that "[o]nce a contract is determined to be ambiguous, the meaning of its terms is generally an issue of fact to be determined in the same manner as other disputed factual issues."[515] That fits situation (i), where the non-movant's extrinsic evidence is sufficient to require that the lawsuit continue to trial. Therefore, the courts that wrote *Pepcol* and opinions with comparable statements might simply have been using language somewhat loosely to describe what normally happens under contextualism when a party offers extrinsic evidence of a special meaning, rather than intending to set forth a rule regarding which parties may successfully move for summary judgment in such cases.

Note further that I found only a few opinions outside of Colorado with language similar to that in *Pepcol*.[516] The vast majority of contextualist decisions from other jurisdictions contain nothing suggesting courts are barred from awarding summary judgment to the party advancing a non-standard meaning based on extrinsic evidence. This further supports the conclusion that *Pepcol* and comparable authorities should not be taken literally with respect to the scope of summary judgment power.[517]

The caselaw discussed in the preceding several paragraphs supports conflicting understandings regarding whether a party asserting a non-standard meaning can successfully move for summary judgment in an interpretative dispute governed by the principles of contextualism. It is thus not possible to definitively answer whether Case Q raises a question of law for the judge or a

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515 *Id.* at 1314. Presumably interpretation is only "generally" an issue of fact if the contract is ambiguous because sometimes the parties do not submit any extrinsic evidence, in which case ambiguity resolution is a question of law. *See supra* notes 50, 241, and accompanying text.

516 *See supra* note 509 and accompanying text.

517 Of course, another possibility is that there are two contextualist approaches on this issue: (1) the Colorado rule, reflected in *Pepcol*, under which only the party arguing for the standard meaning can win the case at summary judgment, and (2) the alternative rule under which either party can win the case at summary judgment. If the Colorado rule governs, then Case Q is just a version of Case Y where the evidence is stronger than usual. If the alternative rule governs, then Case Q is distinct from Case Y.

question of fact for the jury. However, as I noted above, the party advancing a special meaning almost never seeks summary judgment; recall that I have located just four cases where that occurred.[518] While the decisions available in electronic databases like Westlaw are frequently not representative of the broader universe of litigated matters,[519] the paucity of published cases in which the party asserting a non-standard meaning moved for summary judgment supports the conclusion that such motions are rare. Moreover, the extrinsic evidence favoring a special meaning will probably seldom be as strong as in Case Q. Thus, as with Case P, Case Q may identify a problem with contextualist doctrine that is largely theoretical in nature.[520]

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Part VIII analyzed nine hypothetical cases to determine whether they raise a question of law or fact. Chart 2 sets forth a summary of my conclusions with respect to each hypo.

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518 *See supra* notes 512–513, and accompanying text.

519 *See* Silverstein, *supra* note 13, at 229–41.

520 Note that the bulk of my analysis of Case Q might not apply to California, arguably the leading contextualist jurisdiction. As I explained previously, California follows a minority approach to the judge/jury standard: Interpretation is a question of fact in that state, according to most cases, only when there are issues of credibility regarding extrinsic evidence. *See supra* note 493. There are no credibility issues in Case Q. Thus, if the California rule applies to a lawsuit with that structure, then the matter should be adjudicated by the court at summary judgment. But the California Rule can be understood as a version of the disputed extrinsic evidence rule. *See supra* note 493. And I argued in the body text that the disputed extrinsic rule does not logically fit situations like Case Q, to the extent that approach varies from the reasonable jury rule. *See supra* text accompanying notes 501–503. Accordingly, I do not know whether courts in California would apply the California rule to a situation like Case Q. This means that my general uncertainty about the proper resolution of Case Q applies equally to California specifically.

Chart 2: Question of Law or Question of Fact

Legend
"Clear-B" = the text of the contract clearly supports buyer
"Ambig" = the text of the contract is reasonably susceptible to either parties' construction
"Favor-B" = the extrinsic evidence overwhelmingly favors buyer and is either weak, moderate, or strong
"Favor-B/Weak" = the extrinsic evidence overwhelmingly favors buyer, but the evidence is weak
"Favor-B/Moderate" = the extrinsic evidence overwhelmingly favors buyer, and the evidence is moderate in weight
"Favor-B/Strong" = the extrinsic evidence overwhelmingly favors buyer, and the evidence is strong
"Favor-S/Weak" = the extrinsic evidence overwhelmingly favors seller, but the evidence is weak
"Favor-S/Moderate" = the extrinsic evidence overwhelmingly favors seller, and the evidence is moderate in weight
"Favor-S/Strong" = the extrinsic evidence overwhelmingly favors seller, and the evidence is strong
"Divided" = the extrinsic evidence supports the interpretations of both sides and is either weak, moderate, or strong
"Divided/Weak" = the extrinsic evidence supports the interpretations of both sides, but the evidence is weak
"Divided/Moderate" = the extrinsic evidence supports the interpretations of both sides, and the evidence is moderate in weight
"Divided/Strong" = the extrinsic evidence supports the interpretations of both sides, and the evidence is strong
When the text is ambiguous, the summary judgment disposition applies to textualism and both versions of contextualism. When the text is clear, the summary judgment disposition applies only to both versions of contextualism.

Case	Text	Extrinsic Evidence	Summary Judgment Disposition
No Jury Question			
A	Clear-B	Favor-B	For B
B	Clear-B	Divided/Weak	For B
C	Clear-B	Favor-S/Weak	For B
D	Ambig	Favor-B/Strong or Moderate	For B
Jury Question			
X	Ambig	Divided	Denied
Y	Clear-B	Favor-S/Moderate	Denied
Z	Clear-B	Divided/Strong or Moderate	Denied
Unknown			
P	Ambig	Favor-B/Weak	N/A
Q	Clear-B	Favor-S/Strong	N/A

Let me offer two final concerns with this framework. First, the lines separating my examples are unclear on the margins. In other words, cases can be difficult to classify using the parameters identified in Chart 2. To illustrate, when does the weight of extrinsic evidence move from weak to moderate to strong? Likewise, when does evidence change from overwhelmingly favoring one party to divided? Second, fact patterns can raise complexities that go beyond my parameters. For example, what happens in a case where the contractual language is ambiguous, but it does not equally support both interpretations? To be more specific, suppose the textual argument for one reading of the agreement is twice as strong as the textual argument for the other reading, but the instrument is still "reasonably susceptible" to both asserted constructions. In a lawsuit like that, how does contractual language interact with extrinsic evidence of varying weights for each side?

Unresolved issues like those—some of which may be unresolvable—limit to some degree the value of the analysis in this part. Nonetheless, because the nine hypotheticals I addressed are paradigms of interpretive disputes, the discussion

here should provide real guidance regarding the circumstances in which interpretation raises a question of law or fact.

IX. ISSUE 7: CONTEXTUALISM AND THE PAROL EVIDENCE RULE

Courts in contextualist states almost universally proclaim that the parol evidence rule still operates within their borders.[521] Indeed, in *Pacific Gas*, the California Supreme Court wrote that "extrinsic evidence is not admissible to add to, detract from, or vary the terms of a written contract."[522] The parol evidence rule also retains a significant role under the *Restatement (Second) of Contracts*,[523] which adopts contextualism.[524] However, there is a plausible argument that contextualist interpretation substantially or entirely destroys the parol evidence rule. That is because contextualism eliminates the ambiguity determination and thus permits the use of extrinsic evidence to establish a special meaning that contradicts the standard meaning of the contract language.[525] This part addresses whether anything remains of the parol evidence rule in a contextualist interpretive regime.

Let me start with a review of first principles. As I explained in Part II,[526] contract interpretation and the parol evidence rule—in their pure forms—address distinct but closely-connected subjects. Interpretation concerns the process for determining the *meaning* of the terms of an agreement. The parol evidence rule governs whether evidence of prior or contemporaneous terms may be used to *contradict* or *add* to a written contract. Numerous scholars endorse this framework.[527]

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521 *See, e.g.*, Still v. Cunningham, 94 P.3d 1104, 1109 (Alaska 2004); Taylor v. State Farm Mut. Auto. Ins. Co., 854 P.2d 1134, 1140 (Ariz. 1993); Riverisland Cold Storage, Inc. v. Fresno-Madera Prod. Credit Ass'n, 291 P.3d 316, 318–19 (Cal. 2013); Boyer v. Karakehian, 915 P.2d 1295, 1299 (Colo. 1996); Huggins v. Huggins & Harrison, Inc., 103 A.3d 1133, 1140 (Md. Ct. Spec. App. 2014); Briggs v. Kidd & Leavy Real Est. Co., L.L.C., No. 340713, 2018 WL 4603900, at *2 (Mich. Ct. App. Sep. 25, 2018); Conway v. 287 Corp. Ctr. Assoc., 901 A.2d 341, 346 (N.J. 2006); Sanders v. FedEx Ground Package Sys., Inc., 188 P.3d 1200, 1206 (N.M. 2008); Brogan & Anensen LLC v. Lamphiear, 202 P.3d 960, 961 (Wash. 2009).

522 Pac. Gas & Elec. Co. v. G.W. Thomas Drayage & Rigging Co., 442 P.2d 641, 645 (Cal. 1968); *see also supra* note 312 (identifying three other decisions from contextualist states that contain comparable language).

523 *See* RESTATEMENT (SECOND) OF CONTRACTS §§ 209–10, 213–218 (AM. L. INST. 1981); *see also supra* Part II.B (primarily using the *Restatement* to explain the parol evidence rule).

524 *See supra* note 317 and accompanying text.

525 *See supra* Parts III, VII.A.

526 *See supra* note 107 and accompanying text.

527 *See, e.g.*, Kniffin, *supra* note 11, at 77–78, 90 (summarizing the author's view); *id.* at 90–110 (setting forth the author's views in detail); *id.* at 81–90 (presenting the views of

To illustrate, suppose that two parties enter into a written contract under which Seller is obligated to deliver "lumber" to Buyer by "early December" at the price of $10.00 per unit.[528] The writing says nothing about Seller providing a warranty. Consider three scenarios based on these facts.

First, after the contract is executed, a dispute arises over the timing of delivery. The parties disagree as to the cutoff date established by "early December." Buyer asserts that the contract requires delivery by December 5, while Seller counters that the deadline is December 10. This is an *interpretive* argument. What does "early December" *mean*? If the matter proceeds to litigation, the court should apply the interpretation rules.

Second, suppose that the dispute instead concerns the quality of the lumber. Buyer maintains that the wood does not meet the requirements of an oral warranty that Seller and Buyer agreed to during the preliminary negotiations. Seller responds that the parties' written contract is a complete integration, and thus any such warranty promised is not actually an element of their deal. This is a *parol evidence rule* argument. May Buyer introduce evidence that would *add* an oral side term (the warranty) to the express terms contained in the written document? If the matter proceeds to litigation, the court should apply the principles that make up the parol evidence rule.[529]

Third, assume a dispute develops over the price of the lumber. Buyer contends that during the closing the parties orally agreed that Seller would provide the lumber for $8.00 per unit rather than $10.00. Seller replies that the written agreement is integrated with respect to price, and thus the oral promise of $8.00 per unit is not a part of their contract. This too is a *parol evidence rule* argument. May Buyer introduce evidence of an oral side term (the $8.00 price) that *contradicts* a provision set forth in the writing? If the matter proceeds to litigation, the court should apply the principles that make up the parol evidence rule.

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other scholars who endorse this framework); BURTON, *supra* note 1, §4.2.4, at 120–22; *id.* § 3.1.1, at 67; FARNSWORTH, *supra* note 17, § 7.12, at 466; MURRAY, *supra* note 38, § 83[A], at 416–17; *see also* CALAMARI AND PERILLO, *supra* note 7, § 3.9, at 129 ("Standard academic thinking . . . is to the effect that the parol evidence rule is distinct from the topic of interpretation.") (collecting authorities).

528 These facts are based upon *Donald W. Lyle, Inc. v. Heidner & Co.*, 278 P.2d 650 (Wash. 1954), and *Thompson v. Libbey*, 26 N.W. 1 (Minn. 1885).

529 I am using the phrase "parol evidence rule" here to refer to the entire parol evidence process—the integration analysis (step 1) and application of the contradiction and supplementation prongs of the parol evidence rule (step 2). *See supra* notes 68–78 and accompanying text.

These examples constitute archetypes of interpretation, addition, and contradiction. But those three categories significantly bleed together on the margins.[530] Partly as a result, many courts do not differentiate between interpretation and the parol evidence rule.[531] And scholars are divided over whether interpretation and the parol evidence rule can actually be differentiated.[532]

I side with the majority of commentators who maintain that interpreting is not the same as contradicting or adding terms, at least in cases that are at the core of those concepts. But even if I am correct as a general matter, there are good reasons to believe that contextualism specifically extinguishes the parol evidence rule by collapsing the distinction between interpretation, contradiction, and addition. Continuing with the example from above, suppose that Seller argues that "early December" possesses a special meaning in the parties' industry—delivery by December 31. Such a construction plainly conflicts with the standard meaning of the contractual language. But contextualist principles permit Seller to introduce extrinsic evidence in favor of this reading.[533] Does that entail that the *contradiction* prong of the parol evidence rule no longer exists? Likewise, suppose Buyer

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530 *See supra* note 12 and accompanying text (noting that it is exceptionally difficult to distinguish between interpretation and the parol evidence rule); *supra* notes 104–106 and accompanying text (explaining that courts are divided over what constitutes contradicting a contract rather than supplementing it); 12 WILLISTON, *supra* note 133, § 34:7, at 78–79 ("[A]s the cases make clear, the line between explaining and supplementing, on the one hand, and contradicting on the other, can become blurred.").

531 *See* Greenawalt, *supra* note 132, at 587 ("Many courts draw no clear distinction between a plain meaning rule and a parol evidence rule when it comes to interpretation."); BURTON, *supra* note 1, § 4.2.4, at 120 (same); Kniffin, *supra* note 11, at 110–20 (reviewing judicial opinions that conflated interpretation and the parol evidence rule); *see, e.g.*, Taylor v. State Farm Mut. Auto. Ins. Co., 854 P.2d 1134, 1140 (Ariz. 1993); Shay v. Aldrich, 790 N.W.2d 629, 641 (Mich. 2010); URI, Inc. v. Kleberg County, 543 S.W.3d 755, 764 (Tex. 2018).

532 Daniel, *supra* note 163, at 258 (explaining that scholars are split over whether interpretation and the parol evidence rule should be distinguished). For commentators who differentiate between interpretation and the parol evidence rule, see *supra* note 527. For some who do not, see CALAMARI AND PERILLO, *supra* note 7, § 3.9, at 128 (describing "the admissibility of extrinsic evidence on the question of *meaning*" as implicating "a second aspect of the parol evidence rule"), *id.* § 3.16, at 142–43 ("Corbin's discussion proceeds on the assumption that there is a clear-cut distinction between offering evidence of a consistent additional term and offering evidence on the issue of meaning. Nothing could be further from the truth."), and Linzer, *supra* note 12, at 801 ("Thus, the parol evidence rule and the plain meaning rule are conjoined like Siamese twins. Even though many academics and more than a few judges have tried to separate them, the bulk of the legal profession views them as permanently intertwined."). *See also* Kniffin, *supra* note 11, at 120–26 (criticizing various authorities for conflating interpretation and the parol evidence rule).

533 *See supra* Parts III, VII.A.

argues that "lumber" just means lumber of a particular quality in the industry—the same quality as in the oral warranty from the second hypothetical above.[534] Once again, contextualist principles allow Seller to offer extrinsic evidence supporting such a construction.[535] Does this entail that the *addition* prong of the parol evidence rule no longer exists? In short, does contextualism nullify the parol evidence rule by allowing parties to use extrinsic evidence to contradict or add to an integrated agreement under the guise of asserting that the text of the instrument possesses a special meaning?[536]

Many judges and scholars think that the answer is "yes" (or at least "largely yes"). Perhaps the most notorious exponent of this view is Judge Alex Kozinski, formerly of the Ninth Circuit Court of Appeals. In *Wilson Arlington Company v. Prudential Insurance Company of America*, Judge Kozinski cited a series of decisions embracing contextualist interpretation to support his conclusion that "the parol evidence rule has been severely eroded in many jurisdictions during the past few decades."[537] He added that "[o]ften, this erosion has been so complete as to render the parol evidence rule essentially meaningless," and cited *Pacific Gas* as an example.[538] He claimed that in that case, "the California Supreme Court, without expressly abolishing the parol evidence rule, cut the life out if it by permitting the introduction of extrinsic evidence to demonstrate the existence of an ambiguity even when the language of a contract is perfectly clear."[539] In a concurring opinion in *Dore v. Arnold Worldwide, Inc.*, Justice Marvin R. Baxter, formerly of the California Supreme Court, agreed with Judge Kozinski's assessment:

> *Pacific Gas* essentially abrogated the traditional rule that parol evidence is not admissible to contradict the plain meaning of an integrated agreement by concluding that, even if the agreement

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534 *See supra* text accompanying note 529.

535 *See supra* Parts III, VII.A.

536 *Cf.* Greenawalt, *supra* note 132, at 587–88 ("The second, more subtle, point is this: the distinction between evidence about the meaning of language and evidence about supplementary terms can blur if parties are free to use language as they choose. Thus, a party may claim that an omitted term was 'implicit' in the contract's language as a way to escape any bar on showing supplementary terms.").

537 912 F.2d 366, 370 (9th Cir. 1990).

538 *Id.*

539 *Id.* Judge Kozinski's attack on *Pacific Gas* in *Trident Center v. Connecticut General Life Insurance Co.*, 847 F.2d 564, 569 (9th Cir. 1988), is more well-known than *Wilson Arlington Company*. (The critical language from *Trident* is quoted *supra* in note 339.) But his analysis in *Wilson Arlington Company* is more focused on the parol evidence rule.

> "appears to the court to be plain and unambiguous on its face," extrinsic evidence is admissible to expose a *latent* ambiguity, i.e., the possibility that the parties actually intended the language to mean something different.[540]

However, there are two arguments that contextualism does not eviscerate the parol evidence rule.[541] The first goes as

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540 139 P.3d 56, 62 (Cal. 2006) (Baxter, J., concurring) (quoting Pac. Gas & Elec. Co. v. G.W. Thomas Drayage & Rigging Co., 442 P.2d 641, 644 (Cal. 1968)); *accord, e.g.*, Sullivan v. Sovereign Bancorp., Inc., 33 F. App'x 640, 642 (3d Cir. 2002) (applying Pennsylvania law) ("One clearly cannot rely upon inadmissible parol evidence to create an ambiguity that the oral statements then resolve. Such bootstrapping would be the exception that destroys the parol evidence rule."); Individual Healthcare Specialists, Inc. v. Bluecross Blueshield of Tenn., Inc., 566 S.W.3d 671, 692 (Tenn. 2019) ("Under the *Pacific Gas* approach, if extrinsic evidence shows that the contractual language does not comport with the parties' 'actual' intent, the court may override the written words if doing so is necessary to 'correct' the written agreement."); Hous. Expl. Co. v. Wellington Underwriting Agencies, Ltd., 352 S.W.3d 462, 475 (Tex. 2011) (Jefferson, C.J., dissenting) ("To consider deleted language or other previous drafts or negotiations [when construing a facially unambiguous contract] would destroy the parol evidence rule without easing interpretation."); Gilson et al., *supra* note 6, at 36 ("Under this [contextualist] regime, interpretive doctrines such as the parol evidence rule are treated merely as prima facie guidance, which courts can (and should) override by considering additional evidence of the context of the transaction if they believe that doing so is necessary to substantially 'correct' or complete the parties' written contract by realigning it with its 'true' meaning."); Goldstein, *supra* note 32, at 100–02 (concluding that contextualism dispenses with the prohibition on using extrinsic evidence to vary or contradict the express terms of an agreement); Madeleine Plasencia, *Who's Afraid of Humpty Dumpty: Deconstructionist References in Judicial Opinions*, 21 SEATTLE UNIV. L. REV. 215, 241 (1997) (arguing that *Pacific Gas* and two other leading California cases decided around the same time "virtually eliminated the parol evidence rule in California"); *see also, e.g.*, Fid. & Deposit Co. of Md. v. City of Sheboygan Falls, 713 F.2d 1261, 1271 (7th Cir. 1983) (Posner, J.) ("The concept of latent ambiguity may seem to do away with the parol evidence rule . . . ."); Delta Dynamics, Inc. v. Arioto, 446 P.2d 785, 789 (Cal. 1968) (Mosk, J., dissenting) (warning that the three California decisions discussed by Plasencia, *supra*, adopted "a course leading toward emasculation of the parol evidence rule"); Stryker Corp. v. Nat'l Union Fire Ins. Co., 842 F.3d 422, 427 (6th Cir. 2016) (applying Michigan law) (describing contextualist interpretation as a "[b]reaking from the parol evidence rule"); Mark K. Glasser & Keith A. Rowley, *On Parol: The Construction and Interpretation of Written Agreements and the Role of Extrinsic Evidence in Contract Litigation*, 49 BAYLOR L. REV. 657, 669 (1997) (explaining that contextualist interpretation "does substantially undercut the exclusionary effect of the parol evidence rule").

541 Note that courts sometimes contend that the parol evidence rule still possesses life under contextualism without presenting any reasoning in support of their position. *Donoghue v. IBC USA (Publications), Inc.*, 70 F.3d 206 (1st Cir. 1995) (applying Massachusetts law), is illustrative. There, the court concluded that although the consideration of extrinsic evidence during the ambiguity determination "at first glance . . . may seem to subvert . . . the parol evidence rule . . . , closer examination discloses that proceeding in this way facilitates decisions consistent with . . . the rule." *Id.* at 215. But the court did not support this conclusion with any arguments. Instead, it simply recapitulated contextualism and the policy underlying that school of interpretation. *Id.* at 215–16. *See also* Cohanzick Partners, L.P. v. FTM Media, Inc., 120 F. Supp. 2d 352, 360 (S.D.N.Y. 2000) ("The Arizona Supreme Court did not eliminate the parol evidence rule when it decided *Taylor*. Indeed, it expressly stated, at three separate places in the opinion, that the parol evidence rule is still applicable.") (referring to Taylor v. State Farm Mut. Auto. Ins. Co., 854 P.2d 1134, 1138–41 (Ariz. 1993), the case in which the

follows: When extrinsic evidence of a special meaning is not sufficient to establish that a contract is ambiguous—i.e., when the evidence is not strong enough to send the case to the jury—it is the parol evidence rule that bars the evidence from serving any further role in the lawsuit. Extrinsic evidence is frequently too weak to create a question of fact regarding whether the parties employed a special meaning in drafting their contract.[542] Accordingly, the parol evidence rule restricts the admission of evidence in many cases, and thus the rule still operates under contextualism.

A number of decisions in contextualist jurisdictions embrace a version of this argument. For example, in *Taylor v. State Farm Mutual Automobile Insurance Company*, the Arizona Supreme Court wrote:

> [T]he judge need not waste much time if the asserted interpretation is unreasonable or the offered evidence is not persuasive. A proffered interpretation that is highly improbable would necessarily require very convincing evidence. In such a case, the judge might quickly decide that the contract language *is not reasonably susceptible to the asserted meaning*, stop listening to evidence supporting it, *and rule that its admission would violate the parol evidence rule*.[543]

Pursuant to this language, when contractual text is "not reasonably susceptible to the asserted [special] meaning," admitting evidence in support of that meaning "would violate the parol evidence rule."[544] But remember that contextualism jettisons the reasonably susceptible standard as a genuine constraint on the scope of possible interpretations.[545] Instead, the "ambiguity" determination under contextualism is simply an assessment of the weight of the evidence: Is the extrinsic evidence sufficient to advance the case to a jury?[546] As a result, what *Taylor* actually provides is that "admission [of extrinsic evidence] would violate the parol evidence rule" any time

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Arizona Supreme court firmly endorsed contextualism) (offering no additional analysis supporting the claim that the parol evidence rule still functions in Arizona); Isbrandtsen v. N. Branch Corp., 556 A.2d 81, 84–85, 85 n.* (Vt. 1988) (endorsing contextualism, observing in a footnote that the parol evidence rule continues to exist, but providing no real analysis on that point).

542 *See supra* notes 340–345, 458–461, and accompanying text.

543 854 P.2d 1134, 1141 (Ariz. 1993) (emphasis added).

544 *Id.*; *see also id.* at 1138–41 (explaining in detail the principles of Arizona's contextualism).

545 *See supra* notes 314–339 and accompanying text.

546 *See supra* notes 340–342 and accompanying text; *see also supra* Parts VIII.A, VIII.B (identifying examples where the evidence is not strong enough to create a jury question under contextualism and other examples where it is sufficiently strong).

evidence of a non-standard meaning is too weak to create a question of fact.

To the same effect is the Ninth Circuit's opinion applying California law in *A. Kemp Fisheries, Inc. v. Castle & Cooke, Inc.*: "If, after considering the evidence, the court determines that the contract is not reasonably susceptible to the interpretation advanced, the parol evidence rule operates to exclude the evidence. The court may then decide the case on a motion for summary judgment."[547]

The logic implicit in this argument is somewhat easier to see under textualism, so I will begin there. Suppose Buyer and Seller enter into a facially unambiguous contract. Such a contract is, by definition, not reasonably susceptible to the meaning asserted by one of the parties.[548] Assume, therefore, that the judge correctly rules that Buyer's reading is consistent with the ordinary meaning of the text while Seller's is not. In that case, if the court permits Seller to proffer extrinsic evidence supporting its construction, the evidence is necessarily being used to contradict or add to the contract because the judge has already rejected Seller's interpretation. Judge Posner puts the point this way: "If the written contract is clear without extrinsic evidence, then such evidence could have no office other than to contradict the writing, and is therefore excluded."[549] And what bars both contradiction and addition? The parol evidence rule.[550]

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547 852 F.2d 493, 496 n.2 (9th Cir. 1988); *see also* Mellon Bank, N.A. v. Aetna Bus. Credit, Inc., 619 F.2d 1001, 1010 n.9 (3d Cir. 1980) ("If the written contract is unambiguous, the Parol Evidence Rule and the doctrines cited above bar the use of extrinsic evidence for interpretation. If the written contract is ambiguous the Parole [sic] Evidence Rule does not prevent the use of extrinsic evidence to interpret the writing."); Shay v. Aldrich, 790 N.W.2d 629, 641–42 (Mich. 2010) (endorsing contextualism and explaining that the parol evidence rule "prohibits the use of extrinsic evidence to interpret unambiguous language within a document").

548 Because we are dealing with textualism, I am using "reasonably susceptible" in the true sense here. *See supra* notes 304–306 and accompanying text (describing that sense).

549 *In re* Envirodyne Indust., Inc., 29 F.3d 301, 305 (7th Cir. 1994) (Posner, C.J.); *accord* Garza v. Marine Transp. Lines, Inc., 861 F.2d 23, 26–27 (2d Cir. 1988) ("In the absence of ambiguity, the effect of admitting extrinsic evidence would be to allow one party to substitute his view of his obligations for those clearly stated.") (internal quotation marks omitted). Authorities have long recognized this point. *See, e.g.*, 22 C.J. *Evidence* § 1570, 1177–78 (1920) ("Where the language used is clear and unambiguous, extrinsic evidence is not admissible on the ground of aiding the construction, for in such cases the only thing which could be accomplished would be to show the meaning of the writing to be other than what its terms express, and the instrument cannot be varied or contradicted under the guise of explanation or construction.").

550 Of course, this presumes that the writing is a complete integration. *See supra* text accompanying notes 68–72.

Similar analysis can be applied to contextualism. Modifying the example from the previous paragraph, suppose a judge correctly decides that the parties' written contract is not "reasonably susceptible" to the special meaning advanced by Seller because the extrinsic evidence supporting that construction is too weak. In that situation, if the court allows Seller to introduce its extrinsic evidence, the evidence is once again necessarily being used to contradict or add to the contract because the judge has already rejected Seller's interpretation. But such evidence is obviously inadmissible under contextualism; if extrinsic evidence of a non-standard meaning is insufficient to create a question of fact, then the judge will dispose of the interpretation issue at summary judgment in favor of the party arguing for the standard meaning of the contract.[551] And if weak interpretive evidence is barred from trial under contextualism, then contextualism continues to restrict the precise type of evidence governed by the parol evidence rule because weak interpretive evidence *just is* evidence of contradictory or additional terms, pursuant to this argument. As a result, the parol evidence rule remains operational under contextualism.

I think it is helpful to refer to this as the "mirror-image argument." That is because the argument focuses on the fact that contradiction and addition together are the mirror image of interpretation: Whenever evidence purporting to construe an agreement does not qualify as interpretive—because it supports a construction that is inconsistent with the ordinary meaning of the contract under textualism, or because the evidence is not strong enough to create a question of fact over whether the parties intended a special meaning under contextualism—it must fall into either the contradiction category or the addition category. And both of those categories are governed by the parol evidence rule.[552]

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551 *See supra* Part VIII.A (the most helpful material is in note 461 and the accompanying text).

552 Note that there is a gap in this reasoning: It cannot fully account for the treatment of course of performance evidence. The parol evidence rule only bars extrinsic evidence regarding side terms agreed to *prior to* or *contemporaneously with* execution of an integration. *See supra* text accompanying notes 71–72. Evidence concerning terms agreed to *after* formation is outside the scope of the rule. *See supra* text accompanying note 85. A course of performance necessarily occurs subsequent to the parties entering a contract. *See supra* note 31 (defining course of performance). The parol evidence rule thus cannot restrict the use of course of performance evidence unless the evidence is specifically employed to assert the existence of pre-contractual side terms, which is likely rare. This means that in a textualist state, if a contract is facially unambiguous, the prohibition on considering course of performance evidence typically flows exclusively from

It is critical to keep in mind that under the mirror-image argument, what distinguishes interpretive evidence from contradictory or supplementary evidence in a contextualist regime is the *weight* of the extrinsic evidence at issue.[553] If the evidence is strong enough to submit the asserted special meaning to the jury, then the evidence concerns interpretation and may be presented at trial. If the evidence is not strong enough to submit the asserted special meaning to the jury, then the evidence concerns contradiction or addition and is inadmissible at trial. Contextualism preserves the parol evidence rule, according to this argument, because evidence of contradictory or additional terms (i.e., weak interpretive evidence) is barred under that system.[554]

While the mirror-image argument has some commendable features,[555] the argument fails to establish that the parol

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the plain meaning rule. Likewise, in a contextualist state, any limitation on using course of performance evidence normally is derived entirely from the rules of interpretation. *See* CHRISTINA L. KUNZ & CAROL L. CHOMSKY, CONTRACTS: A CONTEMPORARY APPROACH 645 (2010) (explaining that course of performance "enjoys a favored position with respect to the parol evidence rule" and "cannot be barred by the parol evidence rule" if the evidence is presented by skillful attorneys, in part because "course of performance arises from conduct after contract formation"). Accordingly, even if contradiction and addition are the mirror image of interpretation as Judge Posner and others have asserted, the parol evidence rule does not apply in every circumstance in which extrinsic evidence is barred on grounds that it contradicts or adds to the contract. Put another way, the parol evidence rule is not implicated every time a party tries to (1) submit extrinsic evidence to construe a patently unambiguous contract under textualism, or (2) submit extrinsic evidence that is too weak to establish the existence of a non-standard-meaning latent ambiguity under contextualism. But as I am about to explain, the mirror-image argument fails to establish that contextualism preserves the parol evidence rule. And so this particular flaw in the argument is not of critical importance.

553 Under textualism, by contrast, the distinction is qualitative; interpretive evidence and evidence of contradictory or supplemental terms are different in kind.

554 To be fair, contextualist courts may not actually be contending that the difference between interpretive evidence and contradictory or supplemental evidence is nothing more than the strength of the evidence. The cases that set forth some version of the mirror-image argument are generally rather vague. A more charitable reading might thus lead one to conclude that these courts are asserting something other than the mirror-image argument. However, because it is plausible to construe various contextualist decisions as advocating for the mirror-image argument in the form I have described, I concluded that it was important to address that argument.

555 For example, the argument illustrates the close relationship of contract interpretation and the parol evidence rule. The argument therefore helps to explain why courts so often conflate the two areas of law, such as when they write statements like this: "[W]hen a contract is *unambiguous*, the *parol evidence* rule bars our consideration of extrinsic evidence." Saregama India Ltd. v. Mosley, 635 F.3d 1284, 1290 (11th Cir. 2011) (emphasis added); *see also supra* note 531 and accompanying text (discussing courts that do not differentiate between interpretation and the parol evidence rule and providing additional examples); BURTON, *supra* note 1, § 4.2.4, at 120–22 (arguing that quotations like the one from *Saregama* "confuse[] the parol evidence and plain meaning rules," in part because the former rule "applies when an agreement is integrated, whether or not it

evidence rule exists under contextualism. To understand this, we must start with a recap of the reasoning supporting my conclusion in Part VII that contextualism dispenses with the ambiguity determination and its associated reasonably susceptible standard. The essence of the ambiguity determination—which is embraced by textualism—is that language places an absolute limit on the spectrum of possible meanings of a contract. Only when express terms are reasonably susceptible to an asserted construction under standard usage may the judge consider extrinsic evidence supporting that interpretation.[556] In other words, if a proposed understanding of an agreement falls outside the "zone of reasonableness,"[557] then the court must reject that reading and bar any supporting extrinsic evidence from consideration *regardless of the weight of that evidence*.

But under contextualism, the text of an agreement can possess *any* meaning *if the extrinsic evidence favoring that reading is strong enough*.[558] On this view, contractual language is infinitely flexible, which constitutes a complete rejection of the reasonable susceptibility standard.[559] Accordingly, contextualism eliminates the ambiguity determination.[560]

The crucial point to take from the prior two paragraphs is that evaluating whether an ambiguity exists is not the same thing as evaluating the strength of extrinsic evidence. Those two assessments are conceptually distinct. Think about it this way: If all that matters is the *weight* of the extrinsic evidence, then language cannot impose an *absolute* limit on the scope of potential readings of a contract. As a result, because contextualism reduces the ambiguity determination to an assessment of whether the extrinsic evidence sufficiently supports the asserted meaning,[561] *there is no ambiguity determination* under that approach.

Shifting back to the parol evidence rule, that rule operates by discharging side terms agreed to by the parties prior to or

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is ambiguous").

556 *See supra* notes 304–309, and accompanying text.

557 *See* Allen v. United States, 119 Fed. Cl. 461, 480 (2015) ("In order to demonstrate ambiguity, the interpretations offered by both parties must fall within a 'zone of reasonableness.") (internal quotation marks omitted).

558 *See supra* notes 338–339 and accompanying text.

559 *See supra* notes 324–329, and accompanying text.

560 *See supra* note 332 and accompanying text. For the full discussion of the points set forth in this and the prior paragraph, see *supra* Parts VII.A. and VII.B.

561 *See supra* notes 340–345, and accompanying text.

contemporaneously with the formation of a written contract. Since the side terms are extinguished, any extrinsic evidence supporting the existence of those terms is legally irrelevant. And that is true regardless of the strength of the evidence indicating that the parties in fact consented to the side terms. As Professor Burton explained:

> When offered to establish contract terms, the [parol evidence] rule precludes the introduction of evidence of even relevant, probative, and non-prejudicial parol agreements, *no matter what kind of evidence is involved* . . . . [W]hen the rule applies, evidence of a parol agreement is *irrelevant* when offered to establish an agreement's terms.[562]

In *Marani v. Jackson*, the California Court of Appeal presented the point this way:

> The parol evidence rule is not merely a rule of evidence excluding precontractual discussions for lack of credibility or reliability. It is a rule of substantive law making the integrated written agreement of the parties their exclusive and binding contract *no matter how persuasive the evidence* of additional oral understandings. Such evidence is legally irrelevant and cannot support a judgment.[563]

Numerous other primary and secondary authorities are in accord.[564] Therefore, the parol evidence rule functions in the same manner as the ambiguity determination: It sets an *absolute* limit on the consideration of extrinsic evidence. And a limit is absolute only if it governs regardless of the weight of the evidence.[565]

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562 BURTON, *supra* note 1, § 3.1.1, at 65 (emphasis added).

563 228 Cal. Rptr. 518, 521 (Cal. Ct. App. 1986) (emphasis in original).

564 *See, e.g.*, Baum v. Great W. Cities, Inc. of N.M., 703 F.2d 1197, 1205 (10th Cir. 1983); IIG Wireless, Inc. v. Yi, 231 Cal. Rptr. 3d 771, 783 (Cal. Ct. App. 2018); EPA Real Est. P'ship v. Kang, 15 Cal. Rptr. 2d 209, 211 (Cal. Ct. App. 1992); Calomiris v. Woods, 727 A.2d 358, 361–62 (Md. 1999); Abercrombie v. Hayden Corp., 883 P.2d 845, 850 (Or. 1994); DeClaire v. G & B McIntosh Family Ltd. P'ship, 260 S.W.3d 34, 45 (Tex. Ct. App. 2008); RESTATEMENT (SECOND) OF CONTRACTS § 215 cmt. a (AM. L. INST. 1981) ("A binding integrated agreement discharges inconsistent prior agreements, and evidence of a prior agreement is therefore irrelevant to the rights of the parties when offered to contradict a term of the writing."); CALAMARI AND PERILLO, *supra* note 7, § 3.2(c), at 111 ("If the court decides that the parol evidence rule has been violated, it will exclude the proffered term not because it was not agreed upon, but because it is legally immaterial."); FARNSWORTH, *supra* note 17, § 7.2, at 416; MURRAY, *supra* note 38, § 83[B], at 419.

565 Note that when I state that the parol evidence rule bars extrinsic evidence regardless of weight, I am referring only to the second step of the parol evidence rule analysis—application of the limitations on contradiction and supplementation. I am not referring to the first step—whether the writing at issue is a partial or complete integration. The weight of extrinsic evidence can be relevant at step one because some courts look beyond the four corners of the instrument in deciding whether the document is integrated. *See supra* notes 94–98 and accompanying text.

This creates a fatal problem for the mirror-image argument. That argument provides that the parol evidence rule survives under contextualism because sometimes extrinsic evidence is too weak to establish a non-standard-meaning latent ambiguity.[566] One of the assumptions underlying this thesis is that to demonstrate that the parol evidence rule exists, it is sufficient that the admissibility of extrinsic evidence within the scope of the rule turns on the *strength* of the evidence. In other words, the parol evidence rule is operational as long as it is understood to at least bar evidence from the jury *on the basis of weight*. But as I explained in the prior paragraph, for the parol evidence rule to perform its constituting function, it must do more than this; it must prohibit evidence *irrespective of weight* because the rule is supposed to serve as an absolute restriction on the contradiction and supplementation of a written agreement. This means that a key premise of the mirror-image argument is false. Accordingly, the argument fails to establish that contextualism preserves the parol evidence rule.[567]

Now let's turn to the second argument that contextualism retains the parol evidence rule. Contextualist authorities often emphasize that extrinsic evidence may be employed only to give meaning to express contractual terms, not to establish the existence of different or additional terms that are not set forth in the parties' written agreement. For instance, the Washington Court of Appeals wrote the following in *Pelly v. Panasyuk*: "Extrinsic evidence is to be used only to illuminate what was written, not what was intended to be written. Extrinsic evidence is not admissible . . . to show an intent independent of the instrument; or to vary, contradict, or modify the written word."[568] Here is a similar statement from the

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566 *See supra* text accompanying notes 542 and 551–554.

567 *Cf.* LINZER, 6 CORBIN ON CONTRACTS, *supra* note 8, § 25.15[E], at 201 (construing Admiral Builders Sav. and Loan Ass'n v. S. River Landing, Inc., 502 A.2d 1096, 1100 (Md. Ct. Spec. App. 1986), to stand for the proposition that "if you claim an ambiguity [in particular, a non-standard-meaning latent ambiguity] but put forth evidence that is unbelievable, the issue must be resolved against you—not because of the parol evidence rule, but because you haven't made out your case."); *id.* at 207 (construing Lazy Dog Ranch v. Telluray Ranch Corp., 965 P.2d 1229, 1235–36 (Col. 1998), to stand for the proposition "that unconvincing extrinsic evidence should not be excluded but should be disregarded—not because of the parol evidence rule, but because it is unconvincing"). By distinguishing between (1) evidence that is prohibited by the parol evidence rule, and (2) evidence that is rejected because it is "unbelievable" or "unconvincing," the *Corbin* treatise seems to recognize that assessing the weight of interpretive evidence is not the same as applying the parol evidence rule, which is essentially my point in the body text.

568 413 P.3d 619, 629 (Wash. Ct. App. 2018) (citations and internal quotation marks omitted).

Third Circuit applying Pennsylvania law in *Bohler-Uddeholm American Insurance v. Ellwood Group, Inc.*:

> A party may use extrinsic evidence to support its claim of latent ambiguity, but this evidence must show that some specific term or terms in the contract are ambiguous; it cannot simply show that the parties intended something different that was not incorporated into the contract. . . . "[T]he parties' expectations, standing alone, are irrelevant without any *contractual hook* on which to pin them."[569]

Many other decisions from contextualist states contain comparable language.[570]

Tilley v. Green Mountain Power Corporation, an opinion of the Vermont Supreme Court, illustrates the principle articulated in *Pelly* and *Bohler-Uddeholm*.[571] There, the plaintiff-landowners and the defendant-power company entered into a contract granting the defendant an easement to run a power line on the plaintiffs' property.[572] During the preliminary negotiations, the power company orally assured the owners that "'the power line would not be enlarged in scope.'"[573] But the executed written agreement expressly permitted the power company to "add to"

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569 247 F.3d 79, 93 (3d Cir. 2001) (quoting Duquesne Light Co. v. Westinghouse Elec. Corp., 66 F.3d 604, 614 n.9 (3d Cir. 1995)); *accord id.* at 94 n.3 ("In particular, we think that the key inquiry in this context will likely be whether the proffered extrinsic evidence is about the parties' objectively manifested linguistic reference regarding the terms of the contract, or is instead merely about their expectations. The former is the right type of extrinsic evidence for establishing latent ambiguity under Pennsylvania law, while the latter is not.") (internal quotation marks and citations omitted).

570 *See, e.g.*, Dept. of Indus. Relat. v. UI Video Stores, Inc., 64 Cal. Rptr. 2d 457, 462 (Cal. Ct. App. 1997) ("Generally speaking, the rules of interpretation of written contracts are for the purpose of ascertaining the meaning of the words *used* therein; evidence cannot be admitted to show intention independent of the instrument.") (citations, internal quotation marks, and modifications omitted); Hayter Trucking, Inc. v. Shell W. E & P, Inc., 22 Cal. Rptr. 2d 229, 238 (Cal. Ct. App. 1993); Atl. N. Airlines, Inc. v. Schwimmer, 96 A.2d 652, 656 (N.J. 1953) ("So far as the evidence tends to show, not the meaning of the writing, but an intention wholly unexpressed in the writing, it is irrelevant."); Conway v. 287 Corp. Ctr. Assocs., 901 A.2d 341, 346–47 (N.J. 2006) (quoting the sentence from the prior parenthetical); Marshall v. Thurston County, 267 P.3d 491, 494 (Wash. Ct. App. 2011); Renfro v. Kaur, 235 P.3d 800, 803 (Wash. Ct. App. 2010); Bort v. Parker, 42 P.3d 980, 988 (Wash. Ct. App. 2002); *see also* RESTATEMENT (SECOND) OF CONTRACTS § 212 cmt. c (AM. L. INST. 1981) ("The rule of Subsection (1) permits reference to the negotiations of the parties, including statements of intention and even positive promises, *so long as they are used to show the meaning of the writing*.") (emphasis added); Arthur L. Corbin, *The Interpretation of Words and the Parol Evidence Rule*, 50 CORNELL L. Q. 161, 171 (1965) ("Extrinsic evidence is admissible to aid in the process of interpretation . . . [and] to determine the meaning of language that the parties actually gave to it . . . . Such evidence is never relevant or admissible when offered for the purpose of establishing another meaning or intention and to expound and enforce a different contract. Contradiction, deletion, substitution: these are not interpretation.").

571 587 A.2d 412 (Vt. 1991).

572 *Id.* at 413.

573 *Id.*

the power line on plaintiffs' property.[574] When the defendant sought to make changes within the easement that would increase the size of the power line and impact the plaintiffs' view from their land, the plaintiff sued to stop the power company's work.[575] Citing the Vermont Supreme Court's then-recent endorsement of contextualism,[576] the trial judge considered testimony regarding the pre-contractual oral assurance during the ambiguity determination, found the contract ambiguous, and then resolved the ambiguity in favor of the plaintiffs.[577]

The Vermont Supreme Court reversed. It explained that its earlier decision embracing contextualism contained a footnote which "cautioned that the parol evidence rule is still good law."[578] In the case at bar, "the verbal assurance was not simply a context giving meaning to the written agreement; rather, the verbal assurance was an oral, contractual term directly contradicting the later written expression of agreement."[579] Put using the terminology of the *Pelly* and *Bohler-Uddeholm* opinions, the extrinsic evidence in *Tilley* was not offered to construe language from the parties' contract; the evidence was not connected to any "textual hook" within the agreement. Instead, the plaintiff-landowners sought to present evidence of a contradicting side term—to introduce evidence of the parties' intent "independent of the instrument." And that is precisely the type of evidence that the parol evidence rule prohibits. The *Tilley* Court ended by noting that "[t]he rule permitting contracts to be read in light of surrounding circumstances should not be allowed, as it did here, to swallow up the parol evidence rule."[580]

According to cases like *Pelly*, *Bohler-Uddeholm*, and *Tilley*, contextualism preserves the parol evidence rule because extrinsic evidence is barred—no matter how strong—if the evidence is offered to establish the existence of terms *not set forth* in the parties' written agreement. A judge may admit extrinsic evidence only when it is presented for the purpose of *construing specific contractual language*. Explained using my standard hypothetical, the parol evidence rule exists under contextualism because extrinsic evidence can be employed to interpret the language "early December," but *not* to demonstrate that Buyer and Seller

574 *Id.*
575 *Id.*
576 Isbrandtsen v. N. Branch Corp., 556 A.2d 81, 84–85 (Vt. 1988).
577 *Tilley*, 587 A.2d at 413.
578 *Id.* at 414 (citing *Isbrandtsen*, 556 A.2d at 84 n.*).
579 *Id.*
580 *Id.*

orally agreed to a delivery deadline of December 31 or to a warranty not referenced in the contract.[581] I think it is best to describe this line of reasoning as the "textual hook argument."

Note that under the textual hook argument, the same piece of evidence can be relevant for purposes of interpretation, but prohibited if offered in support of an additional or contradicting term.[582] Testimony about a remark made during preliminary negotiations, for example, might be allowable if offered to construe an express contractual provision, but barred if offered to establish the existence of a side term allegedly adopted prior to formation of the agreement.[583] In the abstract, this creates no problem for the textual hook argument because the fact that a rule only limits evidence for some purposes is generally irrelevant to whether the rule exists.

To illustrate, consider Federal Rule of Evidence 404. Rule 404(b)(1) prohibits the use of evidence of a "crime, wrong or other act . . . to prove a person's character in order to show that on a particular occasion the person acted in accordance with the character."[584] Subsection (b)(2) of the rule states that the same evidence "may be admissible for another purpose, such as proving

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581 *See* Bionghi v. Metro. Water Dist. of So. Cal., 83 Cal. Rptr. 2d 388, 393 (Cal. Ct. App. 1999) ("*Pacific Gas & Electric* is thus not a cloak under which a party can smuggle extrinsic evidence to add a term to an integrated contract, in defeat of the parol evidence rule.") (further explaining that during the ambiguity determination, "the court must give consideration to any evidence offered to show that *the parties' understanding of words used differed from the common understanding*" (emphasis added)); Brawthen v. H & R. Block, Inc., 104 Cal. Rptr. 486, 490 (Cal. Ct. App. 1972) ("But this rule [from *Pacific Gas*] must be restricted to its stated bounds; it does no more than allow extrinsic evidence of the parties' understanding and intended meaning of the words used in their written agreement. While it allows parol evidence for this purpose, it is unconcerned with extrinsic collateral agreements."); FARNSWORTH, *supra* note 17, § 7.12, at 466 ("Accordingly, even under the liberal view [contextualism], extrinsic evidence is admissible . . . only where it is relevant to ambiguity and vagueness rather than inaccuracy or incompleteness."). In my example, I am presuming that the contract is a complete integration and that the side terms were agreed upon prior to or contemporaneously with the execution of the instrument.

582 RESTATEMENT (SECOND) OF CONTRACTS § 215 cmt. a (AM. L. INST. 1981) (explaining that extrinsic evidence is "irrelevant . . . when offered to contradict a term of the writing" but "may nevertheless be relevant to a question of interpretation"); Kniffin, *supra* note 11, at 92 ("The same item of extrinsic evidence might therefore be admissible to explain the parties' intended meaning, but inadmissible regarding whether they intended to include an additional term.").

583 *See, e.g.*, Sherman v. Mut. Benefit Life Ins. Co., 633 F.2d 782, 783–85 (9th Cir. 1980) (holding that evidence regarding an assurance that a sales agent would only be fired for cause could be offered to construe a clause providing for termination on 60 days notice or if the company deemed dismissal necessary in its judgment, but could not be offered to assert the existence of a supplemental side term because the written contract at issue was a complete integration).

584 FED. R. EVID. 404(b)(1).

motive, opportunity, intent, preparation, plan, knowledge, identity, absence of mistake, or lack of accident."[585] Critically, the various exceptions in subsection (b)(2) do not eliminate the restriction in subsection (b)(1); rule 404(b)(1) imposes a true limitation on the use of evidence even though the evidence governed by the rule can still be offered for the reasons enumerated in subsection (b)(2). This confirms that a prohibition on using evidence for a particular purpose is a genuine restriction even if the same evidence can be presented for other purposes. As a result, the parol evidence rule exists as long as it blocks the submission of extrinsic evidence for at least some purposes, which it does according to the textual hook argument.

However, one might counter that while the parol evidence rule bars certain uses of extrinsic evidence as a technical matter, the prohibition is illusory in substance. Recall that contextualism permits contracting parties to assert that the language in their agreement possesses a special meaning that is identical in content to a conflicting or additional side term otherwise discharged by the parol evidence rule.[586] This follows, in part, from contextualism's embrace of the infinite flexibility of language.[587] If words can possess any meaning, this objection continues, then a "textual hook" requirement is incapable of imposing a bona fide restraint on the use of extrinsic evidence. If text is always susceptible to any understanding, then side terms and their supporting evidence can always be recast as constructions of express terms and interpretive evidence. And thus capable attorneys can do an end run around the parol evidence rule by couching their arguments as concerning special meanings rather than distinct agreements covering additional and conflicting terms.[588]

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585 FED. R. EVID. 404(b)(2).

586 *See supra* notes 533–536, and accompanying text.

587 *See supra* notes 324–329, and accompanying text.

588 The Calamari and Perillo treatise can be read as advancing this position in several places. *See* CALAMARI AND PERILLO, *supra* note 7, § 3.9, at 129 ("The logic of this dichotomy [between interpretation and the parol evidence rule] is unassailable, so is its impracticality. The very same words offered as an additional term that are rejected because the court deems the writing to be a total integration, can be offered as an aid to interpretation of a written term."); *id.* § 3.16, at 142 ("A contradiction, however, may take place not only by offering into evidence a *term* that contradicts the writing or other record, but also by offering evidence as to *meaning* of the language of the agreement that contradicts the apparent meaning of the language."); *id.* § 3.16, at 143 ("Generally speaking, and certainly under the rules of the Restatement (Second) and Corbin, it is to the advantage of the party offering the evidence to couch the offer of proof in terms of both supplying an additional term and interpreting the writing."); *see also* Calamari & Perillo, *supra* note 193, at 352 ("If evidence of prior and contemporaneous expressions is not

If this objection is correct, then the textual hook argument fails and contextualism does indeed eliminate the parol evidence rule. But the objection is wrong; the textual hook requirement is real despite contextualism's theory of language.

Return to our primary fact pattern: Buyer and Seller enter into a contract for delivery of lumber in "early December." At the closing, Buyer orally assures Seller that delivery at any time before January 1 is sufficient. Later, a dispute erupts over whether Seller can provide the wood on December 31. According to the textual hook argument, the judge should not consider evidence of the assurance unless Seller connects the evidence to the "early December" language. According to the objection, because "early December" can possess any meaning under contextualism, such a connection requirement can always be satisfied.

To see the precise flaw with the objection, we must compare two more detailed versions of the hypothetical, both of which are presented in Chart 3.

admissible to prove terms supplementary to or at variance with a total integration, but is admissible to show the meaning of the integration, the astute trial lawyer will characterize his evidence on what are really supplementary or contradictory terms as evidence on the true meaning of the contract."); Daniel, *supra* note 163, at 258 ("In order to overcome the obstacle of introducing extrinsic evidence to define the terms of an agreement reduced to writing, parties will often state they are actually introducing such matter to 'explain' what the parties meant by the written agreement, and hence the end run around [the parol evidence rule].").

Chart 3

Scenario 1
Seller: Because of various logistical issues, we may not be able to get the lumber to you until the end of the month. Buyer: I can assure you that the end of the month won't be a problem. We always read delivery time periods in a flexible manner in the lumber industry.
Scenario 2
Seller: Because of various logistical issues, we may not be able to get the lumber to you until the end of the month. Buyer: I can assure you that the end of the month won't be a problem. We will accept any lumber received before the first the year. Seller: The contract says we have to provide the product in "early December." So you can see how this situation would make us nervous. Buyer: Yes, that language in the contract clearly obligates you to deliver before December 15, but as I said, we won't hold you to that, so no need to worry about signing the contract.

In Scenario 1, Buyer's oral assurance that it will accept delivery any time before January 1 is connected to the delivery term of the contract. Buyer made the promise, and then explained the basis for the promise as being that "[w]e always read delivery time periods in a flexible manner in the lumber industry." Given this statement, it is clear that Buyer was construing "early December" when offering the assurance. Therefore, testimony regarding the promise is *interpretive* evidence that the judge must consider during the ambiguity determination. In Scenario 2, by contrast, the assurance is not connected to the delivery term, nor to any other provision in the parties' agreement. It is a standalone promise reflecting contractual intent that is "independent of the instrument." In fact, Buyer expressly disavowed any linkage between the assurance and the delivery provision by endorsing the ordinary meaning of "early December": "Yes, that language in the contract clearly obligates you [Seller] to deliver before December 15." The lack of a "textual hook" means that any testimony regarding the promise is *not* interpretive evidence. Instead, it is evidence supporting the existence of a side term that contradicts the written agreement. Therefore, such evidence is irrelevant to the

ambiguity determination and is barred by the parol evidence rule.

The essence of the objection to the textual hook argument is that contextualism always permits evidence of side terms to be presented as interpretive evidence because contextualism embraces the infinite flexibility of language.[589] But the distinction between Scenarios 1 and 2 demonstrates that this is not true. Evidence that satisfies the textual hook requirement—evidence that genuinely concerns the meaning of contractual language, as in Scenario 1—is qualitatively different from evidence that addresses the existence of side terms, as in Scenario 2.

Let me explain further by offering a comparison. Contextualism eliminates the ambiguity determination. As a result, language can, in principle, possess any meaning under that approach. But it does not follow from this that all interpretation disputes in contextualist states should make it to a jury. Sometimes the extrinsic evidence supporting a special meaning is simply not strong enough to advance the case to stage 2 of the interpretive process.[590] The evidence is *quantitatively* insufficient. Likewise, in some cases, the extrinsic evidence offered does not concern interpretation at all; it does not purport to construe any language in the contract. Instead, it addresses something else, such as whether the parties agreed to additional or contradicting side terms. This type of evidence is *qualitatively* insufficient. It deals with the wrong subjects—including subjects that fall within the scope of the parol evidence rule.[591]

The fallacy underlying the objection is that it critically misunderstands the impact of the contextualist theory of language. Contextualism's rejection of the reasonably susceptible standard does nothing more than allow parties to present evidence at stage 1 of the interpretive process indicating that they used words in a non-standard way when drafting their agreement.[592] While this can result in express terms being understood in a manner that is wholly inconsistent with their ordinary meaning, jettisoning reasonable susceptibility does not otherwise eliminate the lines separating interpretation from other contractual categories such as contradiction, addition,

589 *See supra* text accompanying notes 586–588.

590 *See supra* notes 340–345, 458–461, and accompanying text.

591 And thus contextualism is ultimately like textualism in treating interpretive evidence and evidence of contradictory or supplemental terms as different in kind. *See supra* note 553.

592 *See supra* note 581 and accompanying text.

invalidation, and formation. And thus contextualism does not effectively turn all evidence relating to an agreement into interpretive evidence. For example, under contextualism, documents or testimony supporting the conclusion that the contract was induced by fraud or duress, that a party lacked capacity to enter the agreement, or that the parties orally consented to a side term, all remain conceptually distinct from evidence regarding the meaning of express provisions.[593] That is why the textual hook requirement is a true limitation on the use of extrinsic evidence, even though the words that make up a given textual hook can, in theory, possess any meaning.

Of course, it is frequently hard to classify evidence as concerning interpretation rather than contradiction or addition. As stated above, the distinctions between these three categories are unclear at the borderlines.[594] But at their cores, interpretation, contradiction, and addition are indeed different. This means that, contrary to the claims of the objection,[595] skillful attorneys cannot transform plainly contradictory or supplementary evidence into interpretation evidence.

On behalf of the objection, one might argue that lawsuits where the evidence is clearly not interpretive are rare, and that in the bulk of those cases parties commit perjury, enabling them to avoid application of the parol evidence rule. I do not doubt that many disputes involve evidence that can plausibly be treated as either interpretive or concerning side terms.[596] Likewise, litigants and third-party witnesses almost certainly lie under oath in some cases in order to convert evidence of side terms into evidence that appears to be about the construction of contractual language—into evidence that satisfies the textual hook requirement. But the reported

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593 *See id.*

594 *See supra* note 530 and accompanying text.

595 *See supra* note 588 and accompanying text.

596 In fact, California courts appear to believe that this is so common that they frequently combine analysis of interpretation and the parol evidence rule into a single test. *See, e.g.*, Hayter Trucking, Inc. v. Shell W. E & P, Inc., 22 Cal. Rptr. 2d 229, 238 (Cal. Ct. App. 1993) ("Application of the [parol evidence] rule involves a two-part analysis. First, was the writing intended to be an integration . . . ? Second, is the agreement susceptible of the meaning contended for by the party offering the evidence?"); Wang v. Massey Chevrolet, 118 Cal. Rptr. 2d 770, 781 (Cal. Ct. App. 2002) (same); Gerdlund v. Elec. Dispensers Int'l, 235 Cal. Rptr. 279, 282 (Cal. Ct. App. 1987) (same). As do courts in some other contextualist states. *See, e.g.*, Nautilus Marine Enters., Inc. v. Exxon Mobil Corp., 305 P.3d 309, 317–18 (Alaska 2013); Neal & Co. v. Ass'n. Vill. Council Presidents Reg'l Hous. Auth., 895 P.2d 497, 504 (Alaska 1995); *see also id.* at 504–05 (considering extrinsic evidence when interpreting the contract, concluding that the evidence was insufficient to establish an ambiguity, and then barring the same evidence under the parol evidence rule as inconsistent with the express terms).

caselaw strongly suggests that much extrinsic evidence submitted in litigated matters is definitively not interpretive, and that offering parties regularly testify truthfully despite the fact that the parol evidence rule will—or at least might—bar their statements from consideration in the lawsuit.

Tilley is illustrative. The power company's promise in that case was a contradicting term. It was not issued by the company as an interpretation of the contract. The landowner's attorney obviously argued otherwise, and was successful before the trial court. But no testimony—honest or fraudulent—was presented purporting to link the assurance to an express term. And so the Vermont Supreme Court reversed, correctly holding that evidence of the promise was barred by the parol evidence rule. *Tilley* is representative of opinions where courts rejected extrinsic evidence offered to construe an agreement because the evidence did not actually concern the meaning of the disputed contractual language.[597]

Sompo Japan Insurance Company of America v. Norfolk Southern Railway Company[598] is also instructive. There, Sompo presented trade usage evidence relating to the "exoneration clause" in the parties' bill of lading.[599] While the Second Circuit recognized that contextualist principles governed the dispute,[600] the court rejected the evidence because it was offered to nullify the exoneration clause rather than to address the clause's meaning:

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597 *See, e.g.*, Hunt Const. Grp., Inc. v. United States, 281 F.3d 1369, 1373 (Fed. Cir. 2002) (barring trade usage evidence because the offering party did "not claim that there is . . . a term of art included" in the contract that required construction based on such evidence); Jowett, Inc. v. United States, 234 F.3d 1365, 1368–70 (Fed. Cir. 2000) (rejecting "generalized" affidavits setting forth industry practices because the affidavits did not attempt to identify a "term in the contract that has an accepted industry meaning different from its ordinary meaning"); Bionghi v. Metro. Water Dist. of So. Cal., 83 Cal. Rptr. 2d 388, 393–95 (Cal. Ct. App. 1999) (holding that "a contract which provides that it may be terminated on specified notice cannot reasonably be interpreted to require good cause as well as notice of termination, unless extrinsic evidence establishes that the parties used the words in some special sense") (concluding that none of the extrinsic evidence submitted was actually interpretive in nature, in part because the evidence did not concern "the positions of the parties during the negotiations, their differences and agreements, or the way in which they selected words and phrases to express the terms agreed on").

598 762 F.3d 165 (2d Cir. 2014).

599 *Id.* at 180.

600 *Id.* ("Evidence of trade practice and custom may assist a court in determining whether a contract provision is ambiguous in the first instance. Terms that have an apparently unambiguous meaning to lay persons may in fact have a specialized meaning in a particular industry.") (citations omitted).

> But Sompo does not contend that terms in the Exoneration Clause have a specialized meaning in the transportation industry distinct from the ordinary or common meaning that would otherwise be ascribed to them. Instead, the industry practice evidence that Sompo offers is expert testimony that, regardless of what the exoneration clauses mean, they simply are not enforced. In other words, Sompo is asking us to consider evidence of industry practice and custom in order to persuade us to ignore the Exoneration Clause, not to help us interpret it.[601]

Note also that the parties in *Sompo Japan* were sophisticated commercial entities represented by expert counsel.[602] Yet Sompo's lawyers were unable to couch the trade usage evidence as interpretive in nature. *Sompo Japan* is representative of cases where extrinsic evidence was not even offered to establish the meaning of the words in an agreement, and thus there was no question that the evidence fell within the scope of the parol evidence rule and was barred.[603]

The foregoing establishes that the textual hook argument is successful: The rule providing that extrinsic evidence is interpretive only if it is connected to a textual hook creates a genuine limitation on the use of such evidence. And therefore the parol evidence rule exists under contextualism in all jurisdictions that embrace the textual hook requirement.

To be sure, some contextualist authorities do at least partly dispense with the parol evidence rule. For example, the U.C.C. expressly provides that the *addition* prong of the rule does not apply to the incorporation tools.[604] Furthermore, some cases

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601 *Id.* at 180–81. Earlier in the opinion, the Second Circuit also rejected an affidavit on similar grounds. The court ruled that the affidavit was irrelevant because it concerned the meaning of a different bill of lading. It did not even purport to construe the exoneration clause in the bill of lading at issue. *Id.* at 180. This is another example of a type of evidence that does not qualify for use during stage 1 of the interpretive process despite contextualism's flexible theory of language.

602 *Id.* at 167–68.

603 *See, e.g.*, FPI Dev., Inc. v. Nakashima, 282 Cal. Rptr. 508, 518, 522 (Cal. Ct. App. 1991) (party offered extrinsic evidence to support its assertion that its obligation to pay on a note was subject to an oral condition, not to construe any language in the note); Brawthen v. H & R Block, Inc., 104 Cal. Rptr. 486, 490 (Cal. Ct. App. 1972) (party submitted extrinsic evidence to support the existence of a side term providing that he could be terminated only for cause, not for purposes of interpreting a contractual provision stating that the company could fire him on 90 days written notice); *see also* Corbin, *supra* note 570, at 173–82 (collecting authorities in which "the [extrinsic] evidence was not offered to establish an interpretation (a meaning) of the words different from the obvious one, but to produce a legal effect as if they were not there and other words were in their place").

604 *See* U.C.C. § 2-202(a) (permitting an integrated writing, whether partial or complete, to be "supplemented" by course of performance, course of dealing, and usage of

decided under the Code, such as *Columbia Nitrogen*, may have narrowed the scope of the *contradiction* prong as well; those decisions arguably allow for the admission of incorporation tools evidence that relates only to contradictory side terms rather than to interpretation.[605] But these points do not undercut my central claims in this section: (1) as a conceptual matter, contextualism can retain the parol evidence rule despite eliminating the ambiguity determination; and (2) many, if not most, contextualist decisions embrace a version of contextualism that does precisely that.

X. CONCLUSION

The purpose of this Article was to bring greater clarity to the principles of contract interpretation and the parol evidence rule by addressing seven issues that have confounded the caselaw and secondary literature. I believe this Article has accomplished that end. But I leave the final judgment on this matter to the reader. And even if I was successful, many aspects of contract interpretation and the parol evidence rule remain clouded in ambiguity. I hope that more of these mysteries will be resolved in future work undertaken by other scholars.

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trade); *compare id.* § 2-202(b) (barring other types of extrinsic evidence of "consistent additional terms" when the writing is "a complete and exclusive statement of the terms of the agreement").

605 *See, e.g.*, Columbia Nitrogen Corp. v. Royster Co., 451 F.2d 3, 6–11 (4th Cir. 1971) (ruling that course of dealing and trade usage evidence that express price and quantity terms in a contract were only projections rather than binding obligations should have been submitted to the jury); Am. Mach. & Tool Co. v. Strite-Anderson Mfg. Co., 353 N.W.2d 592, 596–98 (Minn. Ct. App. 1984) (admitting course of performance and usage of trade evidence that delivery dates in purchase orders were merely estimates rather than obligations). Some other U.C.C. opinions can be read as only *partly* dispensing with the application of the contradiction prong to the incorporation tools. These cases seem to allow incorporation tools evidence of a side term (i.e., non-interpretive evidence) to "qualify" but not "completely override" an express term. *Nanakuli Paving & Rock Co. v. Shell Oil Co.*, 664 F.2d 772 (9th Cir. 1981), arguably endorses this approach. In Part VII, I treated *Nanakuli* (and its progeny) as being concerned with interpretation instead of the parol evidence rule. *See supra* notes 373–397, and accompanying text. But *Nanakuli* can also be understood as a dispute over a side term providing for price protection rather than as an interpretive dispute over the meaning of "Shell's posted price." *See supra* note 384 (making the same point). And I suspect that many other decisions that follow *Nanakuli*'s qualification rule can likewise be read to concern contradictory evidence rather than interpretive evidence.

The Fox in the Henhouse: The Failure of the Video Game Industry's Self-Regulation with Regard to Loot Boxes

*Carl C. Jones**

INTRODUCTION

You are shopping for a loved one. Perhaps the holidays are approaching, or a birthday draws near, or perhaps you simply wish to show your affection by making a gift out of the blue. Your loved one enjoys video games, so you stop by your local big-box store and the clerk directs you to a glass-paneled shelf, stacked to the ceiling with games in bright neon boxes. You peruse the offerings and ask for the clerk to withdraw a few samples. You note their titles and prices and consider your loved one's tastes. A clear favorite emerges. Almost as an afterthought, you check the game's rating, noting the stark black-and-white box in the lower left-hand corner of the cover: "E10+." An appended note makes the statement a little clearer: "Everyone 10+."

You've seen these eye-catching labels before; they're on virtually every video game you can think of. Out of curiosity you flip the game over, consulting the more detailed rating guide on the back side of the box, in the lower right-hand corner. In plain black text the rating guide cites "Cartoon Violence" and "Comic Mischief" to support the ten-and-up rating. That's all well and good, you think to yourself; comic mischief never seriously hurt anyone. Then something else catches your eye, in a narrower box beneath the rating guide: "In-Game Purchases."

What on earth does that mean?

You decide you will figure that out later. You purchase the game, along with some handsome gift-wrapping. Later, at home, you resume your inquiry. The ratings guide says "ESRB," so you run a quick internet search and stumble across the

* J.D. Candidate, Expected May 2021, Chapman University Dale E. Fowler School of Law. I wish to thank Professor Kurt Eggert, Director of the Alona Cortese Elder Law Center and Professor of Law at Chapman University. Without his insights into gambling law and the philosophical questions surrounding personal autonomy, this Article would have forever remained stuck on Level One. Unlike a loot box, his door was always freely open. I also wish to thank my family for a lifetime of love and support.

Entertainment Software Ratings Board's website.[1] The organization's "About" page lays out its mission statement against an attractive backdrop depicting a city skyline at dusk: "We are the non-profit, self-regulatory body for the video game industry. Established in 1994, our primary responsibility is to help consumers – especially parents – make informed choices about the games their families play."[2] Somewhat relieved, you consult the ESRB's webpage detailing the in-game purchases label. It explains that "microtransactions" are "[s]maller in-game purchases" that "typically augment or personalize the content of a game."[3] The webpage further lists "the key types of in-game microtransactions,"[4] including a term you may not have heard before: "loot boxes."[5]

The ESRB defines loot boxes as follows:

> "Loot boxes" or "loot crates" are like locked treasure chests that contain an array of virtual items that can be used in the game once unlocked. In some games loot boxes can be earned through gameplay and/or can be purchased using either real money or in-game currency. In most cases, you can't see the items before you make the purchase.[6]

You may not remember loot boxes appearing in the games you used to play, and the fact that the contents of a loot box are generally unknown before they are purchased may trouble you. If so, you're not alone.[7]

Loot boxes and other microtransactions represent an opportunity for the video game industry (the "Industry") to monetize particular video game titles for a far longer

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1 ESRB, https://www.esrb.org/ (last visited Dec. 30, 2020) [http://perma.cc/L55P-RYM5].

2 *About ESRB*, ESRB, https://www.esrb.org/about/ (last visited Dec. 30, 2020) [http://perma.cc/PAN2-UT2G].

3 Patricia E. Vance, *What Parents Need to Know About Loot Boxes (and Other In-Game Purchases)*, ESRB (July 24, 2019), https://www.esrb.org/blog/what-parents-need-to-know-about-loot-boxes-and-other-in-game-purchases/ [http://perma.cc/5DBB-BBA9].

4 *Id.*

5 *Id.*

6 *Id.*

7 *See, e.g.*, Ben Johnson, *Loot Boxes Are a Lucrative Game Of Chance, But Are They Gambling?*, NPR (Oct. 10, 2019, 5:08 PM), https://www.npr.org/2019/10/10/769044790/loot-boxes-are-a-lucrative-game-of-chance-but-are-they-gambling [http://perma.cc/S8QS-4WEN]; David Zendle & Paul Cairns, *Video Game Loot Boxes are Linked to Problem Gambling: Results of a Large-Scale Survey*, PLOS ONE (Nov. 21, 2018), https://journals.plos.org/plosone/article?id=10.1371/journal.pone.0206767 [http://perma.cc/333Y-XN33]; Mattha Busby, *Loot Boxes Increasingly Common in Video Games Despite Addiction Concerns*, GUARDIAN (Nov. 22, 2019, 5:51 PM), https://www.theguardian.com/games/2019/nov/22/loot-boxes-increasingly-common-in-video-games-despite-addiction-concerns [http://perma.cc/LEQ2-9LPW]; *How My Son Went from Gamer to Compulsive Gambler*, BBC (Oct. 8, 2019), https://www.bbc.com/news/stories-49941610 [http://perma.cc/F2D9-BU2H].

post-initial-release period than previously possible.[8] Loot boxes are particularly lucrative: current estimates project that "total spending on loot boxes and skin gambling is forecast to go up to $50 billion by 2022."[9] Yet even as loot boxes promise the Industry tremendous profit,[10] players have pilloried them[11] and consumer advocates have raised concerns about their alleged predatory tactics.[12]

This Article seeks to distill the broad cultural and legal conversations about loot boxes in the United States into a coherent summary. Part I presents the history of loot boxes by examining Industry-wide changes in the monetization and development of video games over the past several decades. Part II addresses the alleged financial and psychological costs that loot boxes impose upon consumers by reviewing scientific studies and mainstream reporting on the topic. Part III evaluates the present controversy over whether loot boxes are a type of gambling, analyzing traditional gambling definitions and critiquing existing Industry arguments to the contrary. Part IV reviews existing self-regulatory measures imposed by the ESRB. Part V presents arguments for and against continued Industry self-regulation. Part VI explores possible regulatory solutions, and the identities of the entities, legislatures, or agencies best equipped to implement them.

This Article argues that loot boxes are legally equivalent to gambling. Although others have evaluated whether loot boxes run afoul of current gambling laws, and most have determined that courts are unlikely to find sufficient value in a loot box transaction,[13] this Article comes to the opposite conclusion: that existing case and statutory law is sufficient for a court to

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8 FED. TRADE COMM'N, INSIDE THE GAME: UNLOCKING THE CONSUMER ISSUES SURROUNDING LOOT BOXES, 57–59 (2019) [hereinafter INSIDE THE GAME] (transcript downloadable at https://www.ftc.gov/news-events/events-calendar/inside-game-unlocking-consumer-issues-surrounding-loot-boxes) [http://perma.cc/R5CM-3K26].

9 *Id.* at 58.

10 *See Loot Boxes & Skins Gambling to Generate a $50 Billion Industry by 2022*, JUNIPER RSCH. (Apr. 17, 2018), https://www.juniperresearch.com/press/press-releases/loot-boxes-and-skins-gambling [http://perma.cc/XRT6-HGLZ].

11 *See, e.g.*, Matthew Gault, *Gamers Can't Stop Buying the Loot Boxes They Hate*, VICE (Oct. 9, 2017, 10:42 AM), https://www.vice.com/en_us/article/8x8jq4/gamers-cant-stop-buying-the-loot-boxes-they-hate [http://perma.cc/JB5U-5JBV].

12 *See, e.g.*, INSIDE THE GAME, *supra* note 8, at 9 (remarks of Andrew Smith, Director of the FTC's Bureau of Consumer Prot.).

13 *See, e.g.*, Alexander Mann, *Pseudo-Gambling and Whaling: How Loot Boxes Prey on Vulnerable Populations and How to Curtail Future Predatory Behavior*, 15 WASH. J.L. TECH. & ARTS 200, 225 (2020) (observing that "[T]he prizes for loot boxes do not carry any market value."). *But see* Edwin Hong, *Loot Boxes: Gambling for the Next Generation*, 46 W. ST. U. L. REV. 61, 68 (2019) ("These loot boxes constitute an illegal lottery because in each case, there is a prize, distribution by random change, and consideration. Therefore, they should be regulated as a form of gambling under California law.").

conclude that loot boxes can have value. This Article engages with and critically analyzes the Industry's arguments against such a designation. Additionally, it argues that, even if loot boxes do not rise to the level of gambling as it is traditionally understood, their economic, social, and mental health costs warrant regulation nevertheless as a novel area of law.

Unlike the present literature, this Article takes a dim view of the Industry's arguments for self-regulation, concluding that external regulation is preferable to continued Industry self-regulation under the ESRB. It further argues that the Industry's failure to acknowledge the merits of gambling comparisons, coupled with its repeated reliance on tired and discredited arguments in the face of studies to the contrary, amounts to bad faith conduct. Throughout, this Article advances the legal discussion surrounding loot boxes by analyzing the transcript of a 2019 Federal Trade Commission workshop[14] where members of the Industry, academics, and consumer advocates made their latest arguments in light of the most recent research. Finally, this Article advocates for the use of individual limit-setting, in conjunction with transparent pricing and odds disclosures, as mechanisms to rein in uninformed and compulsive consumer spending on loot boxes.

I. THE HISTORY OF LOOT BOXES

Loot boxes are a relatively new innovation in the Industry.[15] Historically, video games were produced in a "developer-centric" business model, where individual games were envisioned, developed, and ultimately released as standalone titles by their developers, who "put it out there and hope[d] [it was] a hit."[16] From a business standpoint, a game's success was measured by the total number of units sold.[17] That emphasis has since shifted toward a focus on a game's "lifetime value."[18] Where games were previously static products, unchanging after being shipped[19] (much like a movie), a new "player-centric" era has begun, in which the development of "games are being driven by feedback from gameplay itself, from attention paid by publishers and developers to the chatter around these games online. And then they . . . [use] that to iterate on the game after it's already been

14 INSIDE THE GAME, *supra* note 8.

15 *See* Andrew E. Freedman, *What Are Loot Boxes? Gaming's Big Controversy Explained*, TOM'S GUIDE (Aug. 9, 2019), https://www.tomsguide.com/us/what-are-loot-boxes-microtransactions,news-26161.html [http://perma.cc/E3C9-25MH].

16 INSIDE THE GAME, *supra* note 8, at 57.

17 *Id.* at 58.

18 *Id.*

19 *See id.*

shipped."[20] In calculating a game's lifetime value, stakeholders examine "not only how much [consumers] pay to acquire the game . . . but [also] how much value is delivered over the life of the game through things like microtransactions."[21] Such profit windows "are measured in years, not months."[22]

The first commercial home video game system, the Odyssey, was marketed by Magnavox and sold in 1972.[23] Over the ensuing decades, video games have grown into "a $100 billion global industry, and nearly two-thirds of American homes have household members who play video games regularly."[24] Video games are now available across multiple "platforms," such as personal computers ("PCs"), modern video game consoles, and mobile phones.[25] Through the 1990s and into the dawn of the new century, the Industry derived most of its revenue from selling individual, self-contained products to consumers, their ultimate end-users.[26] While these products originally took the form of tangible goods, such as cartridges and discs, the advent of the Internet allowed for games to be distributed via digital downloads.[27] Even at that time, the business of buying a video game still resembled most consumer transactions for the purchase and sale of goods: consumers bought a copy of a video game outright (as one might a book or DVD), or in the case of some online games, purchased a license to play.[28] Video games were sold as complete, finished products.[29] As the Industry moved further into the new decade, "monetisation in video games underwent a significant shift," with a growing emphasis on the sale of supplemental digital products to augment the gameplay experience: microtransactions.[30] While some microtransactions made mere cosmetic changes to a game, others granted players "in-game advantages."[31] In both instances, these supplemental products were available for direct purchase for a set price.[32]

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20 *Id.* at 57–58.

21 *Id.* at 58.

22 *Id.*

23 *Video Game History*, HISTORY, https://www.history.com/topics/inventions/history-of-video-games [http://perma.cc/73P5-PM6G] (last updated June 10, 2019).

24 *Id.*

25 *Id.*

26 David Zendle et al., *The Changing Face of Desktop Video Game Monetization: An Exploration of Trends in Loot Boxes, Pay to Win, and Cosmetic Microtransactions in the Most-Played Steam Games of 2010-2019*, PSYARXIV PREPRINTS 3 (Nov. 1, 2019), https://psyarxiv.com/u35kt [http://perma.cc/TGA7-C4SD].

27 *See id.*

28 *Id.*

29 *See id.*

30 *Id.*

31 *Id.*

32 *See id.*

By 2006, however, the practice evolved, and some of the earliest loot boxes appeared in *ZT Online*, a Chinese massively-multiplayer online game ("MMO").[33] Loot boxes, unlike their direct-purchase predecessors, added "an element of randomisation" to the process of making a video game microtransaction.[34] Now, if a player wished to receive a specific virtual item and that item happened to be distributed via a loot box system, she could not simply purchase that item directly as before; she would have to open one or more loot boxes, until she received the item she desired or she gave up her search.[35]

Today, loot boxes often appear in so-called free-to-play (F2P) games, which do not charge an up-front purchase price to begin playing.[36] Industry advocates have often justified the inclusion of loot boxes and other microtransactions in such games by noting the high cost of developing a video game,[37] as well as the freedom these delayed costs afford players to try out these free-to-play games before making a financial commitment.[38] However, over the past decade, and in particular since the release of Activision Blizzard's *Overwatch* in 2016,[39] loot boxes have been increasingly adopted as an alternative revenue stream by video game developers and publishers, and have been featured in many modern-day video games across platforms and genres.[40] They have appeared in triple-A titles sold in retail and digital stores for a sticker price,[41] as well as free-to-play games available over the internet, whether accessible through personal computers or mobile devices.[42] At present, loot boxes represent a $30 billion industry, an amount projected to rise to $50 billion by 2022.[43]

Because loot boxes require players who seek a particular digital item to pay money, often without any guarantee of receiving the item they desire, critics have likened the process to gambling.[44] Some countries have since passed laws regulating loot boxes by mandating disclosure of the odds of receiving

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33 Steven T. Wright, *The Evolution of Loot Boxes*, PC GAMER (Dec. 8, 2017), https://www.pcgamer.com/the-evolution-of-loot-boxes/ [http://perma.cc/VQ89-ESDF].

34 Zendle, *supra* note 26, at 3.

35 *See id.*

36 *See* Makena Kelly, *How Loot Boxes Hooked Gamers and Left Regulators Spinning*, VERGE (Feb. 19, 2019, 8:00 AM), https://www.theverge.com/2019/2/19/18226852/loot-boxes-gaming-regulation-gambling-free-to-play [http://perma.cc/9X3H-PDBG].

37 *See id.*

38 INSIDE THE GAME, *supra* note 8, at 26 (remarks of Sean Kane).

39 Freedman, *supra* note 15.

40 *See* Kelly, *supra* note 36.

41 *Id.*

42 *See id.*

43 JUNIPER RSCH., *supra* note 10.

44 *See, e.g.*, *What Are Loot Boxes?*, PARENT ZONE, https://parentzone.org.uk/article/what-are-loot-boxes [http://perma.cc/G48K-VSJG].

specific virtual items;[45] others have banned the practice outright.[46] The United States has yet to take significant regulatory action against loot boxes,[47] and the Entertainment Software Association ("ESA," the parent entity of the ESRB[48]) has announced its opinion that loot boxes categorically do not constitute gambling.[49]

However, players,[50] consumer advocates,[51] and politicians[52] continue to voice their concerns about the practice. Academics have begun to examine the psychology driving loot box purchases; an empirical study has noted links between loot box purchases and problem gambling behavior.[53] The federal government has also begun to take note; in August of 2019, the Federal Trade Commission ("FTC") hosted a conference to hear the opinions of players, Industry associations, attorneys, consumer advocates, and academic researchers.[54] The future of regulatory action against loot boxes in the United States is far from certain, and the present status quo grants the ESRB broad self-regulatory oversight over its member entities' activities.[55] Yet calls for enhanced regulation have not abated, and the precise mechanisms for direct government oversight remain uncharted.

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45 T.J. Hafer, *The Legal Status of Loot Boxes Around the World, and What's Next in the Debate*, PC GAMER (Oct. 26, 2018), https://www.pcgamer.com/the-legal-status-of-loot-boxes-around-the-world-and-whats-next/ [http://perma.cc/ZW4J-WJ32].

46 *Gaming Loot Boxes: What Happened When Belgium Banned Them?*, BBC (Sept. 12, 2019), https://www.bbc.com/news/newsbeat-49674333 [http://perma.cc/5QZA-4UW4].

47 *See* Makena Kelly, *Game Studios Would Be Banned from Selling Loot Boxes to Minors Under New Bill*, VERGE (May 8, 2019, 12:00 PM), https://www.theverge.com/2019/5/8/18536806/game-studios-banned-loot-boxes-minors-bill-hawley-josh-blizzard-ea [http://perma.cc/9965-3YSU].

48 *Our History*, ESRB, https://www.esrb.org/history/ (last visited May 3, 2020) [http://perma.cc/JW6Q-CS2W].

49 *See* Paul Tassi, *The ESRB Is Being Willfully Obtuse About Loot Boxes, And Will Never Be Any Help*, FORBES (Feb. 28, 2018, 9:25 AM), https://www.forbes.com/sites/insertcoin/2018/02/28/the-esrb-is-being-willfully-obtuse-about-loot-boxes-and-will-never-be-any-help/#1959c0b76877 [http://perma.cc/8P5A-G47R].

50 *See, e.g.*, Will Fulton, *Do Players Really Like Loot Boxes, or are Game Publishers Forcing Them on Us?*, DIGITAL TRENDS (Nov. 16, 2017), https://www.digitaltrends.com/gaming/do-players-like-loot-boxes/ [http://perma.cc/2K26-U72V].

51 *See, e.g.*, INSIDE THE GAME, *supra* note 8, at 33 (remarks of Jeff Haynes, Senior Editor of Video Games, Common Sense Media).

52 *See, e.g.*, Chris Lee, *Highlights of the Predatory Gaming Announcement*, YOUTUBE (Nov. 21, 2017), https://www.youtube.com/watch?v=_akwfRuL4os [http://perma.cc/83QR-477F].

53 Zendle & Cairns, *supra* note 7.

54 INSIDE THE GAME, *supra* note 8, at 10–11 (remarks of Andrew Smith, Director, FTC Bureau of Consumer Protection).

55 *See ESRB Introduces New Rating Process for Console Downloadable Video Games*, ESRB (Apr. 18, 2011), https://www.esrb.org/blog/esrb-introduces-new-rating-process-for-console-downloadable-video-games/ [http://perma.cc/2NPY-DETF] (featuring ESRB President's claim that "Our rating system is widely considered to be among the most effective in the world, and ESRB continues to be an exemplary model of self-regulation.").

II. THE FINANCIAL AND PSYCHOLOGICAL COSTS OF LOOT BOXES

Ordinary consumers are bearing real psychological and financial costs as a result of the increased implementation of loot boxes.[56] Mainstream reporting on the rise of loot boxes is replete with personal vignettes from parents discovering that their young children are being enticed to spend the equivalent of hundreds or thousands of dollars on loot boxes to chase desired items.[57] However, children are not the only players affected; spouses and parents have also suffered familial strain as a result of their own compulsive spending on loot boxes.[58] Writing about his loot box spending habits, one parent wrote, "I am currently $15,800 in debt. My wife no longer trusts me. My kids, who ask me why I am playing *Final Fantasy* all the time, will never understand how I selfishly spent money I should have been using for their activities."[59] Perhaps even more sobering are the stories of young adults who were introduced to the world of online gambling through loot boxes featured in sports games.[60] Studies have noted that, on average, where non-problem gamblers spend only $2.50 on loot boxes every month, problem gamblers spend $25.[61]

As one author noted, the video game "industry is certainly no stranger to moral panics and appeals to the judicial and legislative systems."[62] It is clear that regulations should not be haphazardly foisted upon an industry based upon scattered and anecdotal reports, in particular an industry as susceptible to public outrage and demonization as the video game industry, a trend just as common today[63] as it was at the Industry's inception.[64] The revenue derived from loot boxes serves a

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56 *See, e.g.*, Mattha Busby, *'Easy Trap to Fall Into': Why Video-Game Loot Boxes Need Regulation*, GUARDIAN (May 29, 2018, 1:50 PM), https://www.theguardian.com/games/2018/may/29/gamers-politicians-regulation-video-game-loot-boxes [http://perma.cc/NP62-Z45S].

57 *See, e.g.*, Kate Jackson, *The Great Game Robbery: How Kids are Racking Up Bills Worth Thousands Buying 'Loot Boxes' on Games Like Fifa and Minecraft*, THE SUN (Oct. 22, 2019, 10:30 PM), https://www.thesun.co.uk/tech/10192098/games-bill-loot-boxes/ [http://perma.cc/F9LD-YLN5].

58 *See, e.g.*, Busby, *supra* note 56.

59 *Id.* (emphasis of game title added).

60 *See How My Son Went from Gamer to Compulsive Gambler*, *supra* note 7.

61 Aaron Drummond et al., *Loot Box Limit-Setting: A Potential Policy to Protect Video Game Users with Gambling Problems?*, 114 ADDICTION 935, 935 (2019).

62 David J. Castillo, *Unpacking the Loot Box: How Gaming's Latest Monetization System Flirts with Traditional Grambling Methods*, 59 SANTA CLARA L. REV. 165, 175 (2019).

63 *See, e.g.*, Lisette Voytko, *Trump Suggests Video Games Connected to Violence: Research Doesn't Support That*, FORBES (Aug. 5, 2019, 12:34 PM), https://www.forbes.com/sites/lisettevoytko/2019/08/05/trump-blames-video-games-for-shootings-but-research-doesnt-support-that/#7c58d92611dc [http://perma.cc/NZ8P-JSNL].

64 *See, e.g.*, Stacie Ponder, *25 Years Later, 'Disgusting' Night Trap is Incredibly*

meaningful purpose: Industry advocates have justified the inclusion of loot boxes in games by noting that they help to offset rising development costs[65] and stagnant, or even falling, video game prices.[66]

One of the strongest arguments in favor of loot box implementation is that it enables players to choose how much they wish to financially support a particular game.[67] At the 2019 FTC conference, Mike Warnecke of the ESA noted, "[W]hen people experience games, they want to be able to kick the tires on it and not . . . [buy] something until they have a chance to experience it. . . . [Y]ou have the chance to expand the content if you decide to like it."[68] Loot boxes undoubtedly allow players to vary their level of financial support for a particular game, and are not mandatory to progress in most, if not all, games that feature them.[69] Indeed, Industry advocates frequently tout players' choice and autonomy in deciding whether or not to buy loot boxes.[70]

It is undeniable that loot boxes make modern-day games profitable for publishers[71] and accessible to players who cannot—or will not—pay anything to play.[72] But one cannot ignore the impact the practice has on vulnerable individuals, who are suffering real-world financial and psychological costs associated with the increased implementation of loot boxes in modern video games. While legal and political decision-makers may ultimately decide to endorse the practice, the decision should not be made lightly or without confronting the human costs.

A *Vice* author sought out the opinions of individuals on the subject, writing:

> I opened myself to a broad spectrum of stories and experiences. The individuals I spoke to ran a wide gamut of gaming contexts and age groups. They played across multiple platforms, from mobile to PC and console. Generally, these individuals had problems with one specific game rather than a problem spread across multiple titles. I did not observe a line between cosmetic economies, such as *Overwatch*, and economies that influence progression such as *Battlefront II* and

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Tame, KOTAKU (Aug. 15, 2017, 2:30 PM), https://kotaku.com/25-years-later-disgusting-night-trap-is-incredibly-tam-1797864067 [http://perma.cc/9JGW-JTH6].

65 INSIDE THE GAME, *supra* note 8, at 25–26 (remarks of Sean Kane).

66 *Id.*

67 *Id.* at 26.

68 *Id.* at 45–46.

69 *Id.* at 46.

70 *E.g.*, *id.* at 26, 46.

71 *Id.* at 59 (remarks of John Breyault).

72 *See id.* at 26 (remarks of Sean Kane).

> *Shadow of Mordor*. The strongest common thread in all of these stories was a similar set of behaviors and impacts. The people I spoke to by-and-large described their spending on loot boxes as impulsive, shameful, and stress-inducing.[73]

This description of loot boxes cuts against the Industry's well-established narrative that players choose to purchase loot boxes as part of an informed process.[74] One Industry advocate claimed, "No one is forced to spend money in a video game that is free to play. They choose what they want to spend and when they want to spend it and how they want to spend it."[75] But those words are difficult to reconcile with those of an affected player, who has spent several hundreds of dollars on loot boxes, who wrote:

> I felt compelled to spend on loot boxes every time a limited time event started so I wouldn't miss out. . . . It warped my whole perception of the game into short periods of anxiety and stress where I had to spend money or play constantly on the hope of not missing out.[76]

The harm inflicted by compulsive loot box spending goes beyond mere embarrassment. Affected individuals have reported intense feelings of shame and self-loathing.[77] In a particularly chilling example, one correspondent in the *Vice* article confessed, "I ended up calling a suicide hotline that night. I felt distraught, pathetic, that I had just blown so much money on nothing but virtual jewels. I felt like I deserved to die for letting it get so bad and for wasting this much money."[78]

These players' experiences are anything but unique,[79] and language of compulsion and anxiety dominates first-hand player discussion of their encounters with loot boxes.[80] It may be easy to

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73 Ellen McGrody, *For Many Players, Lootboxes are a Crisis That's Already Here*, VICE (Jan. 30, 2018, 11:08 AM), https://www.vice.com/en_us/article/kznmwa/for-many-players-lootboxes-are-a-crisis-thats-already-here [http://perma.cc/UD6V-SGKA].

74 *See, e.g.*, INSIDE THE GAME, *supra* note 8, at 26.

75 *Id.*

76 McGrody, *supra* note 73.

77 *See id.*

78 *Id.*

79 *See, e.g.*, Ethan Gach, *Meet the 19-Year-Old Who Spent Over $17,000 on Microtransactions*, KOTAKU (Nov. 30, 2017, 10:00 AM), https://www.kotaku.com.au/2017/11/meet-the-19-year-old-who-spent-over-17000-on-microtransactions/ [http://perma.cc/SB94-FSPM]; Mike Wright, *Children Spending £250 on Fortnite 'Skins' to Avoid Being Labelled 'The Poor Kid' at School, Children's Commissioner Warns*, TELEGRAPH (Oct. 22, 2019, 12:01 AM), https://www.telegraph.co.uk/news/2019/10/21/children-spending-250-fortnite-skins-avoid-labeled-poor-kid/ [http://perma.cc/VYA2-6LNJ]; Zoe Kleinman, *'My Son Spent £3,160 in One Game'*, BBC (July 15, 2019), https://www.bbc.com/news/technology-48925623 [http://perma.cc/N8H3-VS9P].

80 *See, e.g.*, Alysia Judge, *Video Games and Mental Health: 'Nobody's Properly Talking'*, BBC (July 14, 2018), https://www.bbc.com/news/newsbeat-44662669 [http://perma.cc/SQ2V-6UFM].

assume that such players are the exception, and that a few individuals with problematic gambling behaviors are simply making imprudent decisions, but that claim is far from reality.[81] It has become clear in academic circles that there is a statistically-significant correlation between loot box spending and problem gambling activity.[82] Doctors David Zendle and Paul Cairns conducted a large-scale survey of video game players in order to evaluate the connection between these two behaviors.[83] The results of their research were sobering:

> This research provides empirical evidence of a relationship between loot box use and problem gambling. The relationship seen here was neither small, nor trivial. *It was stronger than previously observed relationships between problem gambling and factors like alcohol abuse, drug use, and depression.* Indeed, sub-group analyses revealed that an individual's classification as either a non problem gambler or a problem gambler accounted for 37.7% of the variance in how much they spent on loot boxes. These results may confirm the existence of the causal relationship between buying loot boxes and problem gambling . . . . Due to the formal features that loot boxes share with other forms of gambling, they may well be acting as a 'gateway' to problem gambling amongst gamers. Hence, the more gamers spend on loot boxes, the more severe their problem gambling becomes.[84]

They were quick to point out a significant caveat: "However, it is important to note that this is not the only causal relationship which fits the data. It may be the case that individuals who are already problem gamblers instead tend to spend more on loot boxes."[85] Uncertain of which way the causal arrow pointed, the authors posited:

> It may, indeed be the case that both directions of causality are true: Problem gamblers spend more on loot boxes, whilst buying loot boxes simultaneously leads to increases in problem gambling amongst gamers. However, regardless of which of these outcomes is the case, this research bears an important message when it comes to the regulation of loot boxes within the gaming industry. . . . It may be the case that this spending is leading to problem gambling. It may be that this level of spending is driven by pre-existing problem gambling amongst gamers. . . . *However, in either case, this research provides industry bodies such as the ESRB with crucial evidence to use when determining whether there is still insufficient evidence of links between problem gambling and loot box use*.[86]

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81 *See* Zendle & Cairns, *supra* note 7.
82 *Id.* at 1, 3.
83 *Id.* at 3.
84 *Id.* at 9 (emphasis added).
85 *Id.*
86 *Id.* (emphasis added).

This research illustrates a quantifiable connection between loot box spending and problem gambling behavior,[87] providing academic support for the notion that loot boxes exploit or impose real psychological harm on a very real population of consumers. Finally, the authors of the study looked beyond the legal roadblocks to implementing loot box regulations and couched the matter in human terms:

> This study shows a relationship between loot box spending and problem gambling. . . . Furthermore, we believe that the strength of the relationship that was observed here between problem gambling and loot box spending suggests that important gambling-related harm is experienced by users of loot boxes. We strongly recommend that relevant national and federal regulatory authorities consider restricting access to loot boxes as if they were a form of gambling. . . . *It is our opinion that this relationship remains serious and potentially dangerous regardless of whether loot boxes are technically considered a form of gambling or not.*[88]

While it is unclear whether loot boxes' presence in video games first exposes individuals to further gambling-related harm, or merely exploits the existing problematic gambling tendencies of a subset of players, neither result can be considered trivial. Under both models, the Industry profits off of vulnerable individuals, whether it creates that vulnerability or merely exploits it. Further, the Industry is aware of, and indeed relies upon, the revenue derived from those individuals.[89]

In writing on the topic of habit-forming design in phone applications and video games, Associate Professor Kyle Langvardt discussed the incentives developers have to maximize user "time on device," both from an advertising and a microtransactional approach.[90] He found that, while the majority of players pay little into microtransaction-heavy free-to-play games,[91] "most revenue from micropayments is highly concentrated among a small group of apparent addicts who individually spend thousands of dollars on in-app purchases."[92] Professor Langvardt further illustrated the problematic behavior of heavy spenders, indicating that "0.15 percent of mobile gamers account for 50 percent of the industry's revenue from micropayments. About 1.9 percent make up 90 percent of

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87 *Id.* at 3.

88 *Id.* at 9–10 (emphasis added).

89 *See* Kyle Langvardt, *Regulating Habit-Forming Technology*, 88 FORDHAM L. REV. 129, 140 (2019).

90 *Id.* at 134–46.

91 *Id.* at 140.

92 *Id.* (internal citations omitted).

revenue."[93] He noted that the Industry refers to such players as "whales," and recognize whales as one of their primary revenue streams in games of this kind.[94] Indeed, Professor Langvardt hypothesized that the "unbalanced" rate at which whale and non-whale players paid into certain games "may give game developers strong incentives to encourage addiction-driven, whale-like purchases."[95]

Ultimately, Professor Langvardt concluded that habit-forming design poses "at least three types of harm: addiction, strain on social norms, and degradation of public discourse."[96] He discussed the relatively small population of individuals suffering from the World Health Organization-recognized "problem gaming disorder,"[97] and likened the demographic trend to "the gambling industry, where only a small percentage of the population develops a serious habit."[98] This demonstrates that, as in the gambling industry, loot boxes can pose serious harms to individuals, even if the majority of people engaging in the activity walk away relatively unscathed.

The Industry's leadership in recognizing these harms has been sorely lacking.[99] Professor Langvardt noted that "Industry leaders in both the tech and gambling sectors emphasize the behavioral nature of the problem, and they suggest that they are not responsible for the small minority's problems with impulse control."[100] This moralizing disavowal of responsibility fails to account for the fact that, behind the scenes, the Industry relies heavily on such vulnerable individuals in monetizing its products.[101] Professor Langvardt remarked, "Developers have strong incentives to drive problem use, just as casinos do, and they make every effort to do so."[102]

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93 *Id.*

94 *Id.*

95 *Id.* at 141.

96 *Id.* at 146.

97 *Id.*

98 *Id.*; *see also* Ferris Jabr, *Can You Really be Addicted to Video Games?*, N.Y TIMES (Oct. 22, 2019), https://www.nytimes.com/2019/10/22/magazine/can-you-really-be-addicted-to-video-games.html [http://perma.cc/JLL8-FM9U].

99 Langvardt, *supra* note 89, at 146.

100 *Id.*

101 *Id.* at 140–41; *see also* PocketGamerbiz, *Let's Go Whaling: Tricks for Monetising Mobile Game Players with Free-to-Play*, YOUTUBE (Oct. 3, 2016), https://www.youtube.com/watch?v=xNjI03CGkb4&ab_channel=PocketGamerbiz [http://perma.cc/LGZ5-UERR] (depicting CEO of a developer speaking at a conference, describing his presentation, entitled "Let's go Whaling!," as follows: "It is about a summary of a huge bunch of behavioral psychology, so the tricks on how to monetize a game well. Some of you will probably be slightly shocked by all the tricks I have listed here, but I'll leave the morality of it out of the talk, we can discuss it if we have time later.").

102 Langvardt, *supra* note 89, at 147.

It is necessary to consider the words of the Industry's own representatives in defending these problematic practices. Speaking at the 2019 FTC workshop, Sean Kane, a representative of "more than 100 video game companies,"[103] attempted to normalize problem users' heavy spending as a purely volitional activity, claiming, "I don't think that we, as an industry, needs [sic] to step into that parental role, though, because some of these people are not children. . . . Some of these people are our age and they're spending $1,000 on a game that they love and this is their way of relaxing after a hard day's work."[104] It is difficult to characterize these whales' spending patterns as knowing purchases, however.

Some game mechanisms cloud just how much a player is spending on loot boxes and other microtransactions by employing in-game currencies purchased with real-world money,[105] a level of abstraction that can impede players' ability to evaluate the financial consequences of their purchases.[106] The Industry defends the practice of using in-game currencies as one that helps "to maintain a player's sense of immersion in the game."[107] In its staff perspective write-up a year after the 2019 FTC conference, the FTC recognized as one of its "key takeaways" that in-game currencies "may confuse some players, as it essentially requires a player to remember the real currency to in-game currency 'exchange rate' and calculate it for every transaction."[108]

At the same 2019 FTC conference, a panelist from the National Consumers League, John Breyault, noted the following concerning in-game currency:

> So I'd like to turn now to a specific issue that we're looking at, which is the use of in-game currency. As you've heard from the other panelists, in-game currency has proliferated throughout the top games. In *FIFA*, you've got *FIFA* coins. In *NBA 2K19*, you've got VC. In *Overwatch*, you've got credits. . . . So the currencies obtained via gameplay or purchase, our concern is that they may obscure the true cost of purchasing in-game content. So does it actually tell you how

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103 INSIDE THE GAME, *supra* note 8, at 14.

104 *Id.* at 100.

105 *Id.* at 62–63.

106 *Id.* at 66–67; *see also* Brendan Sinclair, *Is it Time to Retire Virtual Currency?*, GAMESINDUSTRY (Sept. 20, 2019), https://www.gamesindustry.biz/articles/2019-09-20-is-it-time-to-retire-virtual-currency [http://perma.cc/LAU4-LRJZ] (discussing the lubricating effect in-game currency has on players' decisions to purchase microtransactions, by reducing "friction points" and "opportunities for a consumer to consider whether they really want to spend this money").

107 FED. TRADE COMM'N, FTC VIDEO GAME LOOT BOX WORKSHOP: STAFF PERSPECTIVE 4 (2020), https://www.ftc.gov/system/files/documents/reports/staff-perspective-paper-loot-box-workshop/loot_box_workshop_staff_perspective.pdf [http://perma.cc/24CA-EUCZ].

108 *Id.*

> much you're spending in real money down the line? . . . When something's priced at $1.99, you may not think that this is $2 and be more likely to spend money on it. . . . The problem here is that when you combine this with things like these bonuses that are offered here, it puts a lot of cognitive load on the user, creating a complex exchange rate between digital money and real dollars. And it can make it easy to lose track of an object's real world value.[109]

The piecemeal nature in which microtransactions, loot boxes included, extract money from players ultimately causes players to spend more on a free to play game in total than they would have likely consented to spend in advance.[110] In order to address the difficulties surrounding in-game currencies, Section VI below advocates for limit-setting practices as one of several new regulatory mechanisms to be implemented in video games.

Because of developer incentives to drive problematic use and because of the absence of a meaningful Industry response in the face of demonstrated links between loot boxes and problem gambling behavior, it is patently unwise to defer to the Industry as a self-regulatory authority. Concerned consumers must look elsewhere for protection, namely their governments. The function of a government's police power is to protect its citizens from physical harms and perceived social evils.[111] The manner and extent to which that power is exercised is a question of policy and preference, but its existence cannot be denied.[112] There is a longstanding history in the United States of government intervention to protect individuals from predatory and harmful corporate behavior, such as in the decades-long regulatory fight with the tobacco industry.[113] As explained in Section VI below, government loot box regulation is a viable method to address the harms discussed thus far, a remedy forestalled only by misconceptions about the number and type of individuals affected by loot boxes, as well as disinterest by existing regulatory authorities. It is clear that loot boxes harm certain individuals,

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109 INSIDE THE GAME, *supra* note 8, at 62–63. (emphasis of game titles added).

110 *See* Langvardt, *supra* note 89, at 135; *see also* INSIDE THE GAME, *supra* note 8, at 94 ("I don't think that simply saying on a box that you have any in-app purchases available adequately informs your typical parent or consumer just about the level of investment that goes into trying to get people to spend more on a game or in the app."); *id.* at 180 ("It's very hard for consumers to know what they're getting, what it's going to cost.").

111 38 AM. JUR. 2D *Gambling* § 8 (2020); *see also* Randy E. Barnett, *The Proper Scope of the Police Power*, 79 NOTRE DAME L. REV. 429, 430 (2004).

112 *See* Barnett, *supra* note 111, at 430.

113 *See, e.g.*, CHRISTOPHER BANTHIN, TOBACCO CONTROL LEGAL CONSORTIUM, REGULATING TOBACCO RETAILERS: OPTIONS FOR STATE AND LOCAL GOVERNMENTS 1 (2010); *see also* Ned Sharpless & Mitch Zeller, *Achievements in Tobacco Regulation Over the Past Decade and Beyond*, FDA, https://www.fda.gov/news-events/fda-voices/achievements-tobacco-regulation-over-past-decade-and-beyond (last updated Aug. 20, 2019) [http://perma.cc/PJX2-TFFY].

both financially[114] and psychologically.[115] As constituents become better-informed of the pervasiveness and effects of loot boxes, they can press elected and regulatory officials to take action. Whether that action can take the form of enforcement under existing gambling statutes would require a court to find that loot boxes amounted to a form of gambling, discussed further below.

III. LOOT BOXES AS GAMBLING

The controversy over whether loot boxes are a form of gambling ("the gambling determination") continues to rage.[116] The Industry's advocates have been quick to rebut claims to that effect, seeking to distinguish traditional gambling activity from the experience of opening a loot box.[117] The ESRB, an entity purporting to serve as a self-regulator the video game industry, weighed in on the controversy by writing to gaming news source *Kotaku*:

> ESRB does not consider loot boxes to be gambling. . . . While there's an element of chance in these mechanics, the player is *always* guaranteed to receive in-game content (even if the player unfortunately receives something they don't want). We think of it as a similar principle to collectible card games: Sometimes you'll open a pack and get a brand new holographic card you've had your eye on for a while. But other times you'll end up with a pack of cards you already have.[118]

In evaluating whether to take steps to regulate loot boxes, states and nations have grappled with this labelling issue.[119] Countries that have concluded that loot boxes are not a form of gambling have not meaningfully regulated them.[120] Countries

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114 *See, e.g.*, McGrody, *supra* note 73.

115 *See, e.g.*, Zendle & Cairns, *supra* note 7.

116 *See, e.g.*, Andrew V. Moshirnia, *Precious and Worthless: A Comparative Perspective on Loot Boxes and Gambling*, 20 MINN. J.L. SCI & TECH. 77, 77–78 (2019) (noting that loot boxes are unlikely to be labeled gambling in the United States, and advocating instead for "transparency-based" solutions); *see also Loot Boxes Are a Lucrative Game of Chance, But Are They Gambling?*, NPR (Oct. 10, 2019, 5:08 PM), https://www.npr.org/2019/10/10/769044790/loot-boxes-are-a-lucrative-game-of-chance-but-are-they-gambling [http://perma.cc/339C-L4LR]; Hong, *supra* note 13 at 65–67 (arguing loot boxes constitute gambling under the California Penal Code, with a particular focus on protecting minors).

117 Jason Schreier, *ESRB Says It Doesn't See 'Loot Boxes' as Gambling*, KOTAKU (Oct. 11, 2017, 12:46 PM), https://kotaku.com/esrb-says-it-doesnt-see-loot-boxes-as-gambling-1819363091 [http://perma.cc/GJ65-YRFZ].

118 *Id.*

119 *See* Alex Hern & Rob Davies, *Video Game Loot Boxes Should Be Classed as Gambling, Says Commons*, GUARDIAN (Sept. 12, 2019, 1:01 PM), https://www.theguardian.com/games/2019/sep/12/video-game-loot-boxes-should-be-classed-as-gambling-says-commons [http://perma.cc/M5RY-Z9YK].

120 *See* Zoe Kleinman, *Fifa Packs and Loot Boxes 'Not Gambling' in UK*, BBC (July 22, 2019), https://www.bbc.com/news/technology-49074003 [http://perma.cc/DM5N-UK7S].

that have come to the opposite conclusion have heavily regulated or outright banned the practice.[121] As a result, the resolution of this issue one way or the other can have serious financial ramifications for the Industry.[122] While some Industry spokespeople seek to characterize the gambling comparison as misinformed,[123] it seems imprudent to take their word for it without further engaging with the issue. Considering that the governments of multiple nations have found against the ESA's position that loot boxes are not a form of gambling,[124] the controversy is a far cry from being neatly resolved.

A. Defining Gambling

Black's Law Dictionary defines gambling as "[t]he act of risking something of value, esp. money, for a chance to win a prize."[125] While state statutes differ in the precise wording of their gambling definitions, they all focus on the elements of (1) a wager of something of value for (2) a valuable prize awarded through (3) random chance.[126] Some statutes directly acknowledge that not all activities featuring prizes are gambling, such as contests of skill.[127] Regardless of the precise wording of a particular statute, all traditional gambling activity, by nature, requires a participant to risk something of value (i.e. consideration).[128] It is only after a participant risks something of value that they are eligible to win a prize.[129] However, as anyone

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121 *See* Tom Gerken, *Video Game Loot Boxes Declared Illegal Under Belgium Gambling Laws*, BBC (Apr. 26, 2018), https://www.bbc.com/news/technology-43906306 [http://perma.cc/YE7E-NBAW].

122 *See, e.g.*, Alex Hern, *Square Enix Pulls Three Games from Belgium After Loot Box Ban*, GUARDIAN (Nov. 21, 2018, 4:57 PM), https://www.theguardian.com/games/2018/nov/21/square-enix-pulls-games-mobius-final-fantasy-belgium-loot-box-ban [http://perma.cc/H5HA-SAY4]; *see also* Amrita Khalid, *Nintendo Pulls Two Mobile Games in Belgium Due to Loot Box Laws*, ENGADGET (May 21, 2019), https://www.engadget.com/2019-05-21-nintendo-pulls-two-mobile-games-in-belgium-due-to-loot-box-laws.html [http://perma.cc/2QFJ-78U5]; Paul Tassi, *EA Surrenders in Belgian FIFA Ultimate Team Loot Box Fight, Raising Potential Red Flags*, FORBES (Jan. 29, 2019, 10:23 AM), https://www.forbes.com/sites/insertcoin/2019/01/29/ea-surrenders-in-belgian-fifa-ultimate-team-loot-box-fight-raising-potential-red-flags/#2a4b366d3675 [http://perma.cc/KHX8-74L4].

123 *See, e.g.*, Tae Kim, *State Legislators Call EA's Game a 'Star Wars-Themed Online Casino' Preying on Kids, Vow Action*, CNBC (Nov. 22, 2017, 8:57 AM), https://www.cnbc.com/2017/11/22/state-legislators-call-eas-game-a-star-wars-themed-online-casino-preying-on-kids-vow-action.html [http://perma.cc/VEU2-Y8UH].

124 *See* Shabana Arif, *The Netherlands Starts Enforcing Its Loot Box Ban*, IGN (June 20, 2018, 3:07 AM), https://www.ign.com/articles/2018/06/20/the-netherlands-starts-enforcing-its-loot-box-ban [http://perma.cc/QU8E-Q2DV]; *see also* Gerken, *supra* note 121.

125 *Gambling*, BLACK'S LAW DICTIONARY (9th ed. 2009).

126 *See, e.g.*, WASH. REV. CODE § 9.46.0237 (2005).

127 *See id.*

128 38 AM. JUR. 2D *Gambling* § 2 (2020).

129 *See id.*

passingly familiar with the concept of gambling can attest, simply being eligible to win does not guarantee that result. Uncertainty is inherent in all gambling activity.[130]

However, the definition of gambling in *Black's Law Dictionary* is not sufficient on its own. In order to meaningfully discuss whether loot boxes are a form of gambling, a baseline definition must be established.[131] While many of the generalized terms employed in the dictionary definition are reflected time and again in state gambling laws, their arrangement and emphasis varies.[132] Historically, the federal government has only stepped in to regulate gambling where it meaningfully encroaches upon the realm of interstate commerce.[133] As a result, the decision whether and how to regulate gambling has largely fallen to the respective states, each of which makes its own policy determination.[134] Indeed, the ability to regulate gambling is perhaps one of the most iconic and well-settled exercises of a state's police power.[135] As such, we must look to state laws to begin to define gambling. Some states, like California, regulate gambling activity broadly.[136] In listing the forms of gambling conduct it prohibits as a misdemeanor, California law provides:

> Every person who deals, plays, or carries on, opens, or causes to be opened, or who conducts, either as owner or employee, whether for hire or not, any game of faro, monte, roulette, lansquenet, rouge et noire, rondo, tan, fan-tan, seven-and-a-half, twenty-one, hokey-pokey, or any banking or percentage game played with cards, dice, or any device, for money, checks, credit, *or other representative of value*, and every person who plays or bets at or against any of those prohibited games, is guilty of a misdemeanor, and shall be punishable by a fine not less than one hundred dollars ($100) nor more than one thousand dollars ($1,000), or by imprisonment in the county jail not exceeding six months, or by both the fine and imprisonment.[137]

Washington state defines gambling as "staking or risking something of value upon the outcome of a contest of chance or a future contingent event not under the person's control or influence, upon an agreement or understanding that the person or someone else will receive something of value in the event of a certain outcome."[138] Of particular interest is the statute's focus

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130 *See id.*
131 Castillo, *supra* note 62, at 183.
132 *See, e.g.*, Castillo, *supra* note 62, at 183–84.
133 *See* Lottery Case, 188 U.S. 321, 344 (1903).
134 38 AM. JUR. 2D *Gambling* § 8 (2020).
135 *See* 38 AM. JUR. 2D *Gambling* § 8 (2020).
136 *See* CAL. PENAL CODE § 330 et seq. (1991).
137 CAL. PENAL CODE § 330 (1991) (emphasis added).
138 WASH. REV. CODE § 9.46.0237 (2005).

on whether the result of the activity is within a purported gambler's "control or influence," and the necessary implication that activities involving results within a player's control do not constitute gambling.[139]

Other states, perhaps most famously Nevada, embrace gambling activity by permitting it statewide and reap its economic benefits as a result.[140] Under Nevada law: "'Gaming' or 'gambling' means to deal, operate, carry on, conduct, maintain or expose for play any game as defined [by state law], or to operate an inter-casino linked system."[141] Nevada further defines "Game" as "any game played with cards, dice, equipment or any mechanical, electromechanical or electronic device or machine for money, property, checks, credit *or any representative of value . . . .*"[142]

While some states may elect to enact detailed gambling laws, state statutes need not define gambling to avoid being unconstitutionally vague.[143] Perhaps as an inevitable result, states can define the term loosely to suit their needs. It is therefore necessary to view the broad constellation of state gambling definitions to determine its common elements.[144]

Based upon a review of multiple state gambling statutes, one author advanced the following working gambling definition: "any activity in which consideration is given in a game of chance in return for a prize."[145] This Article adopts the same definition for purposes of discussion and critique. Where other scholarly articles have examined loot boxes under these elements and determined that a court would be unlikely to hold their use to be gambling activity,[146] this Article comes to the opposite conclusion. As argued in detail below, players and game developers treat loot

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139 *See id.*

140 *See* NEV. REV. STAT. ANN. § 463.010 et seq. (2019) (also known as the "Nevada Gaming Control Act," in which the Nevada Legislature expressly "[found], and declare[d] to be the public policy of this state, that… the gaming industry is vitally important to the economy of the State and general welfare of the inhabitants.")

141 NEV. REV. STAT. ANN. § 463.0153 (2019).

142 NEV. REV. STAT. ANN. § 463.0152 (2020) (emphasis added).

143 38 AM. JUR. 2D *Gambling* § 1 (2019).

144 Castillo, *supra* note 62, at 183 ("[B]y examining various state statutes' definition of gambling and gambling instruments, a working definition begins to emerge.").

145 *Id.* at 184.

146 *See id.* at 192 (noting that the believed-to-be-absent element of "value" could be found by "more technically-literate court judges [who could] judge 'value' in more than just monetary terms," but concluding that as of yet, "[u]ntil such a shift in perception occurs the in-game items received from loot boxes cannot be considered value"); *see also* Mann, *supra* note 13, at 227 (concluding that "current case law and statutory definitions are inadequate to classify loot boxes as gambling outright"); Moshirnia, *supra* note 116, at 99 ("Nor would loot boxes qualify as gambling if one considers the virtual items to be worthless.").

box contents as things of value; in many games, those contents are often resold for value in player-to-player transactions with the direct sanction of the developer. This Article further argues that the money players pay in order to purchase loot boxes constitutes valuable consideration. The gambling determination, therefore, turns largely upon whether a loot box contains an item of independent value, received at random, for which the purchaser pays consideration.[147]

As authors have noted,[148] and as the ESRB conceded in its own statement on the subject,[149] the element of "chance" is clearly present in opening a loot box, and as such this Article will not further discuss it. Instead, it will engage with the stronger argument against the presence of the element of a valuable prize and, to a lesser extent, consideration.

B. Valuable Prize

In order to evaluate whether a loot box's contents have independent value, we must consider the reasons why players buy loot boxes in the first place. Are they seeking one or more specific advertised items, and all other results are disappointments? Or are they paying for a virtual lightshow, unconcerned with the specific contents of their loot box? Industry representatives frequently contend that loot boxes are not a form of gambling because a loot box always gives the player something.[150] From the perspective of such advocates, the "value" derived from a loot box transaction is the guaranteed receipt of any one or more items inside the loot box.[151] But this interpretation assumes and disregards much. Certainly, a player who receives a free loot box as part of an in-game promotion might open it out of idle curiosity, or a desire to receive something, anything. That player cannot be disappointed, because a loot box will always give him something, whether it be a "skin" (a recolor or texture swap for an existing in-game asset, with no practical gameplay effects), in-game currency, a consumable item, or any number of other possible in-game effects[152] (hereinafter referred to as "items"). But such a player has not purchased his loot box.

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147 *See* Castillo, *supra* note 62, at 183.

148 *Id.* at 187–88.

149 Schreier, *supra* note 117.

150 *Id.*

151 *See id.*

152 *See* Vance, *supra* note 3 (providing ESRB definition which states loot boxes "are like locked treasure chests that contain an array of virtual items that can be used in the game once unlocked.").

Players who purchase loot boxes are making a decision, consciously or not, to enter into a monetary transaction.[153] It is clear that such paying players desire something from their purchased loot boxes. The issue then becomes whether a paying player is purchasing loot boxes for the experience of opening the loot box,[154] or to seek one or more specific items.[155] If one player—let's call him Jace—is simply purchasing the experience, a talking point adopted by some Industry advocates,[156] then he has received a guaranteed thing of value for his purchase. Jace opened his loot box and got an item. He got what he paid for. Ergo, the Industry proclaims, not gambling.[157]

This interpretation is flawed. To illustrate: a one-dollar slot machine that always paid out at least one penny would still amount to gambling activity—the "guaranteed" receipt of a nominal prize would not invalidate the larger game being played. Further, while Jace might be finding value in the chase itself (rather than any particular prize), this makes the practice *more* akin to gambling, not less.[158]

But what of the other player—let's call her Liliana—who has no interest in most of the possible items in the loot box, and sees them simply as chaff through which she must sift to unearth the solitary gem that she desires? Depending on the manner in which that particular video game is monetized, Liliana may not have the option[159] to purchase the item directly from the loot box. In

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153 *See* Imran Khan, *Loot Box Bill Officially Introduced to Senate*, GAMEINFORMER (May 23, 2019, 1:05 PM), https://www.gameinformer.com/2019/05/23/loot-box-bill-officially-introduced-to-us-senate [http://perma.cc/VMK9-QD6Z] (quoting text of unnumbered bill in U.S. Senate that defines "loot box" in pertinent part as "an add-on transaction to an interactive digital entertainment product").

154 *See* INSIDE THE GAME, *supra* note 8, at 127–28 (remarks of Dr. Andrey Simonov).

155 *See id.* at 9 ("There have been anecdotal reports of consumers spending hundreds to thousands of dollars in pursuit of coveted items. . . . In addition, do consumers, especially children or adolescents, adequately understand what they're purchasing and how much time or money they're spending? Are the disclosures adequate? For example, disclosures about the odds of obtaining specific loot box items, especially if those odds may change depending on game behavior.").

156 *See id.* at 116–17, 121–30.

157 *See* Moshirnia, *supra* note 116, at 98–99.

158 *See* INSIDE THE GAME, *supra* note 8, at 127 ("[M]aybe consumers just play loot boxes because they get some utility from a risk. . . . And this is really problematic because this is the same as [in] casinos, and it can lead to problem gambling, to addiction, and to all stories like this.").

159 It is worth noting that a prominent video game featuring loot boxes, Activision-Blizzard's *Overwatch*, adopts a hybrid model. Under this model, players receive free loot boxes periodically for playing games and logging in, while also having the opportunity to buy as many loot boxes as they wish through the in-game store. Any item in a loot box is also available for purchase using the in-game currency known as "credits." Credits cannot be purchased directly and instead must be acquired by opening loot boxes, which pay them out in lots of 50, 150, 200, and 500 according to the rarity of the bundle of credits contained in a particular loot box. Duplicate items received from loot boxes award a

that case, she must roll up her sleeves and begin to open loot boxes, one by one, until she finds what she is looking for or abandons her search out of frustration or economic necessity. Liliana would have paid out real money for the mere chance to receive what she desired. Even if she is ultimately successful, her success could have come after opening one loot box or one hundred. The solitary item she desired could have cost her wildly different amounts of money. Initial research suggests that most loot box purchasers adopt this approach, and "open loot boxes mainly for functional value . . . ."[160]

One might consider the above distinction to be largely philosophical. What do players personally value? Why should the Industry be regulated in dealing with Liliana if they would be free to deal with Jace? Indeed, Industry advocates have often emphasized players' decision to purchase loot boxes as an act of self-expression,[161] noting that often loot box contents are entirely cosmetic and confer no gameplay advantages.[162] These arguments tend to frame the discussion around loot boxes in terms of player agency and expression.[163] The ESA laid out its position as follows:

> Loot boxes are a voluntary feature in certain video games that provide players with another way to obtain virtual items that can be used to enhance their in-game experiences. They are not gambling. . . . In some games, they have elements that help a player progress through the video game. In others, they are optional features and are not required to progress or succeed in the game. In both cases, the gamer makes the decision.[164]

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prorated amount of credits as well. A "Rare" skin (featuring a simple color palette swap of that character's original model) for a particular character costs 250 credits to be directly unlocked, while a new "Legendary" skin for that character (incorporating new visual and audio effects and a more radically altered character model) will cost 3,000 credits. A player could either choose to open their free loot boxes (augmenting them with paid loot boxes as desired) until they got the skin they wanted, or they could use their credits to purchase the skin directly. The purpose of this footnote is to illustrate that, even though players can unlock skins "directly" in *Overwatch*, the currency to do so must be accrued by opening loot boxes. A player attempting to acquire a limited-time skin may not have enough time to purchase that skin directly with their available credits, and will instead need to purchase multiple loot boxes to either find the skin by chance or accrue enough credits to unlock it manually. *See, e.g.*, Daniel Friedman, *Want Overwatch to Get Rid of Loot Boxes? It Might Get More Expensive*, POLYGON (Sep. 5, 2018, 2:00 PM), *http://www.polygon.com/2018/9/5/17822966/overwatch-loot-boxes-skins-events* [http://perma.cc/EW2X-ZAH5] (discussing *Overwatch*'s in-game economy).

160 *See* INSIDE THE GAME, *supra* note 8, at 130.

161 *Id.* at 22 (remarks of Sean Kane).

162 *Id.* at 30–31.

163 *Id.* at 22 ("[C]ustomization in games is exceedingly popular and it's something that [players] do to really interact with their friends. They love to be able to show off some sort of new element that allows their game character to more reflect their own personality.").

164 Hannah Dwan, *Hawaii to Crack Down on 'Predatory' Loot Boxes in Video Games*

In evaluating the ESA's above defense of the practice, Professor Andrew V. Moshirnia noted the wrongheadedness of discussing free will and choice in arguing whether a practice amounts to gambling.[165] Professor Moshirnia wrote:

> Unsurprisingly, the Entertainment Software Association (ESA), a trade association, has strongly opposed any suggestion that loot boxes are a form of gambling. ESA has wrongly made this argument based on the voluntary nature of the activity, rather than the relative value of resulting items. . . . The ESA's approach is odd as gambling definitions do not typically revolve around volition—it is assumed that bets do not place themselves and that a viewer can watch a race without placing a wager.[166]

Further, player-agency arguments disregard the economic value that players[167] and game developers[168] themselves assign to specific items in their loot boxes.

The Industry is nevertheless hesitant to characterize loot box contents as things of real-world value, and prefers to discuss them as fun add-ons.[169] This view is somewhat supported by the monetization structure of some video games, in which players cannot trade the items they receive from loot boxes—the items are permanently associated with individual accounts.[170] One might wonder how the contents of a loot box can be things of value if they cannot be shared, traded, or sold off. Under such a system, one might imagine players enter into a loot box transaction with the understanding that they are receiving nothing of value, because they cannot sell it off and will eventually stop playing that particular game.

This notion does not overcome loot boxes' similarity to traditional gambling activity for two reasons: (1) it fails to acknowledge that many things of value cannot be shared or later sold off, and (2) it also fails to take into account the many online games in which loot box contents can and are traded and resold

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Following Star Wars Battlefront 2 Controversy, TELEGRAPH (Nov. 27, 2017, 4:57 PM), http://www.telegraph.co.uk/gaming/news/hawaii-crack-predatory-loot-boxes-video-games/ [http://perma.cc/AA7W-GCEW].

165 Moshirnia, *supra* note 116, at 95–96.

166 *Id.*

167 *See, e.g.*, Joseph Knoop, *The Most Expensive CS:GO Skins of 2017*, PCGAMER (Nov. 30, 2017), http://www.pcgamer.com/csgo-skins-most-expensive [http://perma.cc/5CDU-BHRR].

168 *See, e.g.*, Maddie Level, *Unboxing the Issue: The Future of Video Game Loot Boxes in the U.S.*, KAN. L. REV. 201, 216 (2019) ("Likewise, in games where the items contained in loot boxes are categorized [by developers] by frequency and rarity, value is inherently assigned to the items.").

169 *See, e.g.*, INSIDE THE GAME, *supra* note 8, at 22.

170 *See id.* at 69–70.

for considerable sums of money with the direct support of the game developer.[171]

To the first point: individuals frequently pay money for services, such as haircuts and car washes, that cannot later be re-sold or cashed out, and the benefits of which diminish over time. That is not to say, however, that these services lack value.[172] The Industry's logic with regard to loot boxes assumes that the ability to trade something is integral to whether that thing is valuable. But the Industry's logic is faulty. It is irrelevant whether the contents of a loot box are freely tradable, as a court could find that the payment of cash for an uncertain, nontransferable prize amounts to gambling activity regardless. However, it is important to note that at least one nation, the Netherlands, has only found gambling activity to take place when the contents of those loot boxes are transferable as part of real-world transactions.[173]

To the second point: in games where players *are* allowed to trade amongst themselves, in-game items can command real-world prices. Some online marketplaces, such as Valve's Steam Community Market ("Steam"), allow players to buy and sell items from a host of affiliated games, many of which were originally exclusively obtained from a loot box mechanism.[174] Steam places an $1800 limit on any single transaction, and charges a five percent transaction fee.[175] Individual game developers determine whether they wish to enable player-to-player trading through Steam's market.[176] This serves as further evidence that many developers acknowledge in-game items to be things of value, and directly profit from selling loot boxes to players, knowing and intending for those players to in turn resell the loot boxes' contents for cash.

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171 *See* Jeremy Laukkonen, *Steam Community Market: What It Is and How to Use It*, LIFEWIRE, https://www.lifewire.com/steam-community-market-what-it-is-and-how-to-use-it-4586933 [http://perma.cc/T2GW-9FD8] (last updated Oct. 17, 2019).

172 *See* Justin Hughes, *The Philosophy of Intellectual Property*, 77 GEO. L. J. 287, 297 (1988) (providing a helpful overview of John Locke's labor theory of property, noting in pertinent part that, human "labor adds value to the goods, if in no other way than by allowing them to be enjoyed by a human being.").

173 *Loot Boxes & Netherlands Gaming Authority's Findings*, DUTCH GAMES ASS'N, http://dutchgamesassociation.nl/news/loot-boxes-netherlands-gaming-authoritys-findings [http://perma.cc/U64K-TPXM] (last visited Apr. 26, 2020).

174 *See, e.g.*, Laukkonen, *supra* note 171.

175 *Community Market FAQ*, STEAM, http://support.steampowered.com/kb_article.php?ref=6088-udxm-7214 [http://perma.cc/A5D4-3P8L] (last visited Apr. 28, 2020).

176 *Id.* ("It is up to the game developer to decide whether or not they want to participate in the Community Market.").

Evidence that players themselves assign value to these in-game items can be found in the steep prices they are often willing to pay for them. For example, players of *Counter-Strike: Global Offensive* (a first-person shooter game with military themes) trade skins for the guns they use in ordinary gameplay.[177] Some of the rarer skins, originally obtained through a loot box mechanism, have commanded staggering prices; in one extreme case, a skin called "Dragon Lore" sold for $61,000.[178]

That is not to say that players are arbitrarily finding value in particular items despite game developers' best intentions; developers themselves are well aware that certain items are more highly sought-after than others, and indeed engineer them to be as such. The manner in which they advertise these rarer items, such as releasing promotional videos highlighting particular items and emphasizing their time-limited nature,[179] suggests that developers intend players to urgently seek out these items in particular. Furthermore, developers entirely control the scarcity of a particular item by setting the percentage chance of a particular item appearing in any given loot box[180] (known colloquially as the "drop rate"[181]). These drop rates can be variable, and where variable, can lead to complicated payout structures.[182] By setting certain items to have a lower drop rate

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177 Andy Chalk, *CS:GO 'Dragon Lore' AWP Skin Sells for More than $61,000*, PCGAMER (Jan. 31, 2018), http://www.pcgamer.com/csgo-dragon-lore-awp-skin-sells-for-more-than-61000 [http://perma.cc/RNR8-VNHF].

178 *Id.*

179 *See, e.g.*, PlayOverwatch, *Overwatch Seasonal Event Lunar New Year 2020*, YOUTUBE (Jan. 16, 2020), https://www.youtube.com/watch?v=eLnET-0CI4M [http://perma.cc/PTN7-D6TQ].

180 *See* INSIDE THE GAME, *supra* note 8, at 33, 49.

181 *See id.* at 49.

182 To illustrate the complexity that can be involved in the implementation of a particular variable-rate loot box mechanic, refer to the example below.
In Nintendo's free-to-play mobile game, *Fire Emblem Heroes*, new collectible items (in this case fantasy characters to be added to a player's "barracks") are introduced into the game at regular intervals, often in sets of three or four. Those characters are advertised as being available in a particular loot box (referred to in this game as a "banner"). New characters often boast unique weapons or abilities, many of which a player can transfer to their existing characters. A player seeking to receive one or more advertised characters must spend in-game currency (purchased with real-world money) in order to receive a randomized character from the banner. The chance to receive a featured character (a "focus hero") is 3% on most banners. Players also have a separate 3% chance to receive a different, randomized character of the same level of rarity from a prior banner (a "non-focus hero"). The other 94% of the time, the player will receive a randomized character of a lower rarity from throughout the game's history. *Fire Emblem Heroes* tracks whether or not a player has received a high-rarity character, and gradually improves the rate at which the rarest characters are available (referred to colloquially as the "pity rate") in increments of 0.25% for every five characters received without receiving a character of the highest rarity, resetting to 3% for both focus heroes and non-focus heroes once one or the other has been obtained. This creates an incentive for a player to continue to continue to spend as their pity rate increases and the opportunity to receive their desired prize

than other items (essentially making those items more "rare"), game developers are tacitly acknowledging that they expect some items to be more desirable or useful to their players. For these reasons, it is disingenuous to claim that monetary value is not often assigned to loot box items, or that particular items are not more highly valued than others.

One author concluded that the "prize" element would be found lacking in United States courts, based upon a two-pronged analysis.[183] In the first prong, the author relied in part on the fact that games made by Electronic Arts ("EA") and Activision-Blizzard contained terms of service that expressly forbade account trading.[184] The author discussed the case of *Kater v. Churchill Downs Incorporated*,[185] noting that an item that merely extended gameplay did not constitute sufficient value to meet the definition of gambling,[186] and further that a game company could not be held responsible for real-world trading enabled by third parties in violation of the game's terms of service.[187]

In *Kater*, a player attempted to bring a class action suit against the operators of a virtual casino, seeking recovery under a Washington state lost-gambling-funds statute, the Washington Consumer Protection Act, as well as an unjust enrichment claim against the casino.[188] Gameplay required users to purchase and spend virtual chips to extend their time in the virtual casino.[189] While the game included a feature allowing users to transfer their chips to other players, the game only allowed players to do so gratuitously.[190] Nevertheless, a secondary market existed,

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improves. Starting a "summoning session" (the term the game uses to describe the loot box mechanism through which players acquire characters) costs five "orbs," the in-game currency. The player then may choose from one of five doors, which are color-coded among four possible colors (red, green, blue, and gray) in order to indicate, broadly, what type of weapon that character uses. Players seeking a particular character will know that character's weapon color, which is advertised in advance, and can select the corresponding door. The door is then opened, and the player receives a character of the chosen weapon color. The player may then choose to continue opening the remaining four doors (for a cumulative cost of 20 orbs if all five doors are opened) or may abandon the summoning session. Three orbs can be purchased via the Google Store at any time for $1.99. Orbs are available in other quantities, up to a bundle of 143 (including 33 "bonus" orbs) for $74.99. *See* Jason Venter, *Understanding Fire Emblem Heroes: A Beginner's Guide*, POLYGON (Feb. 8, 2017, 10:30 AM), https://www.polygon.com/fire-emblem-heroes-guide/2017/2/8/14541874/rewards-base-maps-difficulty-battle-dying-summoning-ritual-teams-merge-arena-heroes-tower-quests.

183 *See* Castillo, *supra* note 62, at 189–92.

184 *Id.* at 190.

185 Kater v. Churchill Downs Inc., 2015 U.S. Dist. LEXIS 175049 (W.D. Wash. 2015).

186 Castillo, *supra* note 62, at 191.

187 *Id.*

188 *Kater*, 2015 U.S. Dist. LEXIS 175049, *1.

189 *Id.* at *2.

190 *See id.* at *3.

whereby players would trade for gameplay-extension chips, using the in-game transfer feature to finalize the transaction after a deal had been struck.[191] Prior to playing any digital games, the plaintiff accepted the terms of use on the casino's website, which expressly "state[d] that virtual chips have no monetary value and cannot be exchanged 'for cash or any other tangible value.'"[192] The plaintiff had purchased and subsequently lost over $1,000 worth of these gameplay chips prior to bringing suit.[193] The district court dismissed the complaint with prejudice, finding that because the terms of service expressly forbade transferring the gameplay-extension chips for value, the defendant "[did] not award something of value satisfying the requisite prize element, and therefore the game [was] not 'illegal gambling' under Washington law."[194] The author based his determination that loot box contents could not constitute things of value partly on this lower court ruling.[195] Ultimately, however, the appellate court reversed the lower court's decision, holding that the gameplay-extension chips were, in fact, a "thing of value," and concluding "that Big Fish Casino falls within Washington's definition of an illegal gambling game."[196] The author's argument as based upon *Kater* is therefore unconvincing.

With regard to real-world trading bans under a game's terms of service, the decision on the part of some game developers to forbid real-world trading of accounts (and therefore the items associated with them) does not necessarily eliminate the real-world monetary value of those items to the players holding them. A player with no intention of selling their account can still be enticed by an attractive advertised item into purchasing a loot box in the hopes of acquiring the item. Their inability to (lawfully) trade that item does not negate that item's value to the player, which could very well constitute a "prize" sufficient to meet most definitions of gambling. Furthermore, the author did not acknowledge the existence of authorized online marketplaces, such as Steam, where players are free to trade items with other players for real-world money and in full compliance with a game's terms of service. For these reasons, this prong of the author's analysis is not convincing.

In the second prong, the author cited the case of *Chaset v. Fleer/Skybox International*[197] to further support his

191 *Id.*

192 Kater v. Churchill Downs Inc., 886 F.3d 784, 786 (9th Cir. 2018) (appellate court ruling reversing district court opinion).

193 *Id.*

194 Kater v. Churchill Downs Inc., 2015 U.S. Dist. LEXIS 175049, *12.

195 *See* Castillo, *supra* note 62, at 192.

196 *Kater*, 886 F.3d at 788.

197 Chaset v. Fleer/Skybox Int'l, 300 F.3d 1083 (9th Cir. 2002).

view that U.S. courts would fail to find prize value in a loot box's contents.[198] *Chaset* concerned a Racketeer Influenced and Corrupt Organizations Act ("RICO") suit by "purchasers of [physical] trading cards" against the manufacturers of those cards, who distributed them at random in manufacturer-sealed booster packs.[199] At issue was the disappointment consumers felt in failing to obtain desirable "chase" cards, and whether that disappointment rose to the level of an injury to property.[200] The Ninth Circuit in *Chaset* dismissed the case for lack of standing, noting that the plaintiffs lacked an injury to property.[201] In pertinent part, the Ninth Circuit wrote:

> At the time the plaintiffs purchased the package of cards, which is the time the value of the package should be determined, they received value—eight or ten cards, one of which might be an insert card—for what they paid as a purchase price. Their disappointment upon not finding an insert card in the package is not an injury to property.[202]

In coming to this conclusion, the Ninth Circuit appears to indicate not that the contents of a pack of cards themselves are worthless, but rather that they have a set value as a sealed pack, calculated at the time of purchase and not when its contents are discovered.[203]

Industry advocates have trotted out the comparison to physical trading cards often in defense of loot box practices.[204] The argument is clear: if trading card packs under *Chaset* have a value as a pack with a certain number of cards inside, and nothing more, then loot boxes, which have a value as a loot box with a certain number of items inside, likely have no further value. A consumer's expectations are not subverted when they open the loot box and fail to find the item they desired, or so the argument might go. But this argument fails to distinguish physical trading cards under *Chaset* from the contents of loot boxes, which differ in significant respects.

For one, the cause of action in *Chaset* was a RICO claim,[205] not an attempt to label trading cards as a form of gambling. The

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198 Castillo, *supra* note 62, at 189.

199 *Chaset*, 300 F.3d at 1085.

200 *Id.* at 1087.

201 *Id.* at 1087–88.

202 *Id.* at 1087.

203 *See id.*

204 *See, e.g.*, INSIDE THE GAME, *supra* note 8, at 42 (ESA representative Mike Warnecke claiming, "For 75 years or more, Americans have been opening up millions of packages of baseball cards to put together their dream team, to get the players that they root for on their home teams, and to build their collections with their friends. It's a common mechanic that people are very familiar with.").

205 Chaset v. Fleer/Skybox Int'l, 300 F.3d 1083, 1085 (9th Cir. 2002).

requirement of an injury to property is an element of a RICO claim,[206] not of a traditional gambling definition. Further, the trading card comparison is inapposite because it fails to take into account the velocity with which consumers can participate in loot box transactions.[207] At the 2019 FTC conference, Professor Adam Elmachtoub explained in response to a question about the trading card comparison:

> [O]ne thing though it's important to recognize, is there's no friction costs for buying loot boxes. There's a huge friction cost for buying a physical item. . . . So when you buy something—even if you buy it from Amazon, you still have to wait to receive it. And by that point, your thrill may have disappeared a little bit.[208]

Noted researcher Dr. David Zendle, at that same conference, responded to Professor Elmachtoub by noting:

> I remember when we were talking to the Australian Senate about this, they sort of said, what are the differences between loot boxes and trading card games in the real world. . . . [O]ne of the things that seems important is the velocity and the volume with which you can make loot box purchases. I mean, you can't go to a shop and just buy Kinder Egg, Kinder Egg, Kinder Egg, Kinder Egg, Kinder Egg, Kinder Egg, Kinder Egg, Kinder Egg, but that's what we see people do with loot boxes.[209]

The above discussion between Professor Elmachtoub and Dr. Zendle draws into sharp contrast the distinction between physical card purchases and digital loot box buys. Whereas physical purchases involve "friction costs," such as taking an item to the cash register or waiting for it to be delivered (which represent opportunities for individuals to rethink their purchase or, more significantly, subsequent purchases), loot boxes can be purchased very quickly using pre-recorded credit card information,[210] large bundles,[211] and even in the case of the Google Play Store, biometrics in the form of one-touch fingerprint purchase authorization.[212] Academics have noted that, particularly in the realm of smart phone gaming, app designers

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206 18 U.S.C.S. § 1964(c) (2000).

207 INSIDE THE GAME, *supra* note, at 159–60.

208 *Id.* at 159.

209 *Id.* at 159–60.

210 *Add, Remove, or Edit Your Payment Method*, GOOGLE PLAY HELP, https://support.google.com/googleplay/answer/4646404?co=GENIE.Platform%3DDesktop&hl=en%20 [http://perma.cc/8GVR-8B9U] (last visited Apr. 29, 2020).

211 INSIDE THE GAME, *supra* note 8, at 221.

212 Nicole Cozma, *Use Your Fingerprint to Authorize Google Play Purchases on Android 6.0 Marshmallow*, CNET (Feb. 26, 2016, 9:20 AM), https://www.cnet.com/how-to/authorize-google-play-purchases-with-your-fingerprint-on-android-marshmallowuse-your-fingerprint/ [http://perma.cc/MR9J-EGXN].

prioritize developing experiences that short-circuit individuals' ability to control their own impulses.[213]

This cuts against the possible moralistic argument that only gamblers are hurt by sharp practices in the realm of digital monetization; apps are increasingly being designed to exploit fundamental weaknesses of human psychology.[214] For these reasons, it is not appropriate to claim that the purchaser of a loot box is in as strong a position to evaluate the value of what they are purchasing as is the purchaser of a physical product; the transaction far better resembles a digital game of chance than the simple purchase of a product. A finder of fact could take the next logical step and hold that loot box contents (whether transferable or not) have value.

C. Consideration

Another argument against the classification of loot boxes as a form of gambling is the purported absence of consideration in the transaction.[215] This argument is not as strong as the argument against the existence of a valuable prize, however, because loot boxes are by definition available for direct purchase using a real-life payment method.[216] *Black's Law Dictionary* defines "consideration" as "[s]omething (such as an act, a forbearance, or a return promise) bargained for and received by a promisor from a promise; that which motivates a person to do something, esp. to engage in a legal act."[217] Consideration is an essential element in all contracts.[218]

As Industry advocates themselves are quick to point out, players are not required to buy loot boxes to play games.[219] As such, any money a player pays in exchange for a loot box is consideration for a single transaction, separate from the purchase price of the game, if any.[220] For this reason, it is clear that players are paying consideration in exchange for loot boxes, regardless of the determination of whether individual items have value or whether there is chance involved.

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213 *See* Langvardt, *supra* note 89, at 141–42.

214 *Id.*

215 *See, e.g.*, Castillo, *supra* note 62, at 185–87.

216 *See, e.g.*, *Purchasing Loot Boxes*, BLIZZARD, https://us.battle.net/support/en/article/73354 (last visited Apr. 28, 2020).

217 *Consideration*, BLACK'S LAW DICTIONARY (9th ed. 2009).

218 *See, e.g.*, CAL. CIV. CODE § 1550 (West 2020) ("It is essential to the existence of a contract that there should be . . . [a] sufficient cause or consideration.").

219 INSIDE THE GAME, *supra* note 8, at 26 (statement of Sean Kane) ("No one is forced to spend money in a video game that is free to play. They choose what they want to spend and when they want to spend it and how they want to spend it.").

220 *See* Castillo, supra note 62, at 186.

One author asserted that because certain titles, such as *Overwatch* and *Star Wars Battlefront II*, made all their in-game items available "after a certain amount of time playing," a would-be plaintiff would be hard-pressed to argue that they had risked their money on a loot box.[221] This argument fails to account for games in which loot box items are only available through loot boxes, and cannot be received through commensurate in-game play. Furthermore, even if items are capable of being unlocked outside of a loot box, a player is still paying consideration when they purchase a loot box hoping to receive particular items immediately by random chance. The opportunity to earn an in-game item outside of a loot box based upon a large time investment does not diminish the cash value of the consideration a player pays in exchange for a loot box. Finally, as another author noted, "California courts have held that consideration need not be paid solely for the chance to win [in a gambling scheme]; rather, it is enough that consideration is paid for something in addition to the chance to win a prize."[222] That author reasoned that consideration's value is not diminished by the guaranteed receipt of a random item from a loot box.[223]

Another author raised an important note, reasoning that, although a tech-savvy fact-finder might accept that loot boxes meet the requisite elements of gambling, most cases would be dismissed nevertheless on the grounds that plaintiffs lack a particularized injury sufficient to constitute standing.[224] From that author's perspective, loot boxes will only be treated as gambling activity by courts when there has been "unequivocal legislation to categorize them as such."[225] However, the objective of this Article is not to claim that individual plaintiffs should be able to recover their lost consideration on a case-by-case basis (which would require those plaintiffs' cases to survive motions to dismiss for lack of standing). Rather, this section has attempted to demonstrate that loot boxes are, in every meaningful sense, a form of gambling, such that game developers should be required to prospectively comply with existing gambling regulations.[226]

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221 *Id.*

222 Hong, *supra* note 13, at 68 (citing Holmes v. Saunders, 114 Cal. App. 2d 389, 390 (1952)).

223 *Id.*

224 Level, *supra* note 168, at 225.

225 *Id.* at 224.

226 It is important to note, however, that policymakers may instead take the opposite approach and elect to offer loot boxes and other forms of "social gaming" special exemptions and protections. *See, e.g.*, Erik Gibbs, *Washington State's Big Fish Could be Off the Hook with New Gambling Bills*, CALVIN AYRE (Jan. 30, 2020), https://calvinayre.com/2020/01/30/business/washington-states-big-fish-could-be-off-the-

Even if loot boxes are ultimately held to not constitute a form of gambling, they remain susceptible to novel forms of regulation. One possible regulatory avenue could be direct FTC oversight over loot boxes and other microtransactions, even if it is settled that they do not constitute gambling.[227] Alternatively, Congress or any given state could pass sweeping limitations or outright bans to curb the practice.[228] Neither of these possible regulatory solutions require a court to hold that loot boxes constitute a form of gambling under existing law. Despite the fierce public-relations battle that is still raging over the gambling determination, its disposition is not the end of the discussion.

IV. CURRENT REGULATORY MEASURES UNDER INDUSTRY SELF-REGULATION

At present, loot boxes are entirely unregulated by any federal or state statute in the United States.[229] In evaluating the current state (or lack thereof) of loot box regulation, two authors for the *National Law Review* commented, "Several states, including Hawaii, Washington, California, and Minnesota, also introduced bills last year to regulate the use of loot boxes in games, but all failed to pass."[230] This failure was not for a lack of interest on the part of the legislators behind the respective bills; Rep. Chris Lee of the Hawaii House of Representatives publicly condemned the practice in introducing his state's ultimately doomed legislation, calling loot boxes "a trap" that has "compelled many folks to spend thousands of dollars in gaming fees online."[231] Vulnerable individuals are not the only ones falling prey to the practice; Rep. Lee himself shared his personal experience with the creeping cost of loot boxes while playing *Clash of Clans* during his downtime, stating, "At one point, I

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hook-with-new-gambling-bills/ [http://perma.cc/LSB7-TBUT] (noting that, as part of the political backlash against the appellate ruling in Washington's *Kater* case, state senators have advanced bills to protect online casinos from gambling regulations where "players are not able to cash out for real money").

227 INSIDE THE GAME, *supra* note 8, at 107 (statement of John Breyault) ("And so to ensure that the industry doesn't take advantage of gamers in its efforts to continue that profitability is an appropriate role for the FTC to take.").

228 *See, e.g.*, *Senator Hawley to Introduce Legislation Banning Manipulative Video Game Features Aimed at Children*, JOSH HAWLEY (May 8, 2019), https://www.hawley.senate.gov/senator-hawley-introduce-legislation-banning-manipulative-video-game-features-aimed-children [http://perma.cc/P2CA-ZXZ5].

229 Steven Blickensderfer & Nicholas A. Brown, *U.S. Regulation of Loot Boxes Heats Up with Announcement of New Legislation*, NAT'L L. REV. (May 9, 2019), https://www.natlawreview.com/article/us-regulation-loot-boxes-heats-announcement-new-legislation [http://perma.cc/FD6H-NGZQ] (noting, "[i]n the United States, there is no legislation currently in place to regulate this practice").

230 *Id.*

231 Lee, *supra* note 52.

started buying crystals. I ended up spending a few hundred dollars over the course of a few months."[232] He reflected that, upon realizing what had happened and deleting the app, "there was no value left. It's just money that's gone."[233]

At the federal level, Senator Margaret Hassan of New Hampshire, in responding to her constituents' concerns, corresponded directly with the president of the ESRB, Patricia Vance, asking the Industry to adopt improved loot box disclosures and to "develop best practices for developers."[234] Senator Hassan further pressed the FTC to look into the practice, questioning nominees on their stance on the dangers posed by loot boxes.[235] The August 2019 FTC conference discussed above was likely the direct result of Senator Hassan's outreach.[236]

On the legislative front, one bill introduced in 2019 would ban loot boxes in games directed primarily toward minors.[237] The practice would prohibit defined "pay-to-win microtransactions and sales of loot boxes in minor-oriented games,"[238] and would further prohibit the "publication or distribution of video games containing pay-to-win microtransactions or purchasing loot boxes where the publisher or distributor has constructive knowledge that any users are under age 18."[239] However, the bill has yet to advance, and some commentators have expressed concerns about

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232 Cecilia D'Anastasio, *Hawaii State Rep Is Drafting Bill Barring Minors from Buying Games with Loot Boxes*, KOTAKU (Dec. 8, 2017, 4:40 PM), https://kotaku.com/hawaii-state-rep-is-drafting-bill-barring-minors-from-b-1821136540 [http://perma.cc/26EC-WJWD].

233 *Id.*

234 Letter from Margaret Wood Hassan, Sen., to Patricia Vance, President of the ESRB, at 1 (Feb. 14, 2018), https://www.hassan.senate.gov/imo/media/doc/180214.ESRB.Letter.Final.pdf [http://perma.cc/G6JS-6CA4]) (regarding loot boxes).

235 Paul Tassi, *US Senator Confronts the ESRB Over Loot Box Classification and Addiction*, FORBES (Feb. 15, 2018, 9:59 AM), https://www.forbes.com/sites/insertcoin/2018/02/15/us-senator-confronts-the-esrb-over-loot-box-classification-and-addiction/#73d8316e5a97 [http://perma.cc/Y28B-PUYR] ("This week, Hassan asked four FTC nominees the question: 'That children being addicted to gaming – and activities like loot boxes that might make them more susceptible to addiction – is a problem that merits attention?'").

236 *Senator Hassan Statement on Announcement that Major Video Game Manufacturers Will Make Loot Box Odds More Transparent*, MAGGIE HASSAN (Aug. 7, 2019), https://www.hassan.senate.gov/news/press-releases/senator-hassan-statement-on-announcement-that-major-video-game-manufacturers-will-make-loot-box-odds-more-transparent [http://perma.cc/JDC7-HMDL] ("The announcement was made at a loot box workshop hosted by the Federal Trade Commission (FTC), which came in response to Senator Hassan's advocacy.").

237 *See* Protecting Children from Abusive Games Act, S. 1629, 116th Cong. §§ 1–5 (2019).

238 *Id.* § 1(a).

239 *Id.* § 1(b).

its potential overbreadth,[240] while others have mocked its chances of passage altogether.[241]

The ESRB, and by extension its parent entity the ESA, are the only entities to have enacted anything resembling loot box regulations.[242] The Industry's advocates frequently argue that sufficient controls are already in place, and that parents need only be educated about the tools the Industry has placed within their control.[243] In response to Senator Hassan's communications with the FTC, and the subsequent announcement that the FTC would be hosting an exploratory panel in August 2019, ESA president Stanley Pierre-Louis noted, "We look forward to sharing with the senator the tools and information *the industry already provides* that keeps the control of in-game spending in parents' hands. . . . Parents *already have the ability* to limit or prohibit in-game purchases with easy to use parental controls."[244] Such arguments imply that no further regulation is necessary, only education.[245]

Despite purporting to engage in self-regulation, the Industry's advocates and representatives frequently disregard suggested regulatory changes by relying on their blanket assertion that loot boxes are not gambling.[246] At the 2019 FTC workshop, an audience question about whether the Industry would seek to connect affected players with resources similar to Gamblers' Anonymous was met with the following response from panelist Mike Warnecke of the ESA: "So, no, it does not include any sort of hotline for that. ESA's position is that loot boxes are not a form of gambling and that it wouldn't be an appropriate solution to that issue."[247]

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240 Owen S. Good, *Anti-Loot Box Bill Poses a Real Threat to Sports Video Games*, POLYGON (June 1, 2019, 7:32 PM), https://www.polygon.com/2019/6/1/18648907/anti-loot-box-law-congress-josh-hawley-senate-nba-2k-fifa-ultimate-team [http://perma.cc/6Q7Z-38NL].

241 Giancarlo Valdes, *'Zero' Chance It Passes: Game Analysts Break Down Senator's Anti-Loot Box Bill*, VENTUREBEAT (May 13, 2019, 11:35 AM), https://venturebeat.com/2019/05/13/zero-chance-it-passes-game-analysts-break-down-senators-anti-loot-box-bill/ [http://perma.cc/N5TX-HQQS] (One securities analyst lambasted the bill, arguing, "Congress simply cannot legislate against pay-to-win, where a game is competitive and people purchase better weapons, gear, etc. . . . That's like legislating against faster cars, nicer handbags, whatever. Too dumb to comment on.").

242 *See, e.g.*, *Parental Controls*, ESRB, https://www.esrb.org/tools-for-parents/parental-controls/ [http://perma.cc/JG27-9VS5] (last visited Apr. 30, 2020).

243 *See, e.g.*, Kelly, *supra* note 47.

244 *Id.* (emphasis added).

245 *See* INSIDE THE GAME, *supra* note 8, at 176–77 (reflecting ESRB President Patricia Vance's statement at the 2019 FTC workshop, "We want to make sure that parents know that when they see that in-game purchase notice . . . if they want to limit their child's ability to spend money, they know how to do it.").

246 *See, e.g.*, *id.* at 74–75 (statement by Renee Gittins).

247 *Id.* at 101.

It was not until the FTC workshop was underway that the ESRB announced that it would seek to compel its member entities to disclose loot box drop rates to players.[248] Although the ESRB did not impose a detailed timetable for compliance,[249] multiple panelists in attendance touted the measure as a significant act of self-regulation.[250] However, commentators have noted that heralding the measure as an act of self-regulation is somewhat disingenuous,[251] as the measure was announced only after China had already enacted laws mandating such disclosure within their markets.[252] Furthermore, the exact method and specificity of odds disclosures under the mandate are unclear, with no set standard.[253] Absent a rigorous and well-defined odds disclosure scheme, players will not be meaningfully informed of the odds against them.[254] Further, even if the Industry committed to a measurable standard for disclosure, at present enforcement would be entirely managed by Industry insiders.[255] Keith S. White, executive director of the National Council on Problem Gambling, stated at the FTC workshop:

> And one of the things that we do a lot in the gambling industry, is we recognize the role of parents, we recognize the role of industry self-verification, but we absolutely believe that there has to be third-party objective regulation. Sometimes that could take the role of the—sometimes that could be the role of the FTC. . . . It's an important consumer protection feature. And so if the industry is going to provide us information on odds and randomness, take a lesson from the gambling side, you got to get it done independently. It's not going to be effective if you're just telling us, oh, trust me, this game, these items

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248 *Id.* at 100–01 (statement by Michael Warnecke).

249 *Video Game Industry Commitments to Further Inform Consumer Purchases*, ENT. SOFTWARE ASS'N, https://www.theesa.com/perspectives/video-game-industry-commitments-to-further-inform-consumer-purchases/ [http://perma.cc/F4B7-GL3E] ("The precise timing of this disclosure requirement is still being worked out, but the console makers are targeting 2020 for the implementation of the policy.") (last visited Apr. 30, 2020).

250 *See* INSIDE THE GAME, *supra* note 8, at 75, 106, 204.

251 Tassi, *supra* note 122.

252 *See, e.g.*, Nathan Grayson, *China Will Force Games With Loot Boxes to Disclose Odds*, KOTAKU (Dec. 8, 2016, 11:35 AM), https://kotaku.com/china-passes-law-forcing-games-with-loot-boxes-to-discl-1789828850 [http://perma.cc/YE8Q-XYHF].

253 *See Video Game Industry Commitments to Further Inform Consumer Purchases*, *supra* note 249.

254 Rebekah Valentine, *Consumer Advocates to ESRB, FTC: Loot Box Odds Disclosure is Not Enough*, GAMESINDUSTRY.BIZ (Aug. 7, 2019), https://www.gamesindustry.biz/articles/2019-08-07-consumer-advocates-to-esrb-ftc-loot-box-odds-disclosure-is-not-enough [http://perma.cc/B588-CEM6] (summarizing the ESA's commitments after the 2019 FTC workshop and arguments stressing that while they are helpful first steps, they are not sufficient on their own).

255 *See id.*

> drop at this rate, especially without any means to independently verify it.[256]

Perhaps the only concrete regulation the ESRB has promulgated in this area has been the requirement of an "In-Game Purchases" label on games featuring loot boxes, among other microtransactions.[257] However, when initially released in 2018, the label did not distinguish between loot boxes and other, less-controversial microtransactions in games, such as one-time purchases of non-randomized content.[258] The words "loot box" do not appear on any ESRB ratings packaging[259]; it is necessary to review the ESRB's website to find loot boxes listed and defined, amongst a wider list defining other types of microtransactions such as "In-Game Currency" and "Expansions."[260] Prior to early April, 2020, the "In-Game Purchases" label said nothing more.[261] Perhaps in direct response to criticisms similar to those outlined above, on April 13, 2020 the ESRB updated the In-Game Purchases label to read on relevant titles, "In-Game Purchases (Includes Random Items)."[262] The ESRB noted that this new measure was intended "[t]o provide even greater transparency about the nature of in-game items available for purchase . . . ."[263] Outlining how the new label would be implemented, the ESRB explained:

> This new Interactive Element, *In-Game Purchases (Includes Random Items)*, will be assigned to any game that contains in-game offers to purchase digital goods or premiums with real world currency (or with virtual coins or other forms of in-game currency that can be purchased with real world currency) for which the player doesn't know prior to purchase the specific digital goods or premiums they will be receiving (e.g., loot boxes, item packs, mystery awards). *In-Game Purchases (Includes Random Items)* will be assigned to all games that include purchases with any randomized elements, including loot boxes, gacha games, item or card packs, prize wheels, treasure chests, and more.[264]

The article released by the ESRB announcing this new change justified the prior exclusion of the element of

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256 INSIDE THE GAME, *supra* note 8, at 191–92.

257 Vance, *supra* note 3.

258 *ESRB To Begin Assigning "In-Game Purchases" Label to Physical Video Games*, ESRB (Feb. 27, 2018), https://www.esrb.org/blog/esrb-to-begin-assigning-in-game-purchases-label-to-physical-video-games/ [http://perma.cc/HJ3B-PDN3].

259 *See id.*

260 Vance, *supra* note 3.

261 *Introducing a New Interactive Element: In-Game Purchases (Includes Random Items)*, ESRB (Apr. 13, 2020), https://www.esrb.org/blog/in-game-purchases-includes-random-items/ [http://perma.cc/89E6-A4X5].

262 *Id.*

263 *Id.*

264 *Id.*

randomization from the label by noting, "According to research, parents are far more concerned about their child's ability to spend real money in games than the fact that those in-game purchases may be randomized."[265] The ESRB claimed that the updated label, explicitly acknowledging randomization, resulted because of outreach from "many game consumers and enthusiasts (not necessarily parents) . . . asking the ESRB to include additional information to identify games that include randomized purchases."[266] Perhaps anticipating further criticism, the ESRB directly acknowledged the lack of the term "loot box," anywhere in the revised literature.[267] It justified the exclusion by observing that "'Loot box' is a term that doesn't encompass all types of randomized in-game purchase mechanics. We want to ensure that the new label covers all transactions with randomized elements."[268] It further noted:

> Moreover, we want to avoid confusing consumers who may not be familiar with what a loot box is. Recent research shows that less than a third of parents have both heard of a loot box *and* know what it is. "Loot box" is a widely understood phrase in and around the video game industry and among dedicated gamers, but most people less familiar with games do not understand it. While this new label is primarily in response to feedback from game enthusiasts, it is still essential that all consumers, especially parents, have a clear understanding of the rating information we provide.[269]

Based on the foregoing, it appears the ESRB prioritizes cleanliness and brevity over meaningful information when crafting on-box video game ratings—further clarification risks raising uninformed consumers' concerns. The fact that the ESRB has updated the label at all suggests that it sees the need to take some nominal action to respond to increased consumer concerns about loot box implementation, despite the ESRB's refusal to directly acknowledge the practice's similarities to traditional gambling activity.

Apart from the Industry's commitment to a mercurial and future standard for loot box odds disclosure, and the (newly-updated) In-Game Purchases label, nothing further is required of game developers by the ESRB with regard to loot box implementation. If this is to be the regulatory standard of the Industry's appointed self-regulator, it is helpful to analyze the arguments for and against such self-regulation.

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265 *Id.*
266 *Id.*
267 *Id.*
268 *Id.*
269 *Id.*

V. ARGUMENTS FOR AND AGAINST INDUSTRY SELF-REGULATION

The Industry's struggle for self-regulation was hard-won. Public outrage had been building against the Industry in the early 1990s,[270] as concerned parents turned their attention from explicit music to explicit video game content.[271] In particular, a street-fighting game called *Mortal Kombat* and a Sega game entitled *Night Trap* raised concerns about the effects of violent and sexual content in these games on video game-playing minors.[272] Senators Joseph Lieberman of Connecticut and Herbert Kohl of Wisconsin brought the issue to the attention of Congress, and held contentious hearings where the publishers of these titles were forced to justify the publication of these games.[273] Senator Lieberman introduced the Video Game Rating Act of 1994, which threatened to unilaterally establish an Interactive Entertainment Rating Commission.[274] Senator Lieberman's purpose in introducing the Act was to show the government's hand and encourage the Industry to take responsibility for its own regulation instead.[275] Senator Lieberman directly warned the Industry to that effect during one such hearing, advising, "The best thing you can do, not only for this country, but for yourselves, is to self-regulate. And believe me, it's not only going to be important to our kids, it's going to be important to the ultimate credibility and success of your business."[276]

As a direct result of sustained public and political pressure, and with the sword of the Video Game Rating Act dangling overhead,[277] the ESA (then called the Interactive Digital Software Association) founded the ESRB in 1994.[278] The ESRB developed a three-part rating system, with multiple content descriptors, "after consulting a wide range of child development and academic experts, analyzing other rating systems, and

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270 Tiffany Hsu, *When Mortal Kombat Came Under Congressional Scrutiny*, N.Y. TIMES (Mar. 8, 2018), https://www.nytimes.com/2018/03/08/business/video-games-violence.html [http://perma.cc/PX5Y-674Z].

271 Charlie Hall, *A Brief History of the ESRB Rating System*, POLYGON (Mar. 3, 2018, 12:00 PM), https://www.polygon.com/2018/3/3/17068788/esrb-ratings-changes-history-loot-boxes [http://perma.cc/RC7P-UCCW].

272 Hsu, *supra* note 270.

273 *Id.*

274 Video Game Rating Act of 1994, S. 1823, 103rd Cong. §§ 1–5 (1994).

275 Gaming Historian, *The Creation of the ESRB – Gaming Historian*, YOUTUBE (Sept. 23, 2016), https://www.youtube.com/watch?v=Wv3HDVd22P8 [http://perma.cc/8LB2-QFGU].

276 *Id.*

277 *See id.*

278 *Our History*, *supra* note 48.

conducting nationwide research with parents."[279] ESRB content rating is voluntary for game developers,[280] although all major console manufacturers[281] and multiple big-box stores[282] require affiliated games to go through the rating process.

The ESRB has developed standardized ratings and enforcement guidelines for all its member entities' video games.[283] Senator Lieberman has since hailed the ratings entity, claiming, "I have long said that the ESRB ratings are the most comprehensive in the media industry. There are many age-appropriate games that are clever and entertaining. Parents should understand and use the ratings to help them decide which video games to buy for their families."[284] Authors have applauded the success of the ESRB's regulatory oversight in working to inform parents and consumers generally of the content of video games.[285]

Long having been the target of calls for "politically-opportune overregulation,"[286] the Industry is perhaps rightly fearful of the imposition of government oversight.[287] One of the strongest arguments for Industry self-regulation is that it wards off government censorship.[288] At the 2019 FTC workshop, Renee Gittins of the International Game Developers Association shared the perspectives of two of her fellow game developers, one supportive of regulation, the other opposed.[289] The opposing perspective provided, "I do not think it is the government's role to regulate. It should be the industry and consumers that do. It could be a slippery slope that could lead to game censorship since the gaming industry has and will always be an easy scapegoat."[290] Ms. Gittins emphasized the

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279 *Frequently Asked Questions*, ESRB, https://www.esrb.org/faqs/#how-was-the-rating-system-created [http://perma.cc/3SES-Z4Z3] (highlighting relevant text viewable under the "How was the rating system created?" drop-down menu) (last visited May 3, 2020).

280 *Id.* (highlighting relevant text viewable under the "Are all games required to have a rating?" drop-down menu).

281 *Id.*

282 Gaming Historian, *supra* note 275.

283 *Ratings Process*, ESRB, https://www.esrb.org/ratings/ratings-process/ [http://perma.cc/7F5T-DGTY] (last visited May 3, 2020).

284 *Senators Hillary Rodham Clinton and Joe Lieberman Join ESRB To Launch Nationwide Video Game Ratings TV PSA Campaign*, ESRB (Dec. 7, 2006), https://www.esrb.org/blog/senators-hillary-rodham-clinton-and-joe-lieberman-join-esrb-to-launch-nationwide-video-game-ratings-tv-psa-campaign/ [http://perma.cc/9369-8Q4B].

285 *See, e.g.*, Kishan Mistry, *P(l)aying to Win: Loot Boxes, Microtransaction Monetization, and a Proposal for Self-Regulation in the Video Game Industry*, 71 RUTGERS L. REV. 537, 570 (2019).

286 Moshirnia, *supra* note 116, at 113.

287 INSIDE THE GAME, *supra* note 8, at 74 (statement of Renee Gittins).

288 *See id.*

289 *Id.* at 73–74.

290 *Id.* at 74.

Industry's concerns about possible creative restrictions outside regulation could impose, adding that "game developers are worried about heavy-handed regulation hurting the game industry and their creativity."[291]

The video game industry's self-regulatory body has been favorably compared to the Motion Picture Association of America ("MPAA") with regard to its ability to preserve the First Amendment rights of the Industry.[292] The MPAA (originally the Motion Picture Producers and Distributors of America, or MPPDA) "was established in 1922 by the major Hollywood production studios in response to increasing government censorship of films, which arose in turn from a general public outcry against both indecency on the screen and various scandals involving motion-picture celebrities."[293] The Agency enabled Hollywood to censor itself and stave off mounting calls for government intervention to police morality in films.[294] The Agency's website notes, "Since that time, the MPA has served as the voice and advocate of the film and television industry around the world, advancing the business and art of storytelling, protecting the creative and artistic freedoms of storytellers, and bringing entertainment and inspiration to audiences worldwide."[295]

However, comparisons of the ESRB to the MPAA are fundamentally flawed. Loot box criticisms have everything to do with the monetization of video games; they have nothing to do with the content of video games.[296] Hypothetically, two nearly identical games could be released, with the same title, characters, plot, and gameplay. One version of the game would not feature loot boxes and would have all of its content freely available upon purchase of the full game. The other version of the game would include loot boxes, with certain in-game items and effects gated behind the mechanism. Only the second game would run afoul of the criticisms levelled against loot boxes. The creative and expressive content of a video game has nothing to do with loot box functionality; it is how that content is parceled-out and subdivided by loot boxes that raises consumer concerns. It is disingenuous to claim that the government would be regulating

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291 *Id.* at 74–75.

292 Mistry, *supra* note 285, at 569.

293 The Editors of Encyclopædia Britannica, *Motion Picture Association of America*, ENCYCLOPÆDIA BRITANNICA (Sept. 14, 2020), https://www.britannica.com/topic/Motion-Picture-Association-of-America [http://perma.cc/9LTZ-GN62].

294 *See id.*

295 *Who We Are*, MOTION PICTURE ASS'N, https://www.motionpictures.org/who-we-are/ [http://perma.cc/U97Z-MHWB] (last visited May 7, 2020).

296 *See* Mistry, *supra* note 285, at 575.

the speech or content of a video game by regulating how loot boxes are implemented; the government would only be regulating how that game was monetized.

Furthermore, the external regulation of loot boxes would not render the ESRB moot. The ESRB continues to perform its function, and it performs it well: rating the content of video games to keep consumers informed.[297] As one author pointed out, "Senator Hassan is correct in noting that further research on monetization mechanics is necessary to guide regulatory efforts. But the ESRB is not best-equipped to handle such a task. The ESRB's function is to review gaming content for such features as age-appropriateness, violence, graphic language, and nudity."[298] Based on that logic, the ESRB is arguably overstepping its authority by inserting itself into the gambling determination. The manner in which a game is monetized is simply not a creative concern, and government oversight of monetization would pose no credible danger of censorship.

However, not all who agree that the ESRB should recuse itself from the regulation of loot boxes agree as to the appropriate next step. That same author went on to argue, "Instead of expanding the ESRB's role, the industry should have a separate self-regulatory organization whose sole purpose is to investigate deceptive monetization techniques, publish guidelines, and enforce compliance."[299] But such a step would only be a half-measure; the newly-formed Industry entity would be just as susceptible to Industry influence and suffer from the same fundamental conflict of interest to which the ESRB is vulnerable.[300] Industries' self-regulation with regard to creativity, as is the case with the MPAA, helps to safeguard those industries' First Amendment rights.[301] However, allowing the Industry to be the sole arbiter of whether its monetization methods are fair, ethical, or legal is the height of folly. It is critical to note that the ESRB exists to protect the Industry from outside regulation, not to protect the public from the Industry.[302] It is the equivalent of leaving the proverbial fox to run the henhouse.

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297 *See id.*

298 *Id.* (footnotes omitted).

299 *Id.*

300 *See* Brendan Sinclair, *Why is the Grand Theft Auto CEO Also Chairman of the ESRB?*, GAMESINDUSTRY.BIZ (Mar. 18, 2015), https://www.gamesindustry.biz/articles/2015-03-18-why-is-the-grand-theft-auto-ceo-also-chairman-of-the-esrb [http://perma.cc/9YE9-DJ53] (noting that the CEO of game company Take-Two Interactive is simultaneously the chairman of the ESRB).

301 *See* Mistry, *supra* note 285, at 569.

302 *See, e.g.*, Tassi, *supra* note 49.

The Industry has consistently failed to act in good faith with regard to consumer concerns about loot boxes.[303] Indeed, the Industry's refusal to recognize the negative effects of loot boxes, even in the face of mounting evidence, amounts to bad faith conduct. *Black's Law Dictionary* defines "bad faith" as "[d]ishonesty of belief or purpose."[304] The Industry has responded to public concerns about the negative psychological effects of loot boxes with persistent skepticism[305] and condescension[306] that betrays such a dishonesty of belief. At the FTC workshop, where an International Game Developers Association ("IGDA") representative read out both a pro- and anti-regulation statement prepared by two of her peers, the pro-regulation statement provided, "Unfortunately, it seems that the industry is having trouble being ethical when there's profit to be made. If someone cannot be trusted to not exploit someone else, then we must place down a regulation to protect others."[307] While the IGDA representative repeated the anti-regulation statement "[i]n summary," she did not acknowledge her pro-regulation peer's statement beyond simply reciting it.[308] While the IGDA spokesperson is only an individual and does not speak for the Industry as a whole, her selective deafness speaks to a pattern on the part of Industry advocates, a pattern of willfully disregarding valid criticisms of the practice of using loot boxes.[309]

The ESRB's decision to add the "(Includes Random Items)" label came only after two years of sustained criticism that the original label insufficiently notified purchasers of the presence of loot boxes—even then, the ESRB minimized consumers' concerns about loot boxes specifically.[310] Further, the Industry refuses to meaningfully respond to criticism in this area, a practice perhaps best illustrated by the frequency with which its advocates refuse to engage in a discussion over loot boxes. In one instance, EA's

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303 *See, e.g.*, Patrick Kobek, *ESRB Adds New Label for Loot Boxes (It's About Time)*, THEGAMER (Apr. 14, 2020), https://www.thegamer.com/esrb-adds-new-label-loot-boxes/ [http://perma.cc/2QRV-8KVE].

304 *Bad Faith*, BLACK'S LAW DICTIONARY (9th ed. 2009).

305 *See, e.g.*, Zendle & Cairns, *supra* note 7.

306 MBMMaverick, *Seriously? I Paid 80$ to Have Vader Locked?*, REDDIT (Nov. 12, 2017, 5:36 PM), https://www.reddit.com/r/StarWarsBattlefront/comments/7cff0b/seriously_i_paid_80_to_have_vader_locked/dppum98/ [http://perma.cc/9856-NDQ6] (showing the EA's community management Reddit account's response to a player loot box complaint by claiming, "The intent is to provide players with a sense of pride and accomplishment for unlocking different heroes.").

307 INSIDE THE GAME, *supra* note 8, at 73–74 (statement of Renee Gittins).

308 *Id.* at 74.

309 *See, e.g.*, Tassi, *supra* note 49.

310 *See Introducing a New Interactive Element: In-Game Purchases (Includes Random Items)*, *supra* note 261.

Vice President of legal and government affairs claimed at a hearing of the United Kingdom's Parliament that *Star Wars Battlefront II*'s randomized purchases were not loot boxes, "but rather 'surprise mechanics.'"[311] He further claimed, despite the increased economic costs loot boxes impose on players, that players actually enjoy the experience, stating, "We do think the way that we have implemented these kinds of mechanics . . . is actually quite ethical and quite fun, quite enjoyable to people."[312]

By failing to even acknowledge loot boxes as loot boxes, or recognize their wild unpopularity amongst players,[313] members of the Industry have effectively stalled meaningful conversation on the subject. When a Reddit user complained about paying a purchase price of $80 for *Star Wars Battlefront II*, only to have Darth Vader locked behind a loot box, the EACommunityTeam account responded, "The intent is to provide players with a sense of pride and accomplishment for unlocking different heroes."[314] That comment has since gone on to be the most "downvoted" (disliked by unique users) post in Reddit's history,[315] with 667,826 downvotes at the time of writing, suggesting that players did not agree with its sentiment.[316] One struggles to see how asking players to pay additional funds to unlock portions of a game they have already purchased would instill "pride" in those players; rather, the argument leaves the impression that the speaker is not being forthright about its true purpose. These incidents illustrate that the Industry is all too willing to engage in bad faith argumentation when confronted about its monetization practices, disingenuously claiming that the feature is somehow beneficial to players.

The Industry's repeated insistence that loot boxes are not a form of gambling, even in the face of mounting evidence of its negative impact on individuals susceptible to gambling-related harm, further demonstrates the Industry's disinterest in communicating in good faith. Dr. Zendle and Dr. Cairns arguably

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311 Dustin Bailey, *EA: They're Not Loot Boxes, They're "Surprise Mechanics," and They're "Quite Ethical"*, PCGAMESN (June 20, 2019), https://www.pcgamesn.com/ea-loot-boxes [http://perma.cc/9YGR-ZH4X].

312 *Id.*

313 *See, e.g.*, Joel Hruska, *Most Gamers Hate Buying Loot Boxes, So Why Are Games Using Them?*, EXTREMETECH (Oct. 13, 2017, 1:02 PM), https://www.extremetech.com/gaming/257387-gamers-hate-buying-loot-boxes-games-using [http://perma.cc/A24G-7Z6R].

314 MBMMaverick, *supra* note 306.

315 Paige Leskin, *EA's Comment on a Reddit Thread About 'Star Wars: Battlefront 2' Set a Guinness World Record for the Most Downvoted Comment of All Time*, BUS. INSIDER (Sept. 9, 2019, 10:39 AM), https://www.businessinsider.com/reddit-world-record-downvotes-ea-star-wars-battlefront-2-2019-9 [http://perma.cc/TZ2B-CUME].

316 MBMMaverick, *supra* note 306.

put the Industry on notice in 2018, when they wrote, in reporting on a large-scale study on the links between loot box purchases and problem gambling behavior, "[i]f loot boxes are attractive to those with problem gambling behaviours, they pose a serious moral question for the games companies who profit from them."[317] They noted that the Industry did not seem to accept such a negative narrative, writing:

> However, criticism of loot boxes has been roundly rebuffed by representatives of the games industry, with the ESRB recently claiming that there was insufficient evidence to state that loot boxes had negative consequences for gamers. They instead declared that "we do not consider loot boxes to be gambling for various reasons . . . loot boxes are more comparable to baseball cards, where there is an element of surprise and you always get something."[318]

Further evidence of the Industry's bad faith in failing to publicly acknowledge the harmful effects of loot boxes can be found in its knowing reliance on revenue derived from "whales."[319] While claiming that it cannot control the behavior of a small addicted outgroup,[320] the Industry simultaneously accounts for the majority of its loot box-related profits from that same small group.[321] If the issue of loot box implementation is a "moral question" as Dr. Zendle and Dr. Cairns posited,[322] the Industry appears to have given its answer.

As discussed more fully in Section IV, the Industry has dragged its proverbial feet on each loot box regulation it has reluctantly advanced, each only in response to an outside stimulus and only after a significant delay. While entities such as the MPAA impose no additional financial burdens on consumers in performing their self-regulatory function, the same cannot be said of the ESRB, which has turned a blind eye to the negative impacts of loot boxes on players. External regulation of the Industry's monetization practices is preferable to the present total abdication of authority to the ESRB.

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317 Zendle & Cairns, *supra* note 7.

318 *Id.* (alteration in original).

319 *See* Langvardt, *supra* note 80, at 140.

320 *See id.* at 146.

321 *See id.* at 140; *see also* Aaron Drummond et al., *supra* note 61, at 935. ("Games containing loot boxes appear to receive a disproportionate amount of revenue via this mechanism from vulnerable problem gamblers, supporting ethical concerns about this monetization method. A deeper analysis of these data casts further disquiet about loot boxes, indicating that almost one-third of the highest spenders on loot boxes ($300+ per month) are moderate-risk or problem gamblers.") (internal citations omitted).

322 Zendle & Cairns, *supra* note 7.

VI. SOLUTIONS

Rather than continue to defer to the ESRB's authority or encourage the Industry to set up a separate self-regulatory entity solely tasked with regulating video game monetization practices,[323] the federal and state governments must step in to fill the void. In 1993, Senator Lieberman threw down the gauntlet and challenged the Industry to regulate itself or suffer government intervention.[324] In this critical area, the Industry has had every opportunity to meaningfully regulate itself, but has instead dragged its feet, advanced bad faith arguments, and abdicated its so-called authority. Apps are increasingly designed to circumvent individuals' psychological resistance to parting with their money,[325] and in-game currencies are obscuring the true cumulative costs of loot box purchases.[326] Action is required. Absent meaningful Industry action, it is unsurprising that consumers have turned to their governments. Whether the FTC takes regulatory action in response to the findings of its 2019 workshop, or state governments successfully pass bills of the sort advanced by Rep. Lee of Hawaii,[327] either result will likely cause a sea change in the Industry with regard to loot boxes.

A. Regulation by the Federal Trade Commission

The Federal Trade Commission seeks to promote competition and protect consumers through its regulation and enforcement mechanisms.[328] The FTC's mission statement with regard to consumer protection provides in part that it seeks to prevent "unfair" and "deceptive" business practices.[329] As illustrated in Sections III and V above, loot boxes constitute unfair and deceptive practices and are thus ripe for FTC regulation. If the moral panics of the 1990s were sufficient to galvanize public support for government censorship of video game creative content, and stir the Industry to meaningful action, then the moral justification for government intervention here is even stronger. Before, public outrage concerned only scandalous and violent video game content, neither of which were proven to have lasting effects on players.[330] Here, however, individuals are

323 Mistry, *supra* note 285, at 575.

324 *See* Gaming Historian, *supra* note 275.

325 *See* Langvardt, *supra* note 89, at 141–42.

326 *See* INSIDE THE GAME, *supra* note 8, at 62–63, 67 (statement of John Breyault); *see also* Sinclair, *supra* note 106.

327 Lee, *supra* note 52.

328 *What We Do*, FTC, http://www.ftc.gov/about-ftc/what-we-do [http://perma.cc/UQ7P-ABZT] (last visited May 7, 2020).

329 *Id.*

330 *See* Kevin Draper, *Video Games Aren't Why Shootings Happen. Politicians Still*

suffering lasting economic, social, and psychological costs as a result of loot box implementation.[331]

Initial investigatory steps have already been taken.[332] One year after the August 2019 FTC Workshop, the agency issued a "staff perspective" report.[333] The report reviewed the issues submitted to the FTC at the workshop and through public comment, distilling the key concerns of panelists and commenters to the following points: (1) mechanics that may confuse or manipulate consumers; (2) users feeling pressure to spend; (3) the impact of the practice on children; (4) the manner in which loot box odds are disclosed; (5) issues concerning in-game purchase disclosures (i.e. in-game currency confusion); and (6) concerns regarding whether developers could give popular content creators loot boxes with better odds for "promotional purposes than odds available to the general public."[334] While the FTC staff perspective report provided an overview of possible future regulatory measures, it emphasized the role of existing ESRB initiatives such as the new "Includes Random Items" label, as well as "other proposed self-regulatory measures."[335] To the extent the staff perspective discussed dissenting views critical of the ESRB, it merely included a section entitled "Mixed views on increased government regulation."[336] The section briefly touched on the idea of implementing "third-party, independent verification of loot box odds" and hoping for "greater industry transparency."[337] A significant portion of this section was devoted to reiterating the Industry's scaremongering that "poorly crafted regulation could harm the industry and inadequately protect consumers."[338] The document emphasized the importance of conducting further research in this "evolving" area, highlighting

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Blame Them., N.Y. TIMES (Aug. 5, 2019), http://www.nytimes.com/2019/08/05/sports/trump-violent-video-games-studies.html [http://perma.cc/2SWJ-AGLY].

331 *See, e.g.*, Ethan Gach, *Meet the 19-Year-Old Who Spent Over $17,000 on Microtransactions*, KOTAKU (Nov. 30, 2017, 10:00 AM), http://www.kotaku.com.au/2017/11/meet-the-19-year-old-who-spent-over-17000-on-microtransactions/ [http://perma.cc/BK7Z-RZ6S]; Mike Wright, *Children Spending £250 on Fortnite 'Skins' to Avoid Being Labelled 'The Poor Kid' at School, Children's Commissioner Warns*, TELEGRAPH (Oct. 22, 2019, 12:01 AM), http://www.telegraph.co.uk/news/2019/10/21/children-spending-250-fortnite-skins-avoid-labeled-poor-kid/ [http://perma.cc/QVJ6-GUCR]; Zoe Kleinman, *'My Son Spent £3,160 in One Game'*, BBC (July 15, 2019), http://www.bbc.com/news/technology-48925623 [http://perma.cc/D3J2-SMUF].

332 *See* FED. TRADE COMM'N, *supra* note 107, at 1.

333 *Id.*

334 *Id.* at 3–4.

335 *Id.* at 6.

336 *Id.*

337 *Id.*

338 *Id.*

the suggestions of "some panelists" who "encouraged the industry to share relevant video game data with researchers."[339] The document's conclusion, while noting the increased relevance of the loot box discussion in light of the COVID-19 pandemic and corresponding increased video game usage, made no recommendations as to how to proceed.[340] Rather, the FTC's staff stated merely that it "encourages [the] industry to continue efforts to provide clear and meaningful information to consumers about in-game loot box and related microtransactions."[341] The FTC did vanishingly little to suggest any direct action on its own part, only noting that it would "continue to monitor developments surrounding loot boxes and take appropriate steps to prevent unfair or deceptive practices."[342]

In merely reciting the criticisms of the Industry's behavior, some of which suggest the Industry harbors improper motives in pursuing this monetization method,[343] while simultaneously deferring to the Industry's present self-regulatory measures, the FTC has signaled its disinterest in stepping into the arena at the present time. For reasons discussed throughout this article, this approach is insufficient to protect consumers. It is not sufficient to allow the Industry to continue to profit through these practices when the FTC has acknowledged the problematic nature of loot box odds disclosures and in-game currencies at present. A tepid commitment to mandate some form of permanent disclosure schedule, written by the Industry itself, at some point in the future does nothing to protect consumers today, and little to protect them tomorrow. Because of the FTC's deference toward the Industry at this point in time, consumers should look elsewhere for protection.

B. Regulation by State Governments

Individual state regulations may be best suited to rein in the Industry. While a single regulatory body is vulnerable to regulatory capture,[344] a robust and varied patchwork of state laws would require the Industry to meaningfully respond or else cease to operate in each jurisdiction entirely. While the Industry has

339 *Id.*

340 *Id.* at 7.

341 *Id.*

342 *Id.*

343 *See, e.g.*, INSIDE THE GAME, *supra* note 8, at 102 (statement of Omeed Dariani) ("I've definitely been in a room where a publisher said we could do better odds on the packs that this person opens for promotional purposes.").

344 *See* Tejvan Pettinger, *Regulatory Capture*, ECONOMICS HELP (May 24, 2018), http://www.economicshelp.org/blog/141040/economics/regulatory-capture/ [http://perma.cc/8UUW-UQF5].

previously pulled entire games out of countries such as Belgium in response to those countries' consumer protection laws,[345] such action would likely not be economically viable for the Industry if such a large global economy as California enacted meaningful loot box regulations. For a prime example of a state's power to compel better behavior on the part of its corporate citizens, look no further than the California Appellate Court's position that gig economy ride-share companies must treat their drivers as employees, rather than as independent contractors.[346] Even where companies threaten to pull out of a state entirely,[347] such a result nevertheless vindicates the right of the state to define what practices it will and will not accept within its borders.

Regulation of loot boxes should be no different. States can, in response to the popular will of their residents, begin to restrict the practice of operating a loot box scheme by passing meaningful regulations on a state-by-state basis. States may define which loot box practices they will accept, and which they will not.[348]

State regulation would also be more effective at striking the correct balance between the interests of consumers and the Industry, because each state can experiment with varying types and degrees of regulatory control over loot boxes. Rather than face a nationwide ban or potentially overbroad and burdensome federal regulation, the Industry would instead be subjected to individual states' efforts to formulate the "best" form of regulation. The Supreme Court has "long recognized the role of the States as laboratories for devising solutions to difficult legal problems."[349]

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345 Hern, *supra* note 122.

346 *See* People v. Uber Techs., Inc., 56 Cal. App. 5th 266, 312 (2020) ("The trial court found that rectifying the various forms of irreparable harm shown by the People more strongly serves the public interest than protecting Uber, Lyft, their shareholders, and all of those who have come to rely on the advantages of online ride-sharing delivered by a business model that does not provide employment benefits to drivers. . . . Accordingly, we conclude that the trial court correctly applied the law . . . ."). Although the subsequent passage of Prop 22 in California's 2020 general election foiled the implementation of the rideshare driver employee classification, the California Supreme Court refused the rideshare industry's request to depublish this opinion. People v. Uber Technologies, Inc., 2021 Cal. LEXIS 913 (2021).

347 *See* Dara Kerr, *Uber CEO: We're Looking at All Our Options if Prop 22 Doesn't Pass*, CNET (Oct. 20, 2020, 10:03 AM), http://www.cnet.com/news/uber-ceo-were-looking-at-all-our-options-if-prop-22-doesnt-pass/ [http://perma.cc/9LKU-8U3W].

348 *See* Fla. Lime & Avocado Growers, Inc. v. Paul, 373 U.S. 132, 146–47 (1963) ("The settled mandate governing this inquiry, in deference to the fact that a state regulation of this kind is an exercise of the 'historic police powers of the States,' is not to decree such a federal displacement 'unless that was the clear and manifest purpose of Congress.' In other words, we are not to conclude that Congress legislated the ouster of this California statute by the marketing orders in the absence of an unambiguous congressional mandate to that effect." (citations omitted)).

349 Oregon v. Ice, 555 U.S. 160, 171 (2009).

Leaving regulation of loot boxes to the states would serve that purpose well.

For example, as the 2019 FTC conference demonstrated, there is not yet a consensus as to how best to define and police loot box odds disclosures, or the precise risks they pose.[350] As a result, each state's legislature could decide how best to define the manner of disclosure it would require, and how those odds would be verified. Different standards could emerge, and the merits of each could be directly compared. Each state's efforts would better inform the others, and over time a reasonable and comprehensive regulatory system would emerge. When new and uncertain areas of the law emerge and the best solution is unclear, consumers are well-served by leaving regulation to the states.[351]

As a practical matter, interested consumers may have an easier time petitioning their respective states for some form of regulatory oversight, since they do not need to receive the consent of legislators from the other states, as would be required if a federal statute was to be passed. For the reasons asserted above, the best method of achieving meaningful regulation of the Industry would be through state-by-state regulation.

C. Suggested Forms of Regulation

Whether the federal or state governments take the regulatory lead, regulators should consider government-set odds-disclosure requirements and limit-setting.

1. Odds Disclosures

As discussed in Section IV, the Industry touted its commitment to mandate loot box odds disclosures by the end of 2020.[352] But the exact Industry standards for odds disclosure remain mercurial, and are unlikely to meaningfully advise consumers.[353] Additional problems arise when considering dynamic odds loot boxes, where the odds of receiving the item varies, because it greatly complicates the ability to determine

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350 *See, e.g.*, INSIDE THE GAME, *supra* note 8, at 66, 205, 209 (statements of John Breyault, Ariel Fox Johnson, and Keith Whyte).

351 *See* United States v. Lopez, 514 U.S. 549, 581 (1995) (Kennedy, J., concurring) ("While it is doubtful that any State, or indeed any reasonable person, would argue that it is wise policy to allow students to carry guns on school premises, considerable disagreement exists about how best to accomplish that goal. In this circumstance, the theory and utility of our federalism are revealed, for the States may perform their role as laboratories for experimentation to devise various solutions where the best solution is far from clear.").

352 *Video Game Industry Commitments to Further Inform Consumer Purchases*, *supra* note 249.

353 *See* Valentine, *supra* note 254.

whether the Industry is adhering to its published odds.[354] Even when the ESRB imposes mandatory odds-disclosure requirements on all its members, no two games are likely to use the same loot box system, which will make use of a centralized and easy-to-understand odds disclosure schedule difficult. Further, the Industry has a vested interest in only complying with these disclosure requirements at the bare minimum, in the most obtuse possible way.[355] In short, two problems are currently posed by the self-regulation initiative as it concerns odds disclosures: (1) it does not reasonably assure consumers that they will be meaningfully informed of the odds against them; and (2) it leaves the Industry to police its own adherence to its standards, with no mechanism for consumer or government oversight.

Government intervention would resolve both issues. A government-set odds disclosure schedule could provide uniformity across different games and mandate transparency, rather than leaving each developer to live up to the ESRB's odds disclosure commitment on a case-by-case basis. As demonstrated in gambling regulation, "self-regulation alone is never enough. It must have an enforceable consumer protection framework and be accompanied by external oversight, research, monitoring, and verification by independent groups."[356] So too would meaningful loot box regulation rely upon external verification of the Industry's compliance. Whereas a dissatisfied consumer currently has little power to review the fairness of the behind-the-scenes operations of her favorite mobile game, regulatory officials would be empowered to do so.

Further, a standardized method of odds disclosures would prevent the Industry from developing novel and confusing payout structures intended only to further obscure players' chances. If all games had to comply with a certain pre-set form of odds-disclosure, new loot boxes could not be developed that would employ inherently confusing probabilities for their own sake. Rather than try to cloud the odds, developers could cultivate player engagement with them by openly and ethically drawing their attention to them. As suggested by Mr. Whyte at the FTC workshop: "[L]et's find a way to make this information in disclosures entertaining and interactive and exciting.

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354 *See* INSIDE THE GAME, *supra* note 8, at 163 (statement of Adam Elmachtoub) ("So I think that with regard to dynamic odds, I think that would be a nightmare to regulate. Because as the odds are changing, you can never, with like just a couple samples, see if you're truly adhering to such odds.").

355 *See id.* at 190 (statement of Keith Whyte) ("I would hate to see [odds disclosure tables] look like what a pay table looks like for a slot machine, which is you know 2.5, zillions of numbers in there, and without a degree in higher math, you're utterly unable to understand this.").

356 *Id.* at 196.

You know, build it into gameplay. Reward players for doing some pro-social behavior, like finding out what really the odds are in this game."[357] The Industry has the ability to better inform its players, and from a financial perspective, has no incentive to do so currently. Government-set and monitored odds-disclosures would remove the tension between ethical and economic considerations in this area.

2. Limit-Setting

Another practice that could assist users in making informed purchase decisions is the requirement of pre-commitment limit-setting.[358] Dr. Aaron Drummond wrote to the journal *Addiction* on the topic of loot boxes in a letter to the editor, in which he provided a brief overview of the controversy and expressed his concerns about the practice's similarities to gambling activity.[359] He cited Dr. Zendle and Dr. Cairns's study, which indicated that problem gamblers spent approximately $25 USD per month on loot boxes, compared to non-problem gamblers, who spent approximately $2.50 USD in the same time period.[360] Noting the parallels between loot box spending and problem gambling behavior, Dr. Drummond advanced pre-commitment limit-setting as a possible solution, one he described as a "largely overlooked regulatory control."[361] Dr. Drummond detailed the limit-setting process as follows:

> In electronic gambling, pre-commitment limit-setting involves users specifying (voluntarily or compulsorily), before engaging in gambling, the maximum they would like to spend. Once reached, this limit triggers a reminder message and a cooling-off period in which the player is unable to gamble further. Limit setting is broadly effective at reducing over-expenditure, and generally viewed positively by gamblers. Our reanalysis suggests a clear need for limit-setting mechanisms on loot boxes, because a substantial proportion (30%) of the highest spenders are moderate-high-risk gamblers. Further increasing the probable utility of limit-setting in this context, unlike traditional gambling platforms gamers cannot bypass the limit-setting restriction simply by switching to a different game—rewards are game-specific.[362]

Dr. Drummond suggested a price point of $50 USD per month as a recommended limit-setting threshold, noting that beyond that point "the proportion of risky gamblers rises substantially . . . , implying that this may be a functional spending cap to minimize over-

357 *Id.* at 190.
358 *See* Aaron Drummond et al., *supra* note 61, at 935.
359 *Id.*
360 *Id.*
361 *Id.*
362 *Id.*

spending by at-risk populations."[363] He also discussed the option of absolute limits on loot box spending as an alternative explored by other researchers.[364] Directly calling upon regulators, Dr. Drummond concluded, "Policymakers would be wise to consider pre-commitment limit-setting and other harm minimization controls used in traditional gambling to regulate loot box spending."[365]

Individuals with experience regulating gambling, such as Keith Whyte of the National Council on Problem Gambling, have spoken out in support of similar practices.[366] At the 2019 FTC workshop, Mr. Whyte noted:

> [A]nother tip from the gambling side is self-exclusion. So one of the most effective ways to help someone who may have a problem with their gambling, or with their gaming use, is to allow them to self-exclude themselves. And in an environment where transactions are monitored, you can use self-exclusion through payment mechanisms, because while people may have many different accounts and play many different games across many different providers and platforms, they're probably using that one credit card, or at least a common bank account. And so payment level blocking can be very effective, buttressing and adding to existing platform level controls and others.
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> Self-exclusion also places a priority, or that places the emphasis on the gambler, or the gamer, and not necessarily the operator.[367]

Not all experts agree that limit-setting would be an effective solution. In a subsequent letter to the editor of *Addiction*, Doctors Daniel L. King and Paul H. Delfabbro critiqued Dr. Drummond's recommendation that limit-setting be incorporated into loot box regulations.[368] They noted:

> Drummond et al. assert that limit-setting 'is broadly effective at reducing over-expenditure, and generally viewed positively by gamblers'. While we agree that a range of harm minimization controls should be examined, we have some reservations about proposing any single regulatory control in isolation of other supporting measures. Introducing a $50 limit on loot box spending, as Drummond et al. propose, may have unintended consequences that lead to other problems (e.g. some players may increase their playing time to compensate for spending less money). Additionally, game designers may find strategies to obtain revenue in other ways by introducing other micro-transaction features, such as features on external or

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363 *Id.*
364 *Id.*
365 *Id.*
366 INSIDE THE GAME, *supra* note 8, at 185–86.
367 *Id.* at 193–94.
368 Daniel L. King & Paul H. Delfabbro, Letter to the Editor, *Loot Box Limit-Setting is Not Sufficient on Its Own to Prevent Players from Overspending: A Reply to Drummond, Saurer & Hall*, 114 ADDICTION 1324, 1324 (2019) (footnotes omitted).

> third-party platforms, which would create further complexities for limit-setting and players keeping track of spending.[369]

The authors did not discard limit-setting as a regulatory measure; rather, they cautioned against over-reliance on a single regulatory mechanism and instead recommended "undertak[ing] a wide consultation and scoping process to develop a comprehensive list of potential countermeasures and related consumer advice and protections, particularly those designed specifically for gaming and in-game purchasing, for the purpose of further review and evaluation."[370] While they raise a valid point, the existence of other possible consumer protection mechanisms should not foreclose the exploration of limit-setting in the here and now. Individuals are suffering real harm in the present; waiting to implement protections until the best protection has been discovered will needlessly prolong their harm. The authors' concerns are further mitigated in light of this Article's recommendation that the states implement their own regulations. By virtue of state-by-state experimentation, the best methodology will be discovered in time, and consumer interests will be advanced (even if only imperfectly) in the interim.

From a philosophical perspective, some might object to placing limits upon an individuals' autonomy by preventing them from making a purchase they desire to make. In evaluating self-limitation as a method of protecting the elderly from predatory lenders, Professor Kurt Eggert engaged in an analysis of the meaning of autonomy.[371] Professor Eggert noted, "If we hold that autonomy has intrinsic value, then to improve the lives of the elderly, we should try to increase their autonomy."[372] He further discussed the difficulties in maximizing elders' autonomy, writing:

> Increasing autonomy is not merely a matter of removing restraints, for even unrestrained, a person may have so few options that she has no real choice in what to do. Nor does merely providing more options provide more autonomy, since the individual given the options may effectively have no way to analyze them or determine which is preferable. To provide the greatest possibility of autonomy, we would need to provide a rich array of options as well as work to ensure that the chooser has the capacity to rate and compare those options.[373]

Professor Eggert confronted the difficulty in determining whether to honor an individual's past wish to bind themselves in

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369 *Id.*

370 *Id.*

371 *See* Kurt Eggert, *Lashed to the Mast and Crying for Help: How Self-Limitation of Autonomy Can Protect Elders from Predatory Lending*, 36 LOY. L.A. L. REV. 693, 695–96 (2003).

372 *Id.* at 732.

373 *Id.* at 733.

the present.[374] He reasoned, "[t]o determine which version of the self-limiter's choice—the earlier decision to limit autonomy or the later decision to revoke that limitation—is closer to being more authentic and voluntary, the relative quality of the choice should be examined."[375] He listed such factors as whether a "decision was made with greater competency, more information, and greater freedom from manipulation, coercion, or fraud, as well as which shows a more 'resolute intention' to make the decision."[376] In considering the philosophical idea of "separat[ing] one's identity into various strands, such as a present self and various future selves,"[377] Professor Eggert theorized that, "[i]f we . . . split the self this way, then the self-limitation of autonomy becomes, to a significant extent, a method for the present self to bind the future self, or for the long-term planning self to bind the self desiring immediate gratification."[378]

Reviewing the efficacy of self-exclusion programs in the realm of problem gambling, Professor Eggert observed that self-exclusion is a "method of providing protection from excessive gambling, while respecting the autonomy of the problem gambler."[379] He explained that self-exclusion programs involve self-identified problem gamblers voluntarily signing up to "request to be personally excluded from one or more, or perhaps all, of the casinos in the state."[380] "The self-exclusion program," Professor Eggert wrote, "is a classic example of the self-limitation of autonomy as a method of consumer protection. Like Ulysses, the compulsive gambler recognizes that he will be unable to resist the siren call of the casinos, and seeks a way to limit his own freedom."[381] He noted that self-exclusion programs "also appeared useful as a 'gateway' to lead problem gamblers to obtain professional counseling for about half of those who self-excluded."[382]

In evaluating the weaknesses of such programs, Professor Eggert conceded, "[t]he greatest potential flaw of these self-exclusion programs appears to be their unreliability, the ease with which gamblers can circumvent them, either by going to a different casino in a state which does not have a central registry, or by tricking the casinos to allow them to gamble."[383] Nonetheless, Professor Eggert

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374 *See id.* at 736.
375 *Id.* at 738.
376 *Id.* (footnote omitted).
377 *Id.* at 739.
378 *Id.*
379 *Id.* at 748.
380 *Id.*
381 *Id.* (footnote omitted).
382 *Id.* at 751–52.
383 *Id.* at 752.

went on to conclude, in analyzing self-exclusion programs as a form of self-limitation:

> A gambler's choice to self-exclude will, in general, likely increase rather than decrease his overall autonomy, at least if it aids the gambler to defeat his addiction. The amount of autonomy the gambler gives up will likely be small so long as he honors the self-exclusion, since he is still free in every other aspect of his life. The risk that he may have erred in his thinking also seems small, since existing evidence indicates that almost all those who self-exclude are problem gamblers. Perhaps most importantly, a gambler is likely to be acting more freely and more true to his essential self when he initially decides to limit his autonomy, rather than later, when his compulsion to gamble would push him to reenter a casino.[384]

As an example, Professor Eggert detailed the Illinois Gaming Board's step-by-step requirements for opting into the self-exclusion program, and noted that "[m]ost likely, people would put much more consideration and thought into going to a gaming board office and self-excluding than they would to dropping quarters into a slot machine."[385]

Just as limit-setting has encouraged individual autonomy in the gambling context, it could be similarly effective at combatting problematic loot box purchase activity. Individuals playing a certain game on their personal account would not be able to circumvent the lock without opening a brand new account, defeating the purpose of accruing rewards on their original account.[386] Professor Eggert's concerns about traditional self-exclusion workarounds are not entirely assuaged in video game circles, however, because those players could go on to simply play a different game or continue to obsessively play the game to make up the difference.[387] However, a player who encounters a message from their past selves, displayed in game and advising them that they have hit their pre-determined limit, will have more of an opportunity to reflect upon their actions than a player who does not see such a message.

While the casinos that opted out of the self-exclusion program (i.e. the casinos that did not have a central registry of participants) provided a venue for would-be self-excluders to cheat their past selves and exceed their personal limits, a government-mandated form of limit-setting would by definition not allow disinterested vendors to "opt out."[388] Unlike

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384 *Id.* at 755–56.
385 *Id.* at 756.
386 Drummond et al., *supra* note 61, at 935.
387 *See* King & Delfabbro, *supra* note 368, at 1324.
388 *See* INSIDE THE GAME, *supra* note 8, at 196 (statement of Keith Whyte) ("But for

commentators at the FTC workshop, who struggled to envision a limit-setting scenario that could survive the perverse incentive individual developers would have to fail to adhere to the Industry standard,[389] a government-mandated limit-setting program would leave no room for lawful noncompliance. The Industry would be required to adhere to limit-setting practices in all of its loot box titles, deprived only of its opportunity to exploit vulnerable individuals.

Professor Eggert, writing about self-exclusion practices, considered the words of philosopher Joseph Raz: "[O]ne cannot force another person to be more autonomous. Instead, the most that can be done is 'by and large confined to securing the background conditions which enable a person to be autonomous.'"[390] By requiring video game developers to implement limit-setting mechanisms in their loot box purchase systems, we as a society would be providing compulsive individuals with a better opportunity to exercise their autonomy than currently available under the ESRB's direction.

VII. CONCLUSION

Loot boxes are linked to problem gambling.[391] Whether they cause problem gambling or merely exploit players' existing tendencies,[392] we as a society should not tolerate the Industry's attempts to monetize the practice under its sole discretion. The ESRB has abdicated its authority by failing to advance meaningful regulations in a timely manner, and Industry advocates frequently engage in bad-faith argumentation to justify the practice and disregard or deny the harm to vulnerable individuals. The psychological and financial harm inflicted by loot boxes is real and pervasive, and individuals and their representatives are beginning to wake up to that fact. Both the federal and state governments have the ability to take action, and have merely neglected to do so thus far. Rather than wait for the ESRB to cede regulatory ground inch-by-inch, consumers should demand regulatory protection by an entity that primarily serves their own interests, not those of the Industry. The state governments are perhaps best equipped and empowered to act on behalf of consumers in this area. Limit-setting mechanisms and meaningful odds disclosures could serve as powerful tools to help

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these [self-exclusion] measures to be effective, it will take true commitment of leadership from ESA, ESRB, and every developer and publisher worldwide, because if you have even one company that chooses not to participate, that opts out, that doesn't comply with standards, the whole system, the foundation of the entire system is undermined.").

389 *Id.*

390 Eggert, *supra* note 371, at 732.

391 Zendle & Cairns, *supra* note 7.

392 *Id.*

consumers make informed purchase decisions, cutting through the veils raised by in-game currencies and piecemeal transactions.

Ultimately, video games are here to stay. They are a beloved pastime for millions of Americans.[393] Video game developers perform a useful role in creating these games for the enjoyment of the public, and loot boxes help to support some of them. This Article's goal is not to chastise developers, nor to advocate for the outright ban of loot boxes. Rather, this Article has attempted to peel back layers of Industry double-talk in order to reveal the very real costs of loot boxes and their similarities to traditional gambling practices, so that readers can decide for themselves how best to proceed. At the very least, perhaps a reader will think twice before hitting "Buy Now" when purchasing a loot box in their favorite game.

The true cost could be far more than $1.99.

393 Myself included.

Unsportsmanlike Conduct – Calling a Penalty on the NFLPA and NHLPA's Duty of Fair Representation for Entering Players

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I. INTRODUCTION

The 2019 National Football League ("NFL") season saw Michael Thomas of the New Orleans Saints shatter the league's single-season receptions record.[1] But a look at the situation that transpired in the summer before this record-breaking campaign shows how close it was to not happening.[2] Thomas, like an increasing number of young, superstar athletes, was unhappy with the terms of his rookie contract[3]—a contract that was provided to Thomas by the New Orleans Saints after he was selected as the forty-seventh overall pick in the 2016 NFL Draft.[4] Thomas' initial deal with the Saints was predetermined by the rookie compensation restrictions in the 2011 collective bargaining agreement agreed upon by league owners and the National Football League Players' Association ("NFLPA").[5]

As a second-round pick, Thomas was given a four-year, $5.1 million contract of which $2.6 million was guaranteed.[6] After being selected to the Pro Bowl following the 2017 and 2018

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1 *See NFL Single Season Leaders – Receptions*, FOOTBALL DATABASE, http://www.footballdb.com/leaders/season-receiving-receptions [http://perma.cc/J42C-TWUP] (last visited Mar. 23, 2020).

2 *See* Mike Triplett, *Why the Saints had to break the bank for Michael Thomas*, ESPN (Jul. 31, 2019), http://www.espn.com/nfl/story/_/id/27294194/why-saints-had-break-bank-michael-thomas [http://perma.cc/GL9Q-EZJV].

3 *Id.*

4 *Id.*

5 *See generally* Nat'l Football League, Collective Bargaining Agreement 2011-2020, Art. 7, https://nflpaweb.blob.core.windows.net/media/Default/PDFs/2011%20CBA%20Updated%20with%20Side%20Letters%20thru%201-5-15.pdf [http://perma.cc/3AJX-R4FV] (last visited May 3, 2020).

6 *Michael Thomas*, SPOTRAC, http://www.spotrac.com/nfl/new-orleans-saints/michael-thomas-18996/ [http://perma.cc/7F78-V8Z8] (last visited Mar. 23, 2020) (showing that, when broken down on a per-year basis, Thomas was earning an average salary of $1,279,743 on his rookie contract).

seasons, and being named a First-Team All-Pro in 2018[7], Thomas was prepared to not report to Saints' training camp in an attempt to secure a better contract.[8] Ultimately Thomas and the Saints agreed on a five-year, $96.25 million contract extension—with a touch over $35.6 million guaranteed—that allowed him to be in training camp with his teammates in preparation for the 2019 season[9], a season that saw Thomas ultimately put out one of the most dominating performances by a wide receiver in NFL history.

In just three years, Thomas had secured a deal worth over fifteen times that of his restrictive rookie deal that was mandated by the collective bargaining agreement. Was Thomas suddenly fifteen times the player he was when he was drafted? Or was this new deal a much more accurate reflection of Thomas' correct value? In an industry where the average career length is measured in single-digit years and not decades, which dwarfs in comparison to the time spent preparing to reach the pinnacle, players must capitalize on their worth quickly.[10]

There are a select number of players who are able to successfully negotiate a significantly more lucrative contract without the threat of a holdout.[11] Unfortunately, Thomas' story is quickly becoming the rule rather than the exception. A number of NFL and National Hockey League ("NHL") players nearing the

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7 *Michael Thomas*, PRO FOOTBALL REF., http://www.pro-football-reference.com/players/T/ThomMi05.htm [http://perma.cc/LZE8-YM6V] (last visited Jan. 26, 2020).

8 *See* Jenna West, *Michael Thomas Doesn't Report to Saints' Training Camp While Seeking New Deal*, SPORTS ILLUSTRATED (July 25, 2019), http://www.si.com/nfl/2019/07/25/michael-thomas-contract-saints-training-camp [http://perma.cc/44TH-85XG].

9 *See* Mike Florio*, Inside the Michael Thomas deal,* NBC SPORTS (July 31, 2019, 8:27 PM), http://profootballtalk.nbcsports.com/2019/07/31/inside-the-michael-thomas-deal/ [http://perma.cc/5V38-V7CG] (stating that, when broken down on a per-year basis, Thomas' new deal pays him an average base salary of $19.25 million per year).

10 *See generally* Heather Brown, *Good Question: How Long Can Athletes Stay In The Game?*, WCCO CBS MINNESOTA (Feb. 8, 2016, 10:44 PM), http://minnesota.cbslocal.com/2016/02/08/good-question-how-long-can-athletes-stay-in-the-game/ [http://perma.cc/4N67-ULG6]; SI Wire, *WSJ data analysis shows average length of NFL careers decreasing*, SPORTS ILLUSTRATED (Mar. 1, 2016), http://www.si.com/nfl/2016/03/01/nfl-careers-shortened-two-years-data-analysis [http://perma.cc/E3XM-XBG3].

11 *See* Mike Florio*, Inside the Christian McCaffery contract,* NBC SPORTS (Apr. 16, 2020, 10:22 PM), http://profootballtalk.nbcsports.com/2020/04/16/inside-the-christian-mccaffrey-contract/ [http://perma.cc/36QZ-Y7Q7] ("McCaffrey got his new deal after only three seasons, without a holdout or any other public ugliness. It's a testament to Panthers owner David Tepper, who recognized that McCaffrey is a high-talent, high-integrity core player who will be part of the franchise's nucleus for years to come."); *see also* Sportsnet Staff, *Connor McDavid signs eight-year, $100M extension with Oilers*, SPORTSNET (July 5, 2017, 3:06 PM), http://www.sportsnet.ca/hockey/nhl/connor-mcdavid-signs-eight-year-extension-oilers/ [http://perma.cc/6AQQ-3LBQ] ("McDavid . . . still has one year remaining on his entry-level contract, so the extension doesn't kick in until the 2018-19 season.").

end of their existing contracts are using the leverage that their performances have created to secure themselves the money that they rightfully deserve. Le'Veon Bell[12], Ezekiel Elliott[13], Melvin Gordon[14], Trent Williams[15], and William Nylander[16] are amongst the most recent high-profile names that are dissatisfied enough with their current contract situation to justify missing playing time to seek out a new contract. The parameters restricting rookie compensation in the NFL and NHL can and must be improved. The NFLPA and The National Hockey League Players' Association ("NHLPA")—the unions that represent these athletes in collective bargaining negotiations with league management—must act with the best interest of *all* their members in mind, not solely veteran players.

Part II of this Article discusses the background and purpose of collective bargaining in American professional sports, the consequences of collective bargaining failure, and the results of player dissatisfaction. Part III of this Article describes the interconnected relationship between antitrust law and labor law in sports and details a current problem in the collective bargaining agreements of the NFL and the NHL—rookies are disproportionately subjected to unduly restrictive contract compensation as a result of bad faith negotiation by their respective players' associations, in violation of the National Labor Relations Act. Part III continues with comparisons to past collective bargaining agreements and shows how players have responded to these restrictions by refusing to play under the existing terms of their contracts and their justification for seeking increased compensation. Finally, Part IV advocates for a proposal that prohibits players' associations from negotiating different rights based on the time a player—or a class of players—has spent

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12 *See* Danny Heifetz, *Le'Veon Bell's Holdout Feels Real This Time*, RINGER (Sept. 5, 2018, 4:46 PM), http://www.theringer.com/nfl/2018/9/5/17824408/leveon-bell-holdout-contract-franchise-tag-pittsburgh-steelers [http://perma.cc/KBG9-LPL4].

13 *See* Bill Williamson, *All You Need To Know About The Ezekiel Elliott Holdout*, FORBES (Aug. 7, 2019, 7:42 PM), http://www.forbes.com/sites/billwilliamson/2019/08/07/all-you-need-to-know-about-the-ezekiel-elliott-holdout/#6290f80471c2 [http://perma.cc/3MPY-4ZJK].

14 *See* Dan Cancian, *Melvin Gordon Holdout: Will Los Angeles Chargers Star Play This Year?*, NEWSWEEK (Sept. 3, 2019, 12:07 PM), http://www.newsweek.com/will-melvin-gordon-play-holdout-contract-los-angeles-chargers-1457433 [http://perma.cc/QJD9-WQBK].

15 *See* Ethan Cadeaux, *A timeline of the Trent Williams holdout: how did we get here?*, NBC SPORTS WASHINGTON (Sept. 16, 2019, 11:18 AM), http://www.nbcsports.com/washington/redskins/timeline-trent-williams-holdout-how-did-we-get-here [http://perma.cc/6YQ4-K5E5].

16 *See* Mike Johnston, *Report: Rival NHL execs question Maple Leafs forward Nylander's value*, SPORTSNET (Oct. 19, 2018, 7:16 PM), http://www.sportsnet.ca/hockey/nhl/report-rival-nhl-execs-question-maple-leafs-forward-nylanders-value/ [http://perma.cc/ZJN7-UKQD].

in the league when negotiating future collective bargaining agreements. Part IV draws comparisons to both sports and non-sports examples of players' associations or unions not setting a maximum amount that entering talent is able to earn and further discusses the importance of implementing uniformity in the rights afforded to players when negotiating with league ownership.

II. BACKGROUND

A. Origins of Collective Bargaining Agreements

Collective bargaining agreements are "document[s] by which a labor union and an employer stipulate to the terms of employment for those employees that are party to the collective bargaining agreement which formulate the foundation for dealings between players' unions and league ownership".[17] Collective bargaining agreements allow these unions—representing the players and their interests—and employers—representing the team owners and their interests—to negotiate and come to terms on crucial matters affecting league play.[18]

The National Labor Relations Act ("NLRA") was introduced by Congress in 1935 "to protect the rights of employees and employers, to encourage collective bargaining, and to curtail certain private sector labor and management practices, which can harm the general welfare of workers, businesses and the U.S. economy."[19] Section 9 of the NLRA provides:

> Representatives designated or selected for the purposes of collective bargaining by the majority of the employees in a unit appropriate for such purposes, shall be the exclusive representatives of all the employees in such unit for the purposes of collective bargaining in respect to rates of pay, wages, hours of employment, or other conditions of employment.[20]

The NFLPA has been the unionized representative body of football players in the NFL since 1956[21], although NFL club owners did not recognize the union until 1968, when the first collective bargaining agreement was entered into.[22] The NHLPA

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17 Blake Yagman, *Weekly Legal Brief: Collective Bargaining, Lockouts, and Strikes*, FRONT OFFICE SPORTS (Apr. 27, 2018), http://www.frntofficesport.com/weekly-legal-brief-collective-bargaining-lockouts-and-strikes [http://perma.cc/68N5-8F8C].

18 *Id.*

19 *National Labor Relations Act*, NAT'L LAB. RELS. BD., http://www.nlrb.gov/how-we-work/national-labor-relations-act (last visited Mar. 1, 2020).

20 29 U.S.C. § 159(a) (2012).

21 *About the NFLPA*, NFL PLAYERS ASS'N, http://www.nflpa.com/about [http://perma.cc/33L5-U6S2] (last visited Feb. 29, 2020).

22 *NFL labor history since 1968*, ESPN (Mar. 3, 2011), http://www.espn.com/nfl/news/story?page=nfl_labor_history [http://perma.cc/DB2X-78SG].

was formed in 1967 and was recognized that same year by NHL club owners.[23] The first collective bargaining agreement between the NHLPA and the NHL was reached in 1975.[24] In the early stages of the respective players' associations, the collective bargaining agreements between the sides were focused on "basic economic rights."[25] It was not until the players garnered more leverage vis-à-vis the owners that they began to redirect the narrative and push for more in their collective bargaining discussions, including securing a share of league revenues, and other salary related issues.[26]

While labor negotiations between players' unions and league owners may appear to be identical to that of non-sports industries, there are much deeper layers of factors to consider.[27] The sports industry combines an employee base that possesses a unique set of skills with a monopolistic employer.[28] There are few, if any, substitute leagues for athletes that wish to ply their trades at the highest level and thus they must subject themselves to a lesser bargaining power vis-à-vis league owners.[29]

B. Purpose of Collective Bargaining Agreements: Parity and Control

Professional sports in North America are part of a large and ever-growing industry.[30] While millions of North Americans enjoy sports on some level, team ownership is a privilege reserved for the ultra-rich.[31] The Dallas Cowboys, often regarded as the benchmark franchise in North American sports, have a valuation of $5.5 billion while the Buffalo Bills, the NFL franchise with the lowest valuation, is still worth just south of $2 billion.[32] The four major sports leagues—the NFL, NHL, National Basketball Association ("NBA"),

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23 *Frequently Asked Questions*, NHLPA, http://www.nhlpa.com/the-pa/what-we-do/faq [http://perma.cc/UF8F-H8LP] (last visited Mar. 1, 2020).

24 *Id.*

25 Gabe Feldman, *Collective Bargaining in Professional Sports: The Duel Between Players and Owners and Labor Law and Antitrust Law*, *in* OXFORD HANDBOOK OF AMERICAN SPORTS LAW 5 (Michael A. McCann ed., 2018).

26 *Id.*

27 *Id.* at 6.

28 *Id.*

29 *Id.*

30 Darren Heitner, *Sports Industry To Reach $73.5 Billion By 2019*, FORBES (Oct. 19, 2017, 7:15AM), http://www.forbes.com/sites/darrenheitner/2015/10/19/sports-industry-to-reach-73-5-billion-by-2019/#7e94448c1b4b [http://perma.cc/8AE2-U8SS].

31 *See* Michael Ozanian et al., *The NFL's Most Valuable Teams 2019: Cowboys Lead League at $5.5 Billion,* FORBES (Sept. 4, 2019, 7:25 AM), http://www.forbes.com/sites/mikeozanian/2019/09/04/the-nfls-most-valuable-teams-2019-cowboys-lead-league-at-55-billion/#2b6b29212f1b [http://perma.cc/8FRJ-DY9Z].

32 *See id.*

and Major League Baseball ("MLB")—collectively recognized approximately $31 billion dollars in revenue in their most recent seasons.[33] All thirty-two NFL teams experienced positive operating incomes in 2019, with profits ranging from $28 million to $420 million.[34] These revenue figures are driven by television deals, advertisements, corporate sponsorships, gate revenues, and merchandise sales.[35]

A vital consideration for these revenue drivers is the concept of parity or "fairness in play."[36] "In order to be successful . . . the public must believe that there is relative parity among the member teams and that each team has the opportunity of becoming a contender over a reasonable cycle of years . . . ."[37] Aiming to meet these parity goals, league collective bargaining agreements set forth and detail important competitive balance measures such as: (1) draft selection order, (2) restriction on player movement, and (3) salary control measures, or "salary caps."[38]

Most incoming players to the NFL and NHL enter through the draft process.[39] It is through this process that organizations are given the "exclusive rights" to secure the services of the player.[40] The NFL determines their draft selection order with a true reversal of the standings from the previous year.[41] The NHL uses a lottery system where each non-playoff team has the

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33 Devon Anderson, *Ranking Professional Sports Leagues by Revenue*, ULTIMATE CORP. LEAGUE (Apr. 10, 2019), http://www.ultimatecorporateleague.com/ranking-professional-sports-leagues-by-revenue/ [http://perma.cc/5BCB-XRPD].

34 *See* Ozanian, *supra* note 31, (showing that the Oakland Raiders realized $28 million in operating income from revenue of $357 million while the Dallas Cowboys realized $420 million in operating income from revenue of $950 million).

35 *See generally* TJ Mathewson, *TV is biggest driver in global sport league revenue*, GLOB. SPORT MATTERS (Mar. 7, 2019), http://globalsportmatters.com/business/2019/03/07/tv-is-biggest-driver-in-global-sport-league-revenue/ [http://perma.cc/8DJS-6B9B].

36 Duane W. Rockerbie, *Exploring Interleague Parity in North America: The NBA Anomaly*, 17 J. OF SPORTS ECON. 286, 286 (2016).

37 Phila. World Hockey Club, Inc. v. Phila. Hockey Club, Inc., 351 F. Supp. 462, 486 (E.D. Pa. 1972).

38 *Collective Bargaining Agreements in Sports: How Do They Work in the United States vs. Europe*, MONEY SMART ATHLETE BLOG (Aug. 29, 2018), http://moneysmartathlete.com/2018/08/29/collective-bargaining-agreements-in-sports-how-do-they-work-in-the-united-states-vs-europe/ [http://perma.cc/8QCF-FVLU].

39 *See* Travis Lee, *Competitive Balance in the National Football League After the 1993 Collective Bargaining Agreement*, 11 J. SPORTS & ECON. 77, 78 (2010); *see generally* Sam McCaig, *From the draft to the NHL: A round-by-round look at the league's skaters and goalies*, HOCKEY NEWS (Oct. 21, 2018), http://thehockeynews.com/news/article/from-the-draft-to-the-nhl-a-round-by-round-look-at-the-leagues-skaters-and-goalies [http://perma.cc/Y3Q3-J25V].

40 Lee, *supra* note 39.

41 *The Rules of the Draft*, NFL OPERATIONS, https://operations.nfl.com/journey-to-the-nfl/the-nfl-draft/the-rules-of-the-draft/ (last visited Nov. 3, 2019) [http://perma.cc/TX63-92Z8].

chance to select first in the draft, with the team that has the worst record given the highest probability to earn the right to select first.[42] Both of these systems seek to provide the least-successful teams in a given year with the opportunity to turn their franchise fortunes around by selecting higher-rated prospects that are available through the draft.

In an effort to allow teams to retain their top-tier talent and remain competitive, collective bargaining agreements also include restraints on player movement. In the early days of sports, perpetual reserve clauses allowed teams to retain the services of their players indefinitely until they were released from their obligations by the team.[43] In modern sports, where perpetual reserve clauses have been abolished, players are under club control for a set period of years before hitting "free agency."[44] It is at this point that a player can then decide on their own where they wish to take their services.[45] Many players elect to spend their entire career with one organization, but many also choose to explore the market and peddle their skills elsewhere upon satisfying their obligations under their respective contracts.[46]

In addition, league collective bargaining agreements also implement a salary control tool that is more or less exclusive to American sports: the salary cap. The NFL[47] and NHL[48] are both governed by a "hard" salary cap, which operates by setting the upper limit of player salaries that a team is permitted to spend in a given league year.[49] These salary control devices aim to foster an environment of parity in American sports by preventing teams with deeper pockets from monopolizing high-end talent in the league, empowering franchises in smaller markets to obtain

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42 *See* Adam Kimelman, *2019 NHL Draft Lottery Will Determine First Three Teams to Pick*, NHL (Apr. 8, 2019), http://www.nhl.com/news/2019-nhl-draft-lottery-faq/c-306581364 [http://perma.cc/AY7U-RMLZ].

43 Jonathan B. Goldberg, *Player Mobility in Professional Sports: From the Reserve System to Free Agency*, 15 SPORTS L. J. 21, 22–25 (2008).

44 *Id.* at 44.

45 *Id.*

46 *See id.* at 56–57.

47 Grant Gordon, *NFL salary cap for 2019 season set at $188.2M*, NFL (Mar. 1, 2019, 5:37 PM), http://www.nfl.com/news/story/0ap3000001020137/article/nfl-salary-cap-for-2019-season-set-at-1882m [http://perma.cc/JJ85-LZNM] ("Officially, the salary cap for 2019 will be $188.2 million . . .").

48 Dan Rosen, *NHL announces salary cap for next season*, NHL (June 22, 2019), http://www.nhl.com/news/nhl-announces-salary-cap-for-2019-20-season/c-308008530 [http://perma.cc/GTH3-QQZ4] ("The NHL salary cap for the 2019-20 season will be $81.5 million . . .").

49 Jim Pagels, *Are Salary Caps for Professional Athletes Fair?*, PRICEONOMICS (Aug. 19, 2014), http://www.priceonomics.com/are-salary-caps-for-professional-athletes-fair/ [http://perma.cc/MJP8-SFPG].

player services, and allowing overall league prosperity by encouraging reasonable competitiveness.[50]

The salary control exhibited in American sports can be contrasted with the five major European soccer leagues: England's Premier League, Italy's Serie A, Spain's La Liga, Germany's Bundesliga, and France's Ligue 1, which all lack a salary cap or luxury tax structure, resulting in staggering salary inequality.[51] In 2018, a survey examining salary inequality was conducted based on the average first-team salaries of teams in major professional sports leagues.[52] From these salaries a fairness metric was created: a ratio calculated by taking the average first-team salaries of the highest spender in a respective league and dividing it by the amount spent by the lowest spender.[53]

Of the eighteen leagues studied in the survey, the major European soccer leagues occupied five of the seven lowest rankings in salary inequality based on the fairness metric.[54] American sports, with their salary caps and luxury tax provisions, all ranked in the top half of fairness metric rankings in that same study.[55] If the raw "fairness metric" ratios are compared, the gap is increasingly apparent: each North American sport has a ratio of less than 4:1, while the Premier League is the only European league with a ratio of less than 10:1.[56] Each of the other four European leagues double the ratio seen in the Premier League.[57]

It would appear that the strive for parity in American sports through salary control devices has been largely successful. Of the forty major American championships in the last decade, 70% have been won by unique teams.[58] In the major European soccer

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50 *What is a Salary Cap in Sports?*, UNIV. KAN. (Apr. 2, 2018), https://onlinesportmanagement.ku.edu/community/salary-caps-in-sports, [http://perma.cc/TN32-9E7H].

51 *See generally Global Sports Salaries Survey 2018*, SPORTING INTEL. (Nov. 25, 2018), http://www.globalsportssalaries.com/GSSS%202018.pdf [http://perma.cc/KQX9-GCJ7].

52 *Id.* at 8.

53 *Id.*

54 *See infra* Appendix A.

55 *Id.*

56 *Id.*

57 *Id.*

58 *See generally NBA & ABA Champions*, BASKETBALL REF., http://www.basketball-reference.com/playoffs/ [http://perma.cc/2SY6-CRR5] (last visited Nov. 3, 2019); *NHL/WHA Playoffs*, HOCKEY REF., http://www.hockey-reference.com/playoffs/ [http://perma.cc/U9EP-LN9V] (last visited Nov. 3, 2019); *Pro Football & NFL History*, PRO FOOTBALL REF., http://www.pro-football-reference.com/years/ [http://perma.cc/K6HW-RHWT] (last visited Nov. 3, 2019); *World Series and MLB Playoffs*, BASEBALL REF., http://www.baseball-reference.com/postseason/ [http://perma.cc/QZ92-JR72] (last visited Nov. 3, 2019) (calculations conducted by author and correct as of May 18, 2020).

leagues that lack the competitive balance measures of American sports, that number drops to 34%.[59]

C. Consequences of Collective Bargaining Failures and Dissatisfaction

1. Lockouts/Strikes

Ultimately, the role of a collective bargaining agreement is to get the players out onto the field, ice, or court. Due to the high-risk nature of professional sports competition and the large considerations involved in each league's collective bargaining agreement, negotiations can be hostile and lead to lockouts instituted by owners or strikes instituted by players' unions.[60] The most notable lockout from a fan and media perspective was the 2011 NFL lockout, which lasted from March 12, 2011 until August 4, 2011 and garnered around-the-clock coverage on major sports news outlets.[61] The NBA experienced a 161-day work stoppage during roughly that same time period when the owners locked the players out from July 1, 2011 to December 8, 2011.[62]

In August of 1994, MLB players instituted a strike mid-season that caused the loss of over 900 scheduled games—including the entirety of the 1994 playoffs.[63] The strike was eventually resolved in April of the following year after 232 days of labor tensions.[64] The NHL is infamously known as the only North American professional sports league to forego an entire season due to a labor dispute.[65] The NHL lost the 2004–2005 season to a lockout before the NHL and the National Hockey League Players' Association ("NHLPA") finally

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59 *See generally Bundesliga Seasons*, FB REF, http://www.fbref.com/en/comps/20/history/Bundesliga-Seasons [http://perma.cc/F7RC-RTMB] (last visited Nov. 3, 2019); *La Liga Seasons*, FB REF, http://www.fbref.com/en/comps/12/history/La-Liga-Seasons [http://perma.cc/7CYU-3HD2] (last visited Nov. 3, 2019); *Ligue 1 Seasons*, FB REF, http://www.fbref.com/en/comps/13/history/Ligue-1-Seasons [http://perma.cc/74XJ-NHGZ] (last visited Nov. 3, 2019); *Premier League Seasons*, FB REF, http://www.fbref.com/en/comps/9/history/Premier-League-Seasons [http://perma.cc/Y3RP-MR56] (last visited Nov. 3, 2019); *Serie A Seasons*, FB REF, http://www.fbref.com/en/comps/11/history/Serie-A-Seasons [http://perma.cc/X7KJ-AYX3] (last visited Nov. 3, 2019) (calculations conducted by author).

60 *See* Alex Remington, *Lockouts, Strikes, And Labor Politics In Pro Sports*, FOOTNOTE (June 5, 2013), http://footnote.co/lockouts-strikes-and-labor-politics-in-pro-sports/ [http://perma.cc/7C9D-VL76].

61 *See generally* CNN Library, *Pro Sports Lockouts and Strikes Fast Facts*, CNN, http://www.cnn.com/2013/09/03/us/pro-sports-lockouts-and-strikes-fast-facts/index.html [http://perma.cc/P7UJ-RZA3] (last updated June 4, 2020, 1:18 PM).

62 *See id.*

63 *See id.*

64 *See id.*

65 *See id.*

agreed to a six-year collective bargaining agreement in July of 2005.[66] After extending the agreement for one additional season, the NHL owners again locked out the players in September of 2012, causing the truncation of the 2012–2013 NHL season.[67]

2. Player Dissatisfaction–The Holdout

Unfortunately for owners, players, and fans of sports, a ratified collective bargaining agreement does not ensure harmony for the duration of the agreement. Players who are unsatisfied with their contract terms (e.g., contract length, base salary, performance incentive bonuses, or guaranteed money) often holdout for a more lucrative contract.[68] A "holdout" is sports industry terminology for a player's refusal to continue playing under the terms of a previously agreed-upon deal.[69] Holdouts are becoming increasingly common in professional sports and ultimately impact not only the team that is losing the services of a player, but also the perception of the team and league in the eyes of sponsors, advertisers, and fans.[70]

In addition to the competitive balance and overall salary restraints detailed above, recent collective bargaining agreements have implemented additional provisions that put restrictions on the negotiable terms in rookie contracts.[71] The restrictions include detailing and limiting the maximum salary payable under a rookie contract, fixing the length of years that a player must sign for under their first contract, and providing movement restrictions following the end of that first contract.[72] With the average career length varying from "three to five years," players realize that there is a sense of urgency to earn their fair share during the very brief window they have before injuries inevitably take a toll.[73] As a result of this short earning potential,

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66 *See id.*

67 *See id.*

68 *See* Jack Bechta, *Why Players Hold Out*, NAT'L FOOTBALL POST, http://nationalfootballpost.com/why-players-hold-out/ [http://perma.cc/DL4C-N68H] (last visited Mar. 6, 2020).

69 Jacob Salow, *Holdouts, Lockouts, and Payouts: The National Football League's Bargaining Power Phenomenon*, 43 L. & PSYCH. REV. 239, 240 (2019).

70 Peter B. Kupelian & Brian R. Salliotte, *The Use of Mediation for Resolving Salary Disputes in Sports*, 2 THOMAS M. COOLEY J. PRAC. & CLINICAL L. 383, 391 (1999).

71 *See* Blake Yagman, *The Weekly Legal Brief: Breaking Down NFL Rookie Contracts*, FRONT OFFICE SPORTS (May 4, 2018), http://www.frntofficesport.com/the-weekly-legal-brief-breaking-down-nfl-rookie-contracts/ [http://perma.cc/PEB9-Y3DX].

72 *See generally* Nat'l Football League, *supra* note 5; Nat'l Hockey League, Collective Bargaining Agreement 2012–2022 at Art. 9, http://www.nhl.com/nhl/en/v3/ext/CBA2012/NHL_NHLPA_2013_CBA.pdf [http://perma.cc/PQ5N-KV87] (last visited Nov. 3, 2019).

73 Brown, *supra* note 10; *see also* Dave Siebert, M.D., *The Impact of Modern Medicine on the NFL*, BLEACHER REP. (May 16, 2013), http://bleacherreport.com/articles/1639848-

a "majority of holdouts" occur when players are in the later stages of their rookie, or entry-level, contracts.[74] These players are on team-friendly deals by virtue of being locked into the restrictive terms set by the collective bargaining agreements of the NFL and NHL.[75] Oftentimes the teams wish to keep the player for longer but are in no rush to sign the player prior to their deal ending and while the player is under team control on less-expensive contracts.[76]

D. NFL and NHL Collective Bargaining History

Before one can understand the gravity and significance of the terms and conditions of the current collective bargaining agreements in the NFL and NHL, it is important to take a brief look back at past agreements that have been negotiated between ownership and players' associations. These agreements have paved the way for the current collective bargaining relationship between players' associations and ownership and provide valuable insight into the circumstances that led to the current agreements.

1. Past NFL Collective Bargaining Agreements

Although collective bargaining in the NFL has been around since 1968[77], it was the 1993 agreement that was heralded as "a groundbreaking CBA that set the framework for every NFL CBA since."[78] The success of the 1993 CBA was evident when that agreement was extended three times—in 1998, 2001, and 2006—without any strikes, lockouts, or litigation between the parties ensuing.[79] The latest renewal of the 1993 CBA saw the agreement last until 2011, at which point the NFL and NFLPA went back to the bargaining table and, eventually, the courtroom.[80]

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projecting-the-impact-of-advancing-modern-medicine-on-the-nfl [http://perma.cc/2K8J-CML6] (noting the progress that modern medicine has made regarding injury research in sports and stating that "[t]he medical community now knows that concussions carry not only short-term, but also long-term, consequences. The age of 'shaking off' a blow to the head is forever over.").

74 Jason Fitzgerald, *Looking at the NFL Training Camp Holdouts*, OVER CAP (July 29, 2019), http://www.overthecap.com/nfl-training-camp-holdouts/ [http://perma.cc/3K7L-72KH].

75 *See* Yagman, *supra* note 71.

76 *See* Fitzgerald, *supra* note 74.

77 *See NFL labor history since 1968*, *supra* note 22.

78 Chris Deubert, et al., *All Four Quarters: A Retrospective and Analysis of the 2011 Collective Bargaining Process and Agreement in the National Football League*, 19 UCLA ENT. L. REV. 1, 12 (2012).

79 *See id.* at 13.

80 *See id.* at 14.

The rookie compensation scheme that we see today was a contentious issue in the 2011 negotiations.[81] Teams had begun choosing to give high-profile rookie players significant amounts of money[82], money that some felt was out of balance, believing that the money should instead be used to pay proven veterans.[83]

2. Past NHL Collective Bargaining Agreements

The 1995 NHL collective bargaining agreement ("1995 CBA") was the first to implement a cap on entry-level players or, as the agreement referred to them, "Group I players."[84] The 1995 CBA placed a prescribed contract length based on the age a player was when they signed their entry-level contract.[85] Players between the ages of eighteen and twenty-one were signed for a period of three years; players between the ages of twenty-two and twenty-three were signed for a period of two years; players that were twenty-four were signed for a period of one year, and there was no required number of years for players aged twenty-five or older, and those players were not in the entry-level system.[86]

The 1995 CBA also delineated the maximum NHL compensation that a player could earn that was contingent on the year they were drafted into the NHL.[87] The amount of any "signing, reporting and roster bonuses" was limited to no more than 50% of the maximum compensation allowed under Section 9.3(a).[88] Although the imposition of a salary cap on entry-level players was a "supposed major victor[y] for the league,"[89] a loophole existed that was exploited by savvy player agents.[90] Article 9.3(c) of the agreement stated that "nothing contained in this Section 9.3 shall be deemed to limit the amount permitted to be paid to any Group I Player in respect of any Exhibit 5

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81 *See id.* at 53.

82 *Rams give Bradford 50M guaranteed*, ESPN (July 31, 2010, 9:09 AM), http://www.espn.com/nfl/news/story?id=5425041 [http://perma.cc/SD89-TYJL].

83 *See Mawae: Big Rookie Contracts Like Ryans' 'Disheartening',* ESPN (May 21, 2008, 4:43 PM), http://espn.go.com/nfl/news/story?id=3406508 [http://perma.cc/4HMQ-E8D3].

84 *See* James Wilton Baillie, *An Examination of the Causes behind the Escalation of Player Compensation Between 1994 and 2004 Leading to the 2004–05 NHL Lockout*, QUEEN'S UNIV. INDUS. REL. CTR., 33 (August 2005), https://irc.queensu.ca/wp-content/uploads/articles/articles_investigation-into-the-collective-bargaining-relationship-between-nhl-nhlpa-1994-2005.pdf [http://perma.cc/GPQ2-V6LQ].

85 *See* Nat'l Hockey League, Collective Bargaining Agreement 1995–2004 at art. 9.1(b), (Jan. 13, 1995) http://www.letsgopens.com/nhl_cba-old.php?id=1 [http://perma.cc/5FJU-ZWTX].

86 *See id.*

87 *See infra* Appendix B.

88 Nat'l Hockey League, *supra* note 85 art. 9.3(b).

89 Baillie, *supra* note 84, at 33.

90 *Id.* at 34.

Performance Bonus(es)."[91] Among other things, Exhibit 5 allowed bonuses for meeting performance metrics such as ice time, goals scored, assists scored, and points scored.[92]

After a lockout caused the loss of the 2004–2005 NHL season, the NHL and NHLPA agreed on the 2005 collective bargaining agreement ("2005 CBA").[93] Most notably, the 2005 CBA was the first NHL CBA to include an overall salary cap on team salaries.[94] Like the 1995 CBA, the 2005 CBA also included the same prescribed length for entry-level contracts[95] and an entry-level compensation maximum based on the year in which the player was drafted,[96] although the compensation figure was scaled down dramatically from 1995 CBA figures.[97] A notable difference in the 2005 CBA was a stricter limitation on the signing and games-played bonus: Section 9.3(b) removed the reporting and roster bonuses, allowed entry-level players to only earn a signing and games-played bonus, and capped said bonuses at 10% of the player's Section 9.3(a) compensation.[98]

III. CURRENT STATE OF AFFAIRS: BAD FAITH NEGOTIATIONS DISPROPORTIONATELY IMPACT ROOKIES

A. Labor Law and Antitrust Exemptions in Sports

Antitrust law and collective bargaining—through federal labor law—are concepts that are in direct conflict with one another.[99] Simply put, "antitrust law promotes competition while labor law endorses activities that restrict it."[100] The Sherman Act, the main federal antitrust statute states: "Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States . . . is declared to be illegal."[101] The NFL and NHL—and other North

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91 Nat'l Hockey League, *supra* note 85, at art. 9.3(c).

92 *See id.* at Exhibit 5.

93 *See generally* CNN Library, *supra* note 61.

94 *See* Nat'l Hockey League, Collective Bargaining Agreement 2005–12 at art. 50.5(b), (July 22, 2005), http://www.letsgopens.com/NHL-2005-CBA.pdf [http://perma.cc/S7M2-JF2A].

95 *Id.* at art. 9.1(b).

96 *See infra* Appendix C.

97 *Compare infra* Appendix B with Appendix C.

98 *See* Nat'l Hockey League, *supra* note 94, at art 9.3(a)–(b). This number was down from the 50% allowable under the 1995 CBA.

99 *See* Wood v. Nat'l Basketball Ass'n, 809 F.2d 954, 959 (2d Cir. 1987).

100 *Antitrust Law – Nonstatutory Labor Exemption – Second Circuit Exempts NFL Eligibility Rules from Antitrust Scrutiny* – Clarett v. National Football League, 118 HARV. L. REV. 1379, 1379 (2005).

101 15 U.S.C. § 1 (2018).

American sports leagues—are, by their very nature, violations of antitrust laws.[102] The teams in these leagues "must cooperate on a business level to maintain competitive balance between them [and b]y cooperating economically instead of competing with one another, clubs are apparently violating antitrust laws."[103] This dichotomy has been addressed and minimized in two ways: the "statutory labor exemption"—codified as the Norris LaGuardia Act and Sections 6 and 20 of the Clayton Act—and the "non-statutory labor exemption."[104]

In *Connell Construction Co., Inc. v. Plumbers and Steamfitters Local Union No. 100*, the Supreme Court interpreted the statutory labor exemption statutes to mean that "labor unions are not combinations or conspiracies in restraint of trade, and exempt[s] specific union activities . . . from the operation of the antitrust laws."[105] The non-statutory labor exemption was first explored in the sports capacity in *Mackey v. National Football League*.[106] In *Mackey*, NFL players brought an antitrust challenge against the so-called Rozelle Rule, which permitted the Commissioner of the NFL to compensate a team losing the services of a player that was previously under contract with the said team by "nam[ing] and then award[ing] to the former club one or more players . . . of the acquiring club as the Commissioner in his sole discretion deem[ed] fair and equitable."[107] The Rozelle Rule was instituted not through collective bargaining, but was instead adopted by league owners as a unilateral amendment to the NFL Constitution.[108]

The *Mackey* court described the appropriateness of the non-statutory labor exemption by developing a three-prong test.[109] In order for the non-statutory labor exemption to apply, the restraint must (1) primarily affect only the parties to the collective bargaining agreement, (2) be a mandatory subject of collective bargaining, and (3) be the product of bona fide arm's length bargaining.[110] The court ruled that the Rozelle Rule met prongs one and two of the non-statutory exemption test, but failed on prong three as the court found the Rozelle Rule was not

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102 *See* Leah Farzin, *On the Antitrust Exemption for Professional Sports in the United States and Europe*, 22 JEFFREY S. MOORAD SPORTS L. J. 75, 75 (2015).

103 *Id.*

104 Feldman, *supra* note 25, at 8.

105 Connell Constr. Co., Inc. v. Plumbers and Steamfitters Local Union No. 100, 421 U.S. 616, 622 (1975).

106 Mackey v. Nat'l Football League, 543 F.2d 606 (8th Cir. 1976).

107 *Id.* at 610–11.

108 *Id.* at 610.

109 *Id.* at 614.

110 *Id.*

the product of arm's length negotiation.[111] In its opinion, the court stated that the Rule was unilaterally implemented by team owners *prior* to any collective bargaining agreement between league ownership and the players' union and found that there was a lack of sufficient evidence that the union had received reciprocal consideration.[112] Following the Eighth Circuit, a number of lower district courts and sister circuit courts adopted the *Mackey* test as the barometer for the non-statutory labor exemption.[113]

The Supreme Court took up the non-statutory labor exemption in the sports context in *Brown v. Pro Football, Inc.*, and closed up the holes that the statutory labor exemption did not immediately address.[114] *Brown* involved a challenge to the NFL's creation of a "developmental squad" of players that "would play in practice games and sometimes in regular games as substitutes for injured players."[115] When the players' association and the NFL could not agree on the wages and benefits of the development squad, the league unilaterally implemented the last best proposal.[116] In delivering the opinion of the Court, Justice Breyer succinctly stated the aim and purpose of the non-statutory labor exemption, stating:

> As a matter of logic, it would be difficult, if not impossible, to require groups of employers and employees to bargain together, but at the same time to forbid them to make among themselves or with each other *any* of the competition-restricting agreements potentially necessary to make the process work or its results mutually acceptable. Thus, the implicit exemption recognized that, to give effect to federal labor laws and policies and to allow meaningful collective bargaining to take place some restraints on competition imposed through the bargaining process must be shielded from antitrust sanctions.[117]

A particularly noteworthy sports antitrust case is *Clarett v. National Football League*, wherein Maurice Clarett, a former standout running back at Ohio State University, challenged the NFL's draft eligibility rules that required hopeful NFL players to wait three full football seasons after high school graduation before the player would be eligible to enter the NFL

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111 *Id.* at 615–16.

112 *Id.* at 616.

113 *See, e.g.*, Bridgeman v. Nat'l Basketball Ass'n, 675 F. Supp. 960, 964 (D.N.J. 1987); Cont'l Mar., Inc. v. Pac. Coast Metal Trades Dist. Council, 817 F.2d 1391, 1393 (9th Cir. 1987); McCourt v. Cal. Sports, Inc., 600 F.2d 1193, 1197-98 (6th Cir. 1979); Wood v. Nat'l Basketball Ass'n, 602 F. Supp. 525, 528 (S.D.N.Y. 1984); Zimmerman v. Nat'l Football League, 632 F. Supp. 398, 403–04 (D.D.C. 1986).

114 Brown v. Pro Football, Inc., 518 U.S. 231 (1996).

115 *Id.* at 234.

116 *Id.* at 235.

117 *Id.* at 237 (emphasis in original).

Draft.[118] Clarett was the first freshman to be listed as the starting running back for Ohio State since 1943, and he did not disappoint as he led the Buckeyes to a national championship that season.[119] Unfortunately for Clarett, that is where the positives stopped. Clarett was accused of receiving "preferential treatment" from Ohio State administrators,[120] "charged with misdemeanor falsification" of a police report,[121] and eventually suspended by Ohio State and the NCAA for accepting improper benefits before he played a single snap in his sophomore season.[122]

After his troubles at Ohio State, Clarett sought to enter the 2004 NFL Draft despite the NFL's three-year rule.[123] Clarett, who had graduated from high school in December 2001[124], posited that NFL teams were "horizontal competitors for the labor of professional football players and thus may not agree that a player will be hired only after three full football seasons . . . ."[125] In overturning the district court, the Second Circuit ruled that that the non-statutory labor exemption applied and that Clarett did not have antitrust standing to bring his claim, as doing so would usurp federal labor law policies.[126] Clarett's writ of certiorari was denied by the Supreme Court[127], and he was barred from entering the 2004 NFL Draft.[128] After he was forced to take a year off from football, Clarett eventually entered the 2005 NFL Draft where he was drafted 101st overall by the

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118 Clarett v. Nat'l Football League, 369 F.3d 124, 126 (2d Cir. 2004).

119 *Id.* at 126.

120 *See Timeline: The rise and fall of Maurice Clarett*, ESPN (Aug. 9, 2006), http://www.espn.com/nfl/news/story?id=2545204 [http://perma.cc/QSH4-LK8C] (quoting a teaching assistant at Ohio State, who said Clarett "walked out of a midterm exam but passed the class after the professor gave him an oral exam.").

121 *See id.* (stating that, in July of 2003, Clarett had claimed that "more than $10,000 in clothing, CDs, cash and stereo equipment was stolen in April" from a car Clarett had "borrowed from a local dealership." Less than two month later, he was facing charges for falsifying information.).

122 *See id.* (explaining that Ohio State athletic director Andy Geiger suspended Clarett one day after Clarett was charged by police, claiming that Clarett had "received special benefits worth thousands of dollars from a family friend and repeatedly misled investigators).

123 *Clarett*, 369 F.3d at 126.

124 *Id.*

125 *Id.* at 130.

126 *Id.* at 143.

127 Clarett v. Nat'l Football League, 369 F.3d 124 (2d Cir.), *cert. denied*, 544 U.S. 961 (2005).

128 In what can be described as adding insult to injury, when the 2011 NFL/NFLPA CBA was passed, Article 6, Section 2(b)–the provision which dealt with the three-year draft eligibility rule–gave an example to illustrate the rule with pointed similarities to Clarett's situation: "For example, if a player graduated from high school in December 2011, he would not be permitted to apply for special eligibility, and would not otherwise be eligible for selection, until the 2015 Draft." Nat'l Football League, *supra* note 5, at 17.

Denver Broncos.[129] Clarett was cut by the Broncos before ever playing a snap in the NFL.[130]

The *Clarett* case provides some rather pivotal language regarding prospective rookie players entering the NFL. Clarett had argued that the rules governing eligibility for prospective players were "an impermissible bargaining subject" due to their impact on those who had not been parties to the agreement, i.e. those college football players that were otherwise not members of the NFLPA.[131] In ruling on the eligibility rules, the court stated: "prospective players no longer have the right to negotiate directly with the NFL teams over the terms and conditions of their employment. That responsibility is instead committed to the NFL and the players union to accomplish through the collective bargaining process."[132] It is well settled that once a group of employees has unionized and selected an exclusive bargaining representative, negotiation privileges lie with the union and not with individual players.[133] However, the Second Circuit appears to be misconstruing the NFLPA's representation of the *prospective* players' interests.[134]

The preamble to the NFL/NFLPA collective bargaining agreement states that the agreement is between the "National Football League Management Council which is recognized as the sole and exclusive bargaining representative of present and future employer member Clubs of the National Football League" and the "[NFLPA]."[135] The NFLPA is the:

> Sole and exclusive bargaining representative of present and future employee players in the NFL in a bargaining unit described as follows:
>
> 1. All professional football players employed by a member club of the National Football League;
>
> 2. All professional football players who have been previously employed by a member club of the National Football League who are seeking employment with an NFL Club;

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129 *See 2005 Denver Broncos Draft*, FOOTBALL DATABASE, http://www.footballdb.com/teams/nfl/denver-broncos/draft/2005 [http://perma.cc/3DVF-5QQA] (last visited Apr. 3, 2020).

130 *See* John Clayton, *Broncos to release Maurice Clarett*, ESPN (Aug. 28, 2005), http://www.espn.com/nfl/news/story?id=2145372 [http://perma.cc/7TZZ-SK8B].

131 *Clarett*, 369 F.3d at 140.

132 *Id.* at 138.

133 *See National Labor Relations Act*, *supra* note 19.

134 *See* Matthew Strauser, *Upon Further Review: Reconsidering Clarett and Player Access to the NFL*, 29 MARQ. SPORTS L. REV. 247, 250 (2018).

135 Nat'l Football League, Collective Bargaining Agreement 2020 at xvi, http://nflpaweb.blob.core.windows.net/media/Default/NFLPA/CBA2020/NFL-NFLPA_CBA_March_5_2020.pdf [http://perma.cc/888P-B2GN] (last visited Mar. 25, 2020).

> 3. All rookie players *once they are selected* in the current year's NFL College Draft; and
>
> 4. All undrafted rookie players *once they commence negotiation* with an NFL Club concerning employment as a player.[136]

The plain language of the collective bargaining agreement negotiated and entered into by NFL Management Council and the NFLPA appears to explicitly exclude college players—or any other prospective player seeking to enter the league—from membership in the players' association until *after* they are selected in the "College Draft"[137] or until they begin negotiations with a team following the draft.[138] This notion is confirmed by an NFL player agent who states that "incoming [NFL] players aren't technically considered a part of the union."[139] On the other hand, the NHL/NHLPA CBA preamble states that the agreement is "between the National Hockey League . . . which is recognized as the sole and exclusive bargaining representative of the present and future Clubs of the NHL, and the National Hockey League Players' Association . . . recognized as the sole and exclusive bargaining representative of present and future Players in the NHL."[140]

Retired players are on the reciprocal end of the playing spectrum from rookies, and it has been said that "the NFLPA negotiates with the League on behalf of the active players, and the interests of the active players . . . are not consistent with that of the retired players insofar as the League offers a single compensation pie to the players, such that any slice allocated to the retired players results in a smaller slice for the active players."[141] Here, a direct comparison can be drawn between the interests of the active players and retired players not having their interests aligned and veteran (active) players not having their interests aligned with entering rookie players, in the same sense that any slice allocated to the rookies results in a smaller slice for the veteran players.

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136 *Id.* (emphasis added).

137 *See id.* The NFL-NFLPA CBA uses the phrase "College Draft" to mean the draft that a vast majority of players use as their method to enter the league, see discussion in Part II *infra*.

138 *See id.*

139 Joel Corry, *Agent's Take: Fixing the rookie wage scale, plus a look at its history and how it works*, CBS SPORTS (Apr. 24, 2019, 3:02 PM), http://www.cbssports.com/nfl/news/agents-take-fixing-the-rookie-wage-scale-plus-a-look-at-its-history-and-how-it-works [http://perma.cc/T5HU-WU4Z].

140 Nat'l Hockey League, *supra* note 72, at 1.

141 Eller v. Nat'l Football League Players Ass'n, 872 F. Supp. 2d 823, 834 (D. Minn. 2012).

The statutory and non-statutory labor exceptions provide us with a glimpse of the preference that labor law, via collective bargaining, is given over antitrust law when the two are at odds, especially in the sports context.[142] This deferment to labor law has been shown in numerous sports cases where courts have been reluctant to rule in favor of plaintiff-athletes' antitrust claims, instead opining that such claims are better left to the jurisdiction of the National Labor Relations Board as provided by federal labor law.[143] These decisions are "rooted in the observation that the relationships among the defendant sports leagues and their players were governed by collective bargaining agreements and thus were subject to the carefully structured regime established by federal labor laws."[144]

B. Current Collective Bargaining Agreements

With an understanding of applicable antitrust and labor laws, it is time to turn to the current collective bargaining agreements that govern the NFL and NHL today and examine how they limit rookie athletes seeking to enter the league. While the overarching goals are the same—establishing a framework that details the terms and conditions of employment—collective bargaining agreements in sports are as unique as the leagues themselves.[145] MLB players are not permitted to engage in pro boxing, but receive their own room on the road.[146] NHL players must have established significant service time to receive their own room, but receive six months of mortgage or rent coverage if they are traded.[147] NBA players only receive three months coverage if they are traded, but receive extra-long beds and porter baggage service on the road.[148] NFL players can be fined twice a week for being overweight, but cannot be disciplined for hair preferences.[149] A main point of difference in league collective bargaining agreements deals with the terms surrounding the rookie, or entry-level, contract.[150]

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142 Feldman, *supra* note 25, at 9.

143 *See* Nat'l Basketball Ass'n v. Williams, 45 F.3d 684, 693 (2d Cir. 1995) (noting "the soup-to-nuts" array of rules and remedies afforded under the labor laws).

144 *Clarett,* 369 F.3d at 135.

145 *See* Eric Macramalla, *Part 4 in A Series Comparing the CBAs: Weird & Quirky Clauses*, OFFSIDE SPORTS L. (Jan 31, 2011, 10:59 AM), http://offsidesportsblog.blogspot.com/2011/01/part-4-in-series-comparing-cbas-weird.html [http://perma.cc/4UH4-55ND].

146 *Id.*

147 *Id.*

148 *Id.*

149 *Id.*

150 *See generally* Andrew Brandt, *The Differences in Rookie Contracts*, NAT'L FOOTBALL POST, http://nationalfootballpost.com/the-differences-in-rookie-contracts/ [http://perma.cc/WJR9-CDRA] (last visited Apr. 20, 2020).

1. NFL/NFLPA

The NFLPA and NFL owners reached a new collective bargaining agreement on March 15, 2020.[151] This new agreement comes with one year remaining on the previous deal that was entered into in 2011 and runs through the 2030 NFL season.[152] Article 7 of the NFL/NFLPA collective bargaining agreement is entitled "Rookie Compensation and Rookie Compensation Pool."[153] For the purposes of this Article, the relevant portions of Article 7 of the CBA are the "Total Rookie Compensation Pool" and the "Year-One Rookie Compensation Pool" as explained in Section 2[154] and the "Rookie Contract Length" as explained in Section 3.[155]

Section 2 provides: "For the 2020 League Year, Total Rookie Compensation Pool . . . may not exceed $1,430,000,000 [and] The Year-One Rookie Compensation Pool . . . shall equal $260,000,000."[156] Section 2 continues with a complicated formula for computing the increase(s) in the Total Rookie Compensation Pool and the Year-One Rookie Compensation Pool.[157] In addition to the amount of compensation to be afforded under Section 2, Section 3 provides:

> Every Rookie Contract shall have a fixed and unalterable contract length: (i) four years for Rookies selected in the first round of the Draft, with a Club option for a fifth year as described in Section 7 below; (ii) four years for Rookies selected in rounds two through seven of the Draft (including any compensatory draft selections); and (iii) three years for Undrafted Rookies.[158]

The full NFLPA membership vote on the passage of the new 2020 NFL/NFLPA collective bargaining agreement was very close, passing by a vote of 1,019 to 959.[159] The ratification of the agreement, which was proposed to the players by team owners, was a hot button topic in the football world and one that divided players in the league.[160] Many in the football community, players and pundits alike, thought that the players were giving up too

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151 *See* Grant Gordon, *NFL player vote ratifies new CBA through 2030 season*, NFL (Mar. 15, 2020, 1:01 PM), http://www.nfl.com/news/story/0ap3000001106246/article/nfl-player-vote-ratifies-new-cba-through-2030-season [http://perma.cc/5JHV-R9EX].

152 *See generally id.*

153 Nat'l Football League, *supra* note 135, at art. 7.

154 *Id.* at art. 7 § 2.

155 *Id.* at art. 7 § 3.

156 *Id.* at art. 7 § 2.

157 *Id.*

158 *Id.* at art. 7 § 3.

159 Gordon, *supra* note 151.

160 *See* Jordan Heck, *NFL CBA vote: Tracking which players are voting 'yes' and 'no'*, SPORTING NEWS (Mar. 11, 2020), http://www.sportingnews.com/us/nfl/news/nfl-cba-vote-players-tracker-yes-no/dqf1q13xwyau1m40illiiattr [http://perma.cc/22G4-X3DE].

much to the owners—including the addition of a 17th regular season game—by accepting the very first offer the owners proposed.[161]

Despite some significant changes to parts of the collective bargaining agreement, the structure of the rookie compensation article in the new 2020 agreement retains the same substantive information that was included in the 2011 agreement, with the 2020 agreement adding additional language.[162] Interestingly, some of the players who were the most outspoken against the proposed collective bargaining agreement included established superstar players such as Russell Wilson, Aaron Rodgers, JJ Watt, and Richard Sherman, who felt that the players were being taken advantage of by team owners.[163] In a tweet to his followers indicating his stance on the issue, Russell Wilson drew comparisons to the NBA and MLB agreements that put the players first and said that "ALL @NFL players deserve the same."[164]

2. NHL/NHLPA

The most recent collective bargaining agreement between NHL owners and the NHLPA was ratified on January 12, 2013.[165] Much like the NFL/NFLPA agreement, the NHL/NHLPA agreement places strict guidelines on rookie contracts, or "entry level" contracts as they are referred to by the NHL.[166] Unlike the NFL, the NHL determines the length of an entry-level contract based on the player's age when the contract is signed.[167] The signing age parameters are the same as they have been in the previous two NHL CBAs: players between the ages of eighteen and twenty-one are signed for three years; players between the

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161 *See generally id.*; Dan Graziano, *NFL CBA approved: What players get in new deal, how expanded playoffs and schedule will work*, ESPN (Mar. 15, 2020), http://www.espn.com/nfl/story/_/id/28901832/nfl-cba-approved-players-get-new-deal-how-expanded-playoffs-schedule-work [http://perma.cc/9M6U-U6N7].

162 *Compare* Nat'l Football League, *supra* note 5, *with* Nat'l Football League, *supra* note 135 at art. 7 (showing that additions were made to the 2020 agreement that were not present in the 2011, primarily in the form of the calculations used to compute the relevant figures discussed; dates used in the 2011 agreement were updated to reflect the new time frame that would be covered by the 2020 agreement and baseline dollar amounts were updated to reflect the new financial position of the NFL and NFLPA at the time the 2020 agreement was proposed and agreed upon.).

163 Jordan Heck, *NFL players think the proposed CBA by owners is awful: 'Rip it up!'*, SPORTING NEWS (Feb. 26, 2020), http://www.sportingnews.com/us/nfl/news/nfl-players-cba-owners/jcr7tof3e21s15wjh4bqzbo3h [http://perma.cc/LPD4-RZ99].

164 Russell Wilson (@DangeRussWilson), TWITTER (Feb. 26, 2020, 7:16 AM), http://twitter.com/DangeRussWilson/status/1232685882915872769.

165 *Union ratifies new CBA*, NHL (Jan. 12, 2013), http://www.nhl.com/news/union-ratifies-new-cba/c-649889 [http://perma.cc/M6XV-JGR6].

166 Nat'l Hockey League, *supra* note 72, at 23.

167 *Id.*

ages of twenty-two and twenty-three are signed for two years; players who are twenty-four are signed for one year, and players twenty-five and older are not subject to the entry-level system.[168] For age calculation purposes, a player's age is determined as of his "age on September 15 of the calendar year in which he signs [a contract], regardless of his actual age on the date he signs."[169]

Unlike the formula used by the NFL/NFLPA, the NHL/NHLPA collective bargaining agreement allots a set compensation based on the year the player was drafted, with no consideration to where in the draft the player was taken.[170] Players drafted in 2005 or 2006 receive $850,000 per year; players drafted in 2007 or 2008 receive $875,000 per year; players drafted in 2009 or 2010 receive $900,000 per year, and players drafted from 2011 to 2022, the entire length that this collective bargaining agreement covers, will receive $925,000 per year under their entry-level contract.[171]

C. Rookie and Entry-Level Players are Not Adequately Represented

When it comes time to negotiate with the leagues and their ownership groups on collective bargaining agreements, players' associations turn to their leadership: the executive board and the player representatives from each league team.[172] Every NFL and NHL team elects one player representative to serve on their respective players' association.[173] The tables in Appendix D and Appendix E detail the designated player representative for each NFL and NHL team, respectively.[174] The column on the far right side of each table indicates the number of years that the player has been in the league for purposes of determining if that particular player is on their rookie, or entry-level, contract.[175]

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168 *Id.*

169 *Id.* at 24.

170 *Id.*

171 *Id.* at 24–25.

172 *See generally* Chris Bumbaca, *What we know about proposed NFL collective bargaining agreement, timeline of talks*, USA TODAY (Feb. 26 2020, 10:49 AM), http://www.usatoday.com/story/sports/nfl/2020/02/26/nfl-collective-bargaining-agreement-facts-deal-details-players-association/4878534002/ [http://perma.cc/S9PG-5PSU].

173 *See Board of Player Representatives*, NFL PLAYERS' ASSOC., http://www.nflpa.com/about/nflpa-officers#board [http://perma.cc/X9T7-QMUS] (last visited Apr. 10, 2020); *see also Executive Board*, NHL PLAYERS' ASSOC., http://www.nhlpa.com/the-pa/executive-board [http://perma.cc/9SE9-8YD8] (last visited Apr. 10, 2020).

174 *See infra* Appendix D; *see also infra* Appendix E.

175 *See infra* Appendix D; *see also infra* Appendix E.

NFL teams most recently selected their player representatives in the fall of 2018.[176] Of the players serving as player representatives for NFL teams, only one of the thirty-two player representatives—Ronnie Stanley of the Baltimore Ravens—was playing under the terms of his rookie contract when he was selected to be a player representative.[177] Christian Wilkins, the youngest player representative in terms of years of experience, was not yet drafted as a member of the Miami Dolphins during the last general election for player representatives,[178] but was selected when the original Dolphins player representative and alternates were traded or released from the team.[179] Of the NHL player representatives, only one of the thirty-one player representatives—Brady Tkachuk of the Ottawa Senators—is playing under the terms of his entry-level contract.[180] Although Matt Roy of the Los Angeles Kings is only in his third season in the NHL, he signed his entry-level contract at age 22 and thus that contract had a two-year term.[181]

Both the NFLPA and NHLPA Constitutions codify this barrier to player representation in their association bylaws. The NFLPA Constitution requires that "[i]n order to be eligible for election or temporary appointment as a Player Representative or Co-Alternate Player Representative, a person must have been a member in good standing of the NFLPA for at least one (1) year prior to his election or appointment."[182] The NHLPA Constitution

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176 *See Board of Player Representatives*, *supra* note 173.

177 *See infra* Appendix D.

178 *Christian Wilkins*, NFL, http://www.nfl.com/prospects/christian-wilkins/32195749-4c08-1088-ad8a-aada01ec7ce9 [http://perma.cc/4WNN-HLA2] (last visited Apr. 17, 2020) (showing that Wilkins was drafted with the 13th overall pick in the 2019 NFL Draft).

179 *See* NFLPA (@NFLPA), TWITTER (Oct. 21, 2018, 9:00 AM), http://twitter.com/NFLPA/status/1054039680197509121 [http://perma.cc/CA3J-AGVM]; *see also* Herbie Teope, *Dallas Cowboys trade for Dolphins DE Robert Quinn*, NFL (Mar. 28, 2019, 3:28 AM), http://www.nfl.com/news/dallas-cowboys-trade-for-dolphins-de-robert-quinn-0ap3000001024615 [http://perma.cc/QAF9-LL8K]; *see also* Josh Alper, *Dolphins release Ted Larsen, Andre Branch*, PRO FOOTBALL TALK (Mar. 7, 2019, 4:18 PM), http://profootballtalk.nbcsports.com/2019/03/07/dolphins-release-ted-larsen-andre-branch/ [http://perma.cc/NLY6-DXUQ]; *see also* Kevin Nogle, *Dolphins cut John Denney*, SB NATION (Sept. 2, 2019, 10:14 AM), http://www.thephinsider.com/2019/9/2/20844435/dolphins-cut-john-denney [http://perma.cc/6R45-GQSZ]; *see also* Kevin Patra, *Texans trade for Dolphins' Laremy Tunsil, Kenny Stills*, NFL (Aug. 31, 2019, 7:24 AM), http://www.nfl.com/news/texans-trade-for-dolphins-laremy-tunsil-kenny-stills-0ap3000001045889 [http://perma.cc/6FVD-92H4].

180 *See infra* Appendix E.

181 *Matt Roy*, CAPFRIENDLY, http://www.capfriendly.com/players/matt-roy [http://perma.cc/96L3-F5JB] (explaining that Roy's 2019–20 contract was negotiated freely by him and his agent).

182 *NFL Players Ass'n Constitution*, NFL PLAYERS' ASS'N (Mar. 2017), http://nflpaweb.blob.core.windows.net/media/Default/PDFs/NFLPAConstitution2017.pdf [http://perma.cc/CL5Y-ZPCY].

takes this even further by requiring that player representatives must "have been on an NHL Club roster for at least 160 games."[183]

The discrepancy in the years of experience is undoubtedly apparent when it comes to the bargaining tables and the collective bargaining agreements that result therefrom. As was discussed in Part II.B, the salary cap structure of the NFL and the NHL exists to promote parity in the leagues and to avoid the wealthier teams from overspending.[184] With that limiting number in mind, there is only a finite amount of money that teams are permitted to spend. Limiting the compensation that is permitted to be paid to players entering the league guarantees that there is a higher percentage of the salary cap to be had by the veteran players. Without equality of representation on either the player representative staff or the association executive boards, there are no incentives for the interests of the continuous stream of incoming talent. To be certain, those that serve as veterans realize the inequality that they had to overcome as rookies, and now that they are in a more preferential position, they are certainly not going to give up less of their own rights to benefit the incoming class. Inevitably, that cycle repeats itself in perpetuity.

D. Unequal Position Runs Afoul of Policy Concerns Behind the Passage of the NLRA

Ingrained in the passage of the NLRA were underlying policy concerns that justify such action.[185] In enacting the NLRA, Congress realized that inherent differences in the "bargaining power between employees who do not possess full freedom of association or actual liberty of contract, and employers who are organized in the corporate or other forms of ownership association substantially burdens and affects the flow of commerce . . . by depressing wage rates."[186] It was well understood that protecting employees' rights to organize was important to the commerce and the hopes of resolving disputes that arose between employers and employees.[187]

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183 *Constitution of the Nat'l Hockey League Players' Ass'n*, NAT'L HOCKEY LEAGUE PLAYERS' ASS'N, http://ipmall.law.unh.edu/sites/default/files/hosted_resources/SportsEntLaw_Institute/League%20Constitutions%20&%20Bylaws/nhlpa_constitution.pdf [http://perma.cc/NR76-LWBZ] (last visited May 4, 2020).

184 *See Collective Bargaining Agreements in Sports, supra* note 38.

185 *See* 29 U.S.C. §151 (2018).

186 *Id.*

187 *See id.*

The policy concerns were not solely limited to protection of employees but included protection from unwanted practices by unions.[188] In realizing that labor unions could take damaging action like employers, it was said:

> Experience has further demonstrated that certain practices by some labor organizations, their officers, and members have the intent or the necessary effect of burdening or obstructing commerce by preventing the free flow of goods in such commerce through . . . concerted activities which impair the interest of the public in the free flow of such commerce. *The elimination of such practices is a necessary condition to the assurance of the rights herein guaranteed.* It is hereby declared to be the policy of the United States to eliminate the causes of certain substantial obstructions to the free flow of commerce.[189]

However, despite these issues being plainly obvious over eighty years ago, it is these very practices that are rearing their heads today and causing the exact havoc that was sought to be eliminated. The NFLPA and NHLPA, through their representation comprised almost entirely of veteran players no longer concerned with the plight of the rookie, have engaged in practices that have the "effect of burdening or obstructing commerce" by preventing the free flow of goods—in this context, players services—through their unreasonable control of rookie salaries.[190] The plain language of the NLRA indicating the policy justifications for a lack of "obstructions to the free flow of commerce" can certainly be found to extend to services where those services themselves form the basis of the commerce in question.[191]

IV. GOOD FAITH BARGAINING AND FAIR REPRESENTATION FOR ALL

In order for there to be true pay equity in these professional sports leagues, the arbitrary maximum cap placed on rookie or entry-level contracts must be abolished. This Article proposes that any restrictions on rookie or entry-level contract earnings be abolished in any new collective bargaining agreements moving forward. This is not to suggest that every rookie or entry-level player should be making comparable salaries to those proven veterans, but rather that they have the *ability* to do so and are not otherwise unduly burdened by a blanket cap on their contracts merely based on their tenure status.

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188 *See id.*
189 *Id.* (emphasis added).
190 *Id.*
191 *See generally id.*

This Article is hardly the first to propose that the rookie wage structure, as it is currently structured, needs re-working.[192] The rookie wage structure that is now in place has been called "an overcorrection to how incoming players were previously compensated."[193] It has previously been suggested that the amount of time an NFL player is under his rookie contract can be shortened by one year—moving from five years to four years for first-round picks, from four to three years for other draftees, and from three to two years for undrafted players.[194] Under previous proposals, players would be able to renegotiate their rookie contracts one year earlier and the negotiation window would open following the second year of the contract, as opposed to the third.[195] However, these minor tweaks to an already-broken system do not adequately fix the problem and also discount the tremendous success that players on rookie or entry-level contracts are having in recent years.

The NFL's role in this rookie wage problem is two-fold. First, the discussion in Part III.A above shows that there appears to be a very strong case that college athletes or other prospective NFL players are in fact not members of the NFLPA. This would appear to open the possibility that antitrust claims, potentially brought by the prospective players, would not be protected by the non-statutory labor exemption, based on the tests that circuit courts have developed in past opinions. Second, and alternatively, if the prospective players are deemed to be subject to the conditions of the CBA, the disparate treatment that they receive by virtue of being a new player in the league should be a ripe scenario for a duty of fair representation claim with the NLRB. The NFLPA is far from a bargaining unit that is above reproach and a recent claim by current NFL player Russell Okung accuses NFLPA Executive Director DeMaurice Smith with making threats of retaliation regarding players being outspoken against the recently ratified 2020 NFL/NFLPA CBA.[196]

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192 *See generally* Corry, *supra* note 139; Joel Corry, *Agent's Take: Here's how the NFL would look if the rookie wage scale didn't exist*, CBS Sports (Apr. 24, 2018, 7:00 AM), http://www.cbssports.com/nfl/news/agents-take-heres-how-the-nfl-would-look-if-the-rookie-wage-scale-didnt-exist/ [http://perma.cc/UQF4-B33W].

193 Corry, *supra* note 192.

194 *Id.*

195 *Id.*

196 *See* Gregg E. Clifton, *NFL Players Association Executive Committee Member Files ULP Against Own Union and Its Leaders*, NAT'L L. REV. (Mar. 10, 2020), http://www.natlawreview.com/article/nfl-players-association-executive-committee-member-files-ulp-against-own-union-and [http://perma.cc/Q475-AP7X].

Young NFL and NHL players entering the league are not given adequate representation to ensure that their needs have a fair shot of being met and, in fact, history has provided us with examples of the exact opposite: player representatives are explicitly outspoken in their desire to throttle down the earning capacity of select members of the group they are elected to represent, merely because they are new to the league.[197] This is quite clearly a breach of the duty of fair representation and the "statutory obligation to serve the interests of *all* members without hostility or discrimination toward any."[198] Instead of focusing on pumping up veteran players and their salaries by evidencing how they have proven themselves, the NFLPA and NHLPA seem intent on bringing rookie compensation down in a manner akin to the "cycles of abuse" of hazing where "members model for new members the accepted methods for initiation" which—in this scenario—is artificially throttled salaries.[199]

Whatever the initial reasons or justifications for the rookie salaries in both the NFL and NHL, there are even stronger arguments for its removal. Rookie players are enjoying tremendous success in recent years, winning awards for both league[200] and Super Bowl most valuable player honors.[201] One need look no further than MLB for a sports world example with no maximum rookie contracts.[202] MLB, as mentioned earlier in this Article, does not have a hard salary cap and there is also no

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197 *See Mawae: Big Rookie Contracts Like Ryans' 'Disheartening'*, *supra* note 83; *see generally* Liz Mullen, *The making of a union*, SPORTS BUS. J. (Jan. 23, 2017), http://www.sportsbusinessdaily.com/Journal/Issues/2017/01/23/Labor-and-Agents/NHLPA.aspx [http://perma.cc/9T6R-BX24].

198 Vaca v. Sipes, 386 U.S. 171, 177 (1967).

199 *Why do groups haze members?*, ELON U., http://www.elon.edu/u/hazing/facts/theories-research/ [http://perma.cc/D8MC-6QCZ] (last visited Apr. 29, 2020).

200 *AP NFL Most Valuable Player Winners*, PRO FOOTBALL REFERENCE, http://www.pro-football-reference.com/awards/ap-nfl-mvp-award.htm [http://perma.cc/96MY-UYRU] (last visited May 4, 2020) (showing that Cam Newton in 2015, Patrick Mahomes in 2018 and Lamar Jackson in 2019 were all on their rookie contracts when they were voted most valuable player); *see also NHL Hart Memorial Trophy Winners*, HOCKEY REFERENCE, http://www.hockey-reference.com/awards/hart.html [http://perma.cc/B4MQ-DAX9] (last visited May 4, 2020) (showing that Sidney Crosby in 2006–07 and Connor McDavid in 2016–17 were on their entry-level contracts when they won the Hart Memorial Trophy for NHL most valuable player).

201 *NFL History – Super Bowl MVPs*, ESPN, http://www.espn.com/nfl/superbowl/history/mvps [http://perma.cc/6F2F-LAXN] (last visited May 4, 2020) (stating that Von Miller in Super Bowl 50 and Patrick Mahomes in Super Bowl LIV were on their rookie contracts when they were awarded Super Bowl most valuable player).

202 *See* Andrew Brandt, *The Differences in Rookie Contracts*, NAT'L FOOTBALL POST, http://nationalfootballpost.com/the-differences-in-rookie-contracts/ [http://perma.cc/5YHW-LW8U] (last visited May 1, 2020).

limit on the amount that teams are permitted to pay their incoming players.[203] Instead, the MLB league office provides clubs with recommendations for signing bonuses and overall compensation for rookies.[204] These figures are merely suggestions that teams can choose to follow or not, but this format does provide for highly-talented players entering the league to have a fighting chance to earn themselves appropriate money right off the bat.[205] It is the "truest free-market application to [the] selection process, giving players at the top leverage (whether real or perceived) to negotiate without any of the parameters imposed by the [rookie] caps of the other sports."[206]

A related industry for comparison to professional athletes is the television and film industry. Here, like in professional sports, the most in-demand talent can be of any age and it is not uncommon for younger talent to be wildly successful, sometimes even more so than individuals that have been in the business for longer periods of time. These television and film personalities are represented by the Screen Actors Guild – American Federation of Television and Radio Artists ("SAG-AFTRA").[207] SAG-AFTRA is the unionized representative body of "approximately 160,000 actors, announcers . . . and other media professionals."[208] The union is responsible for "negotiating the best wages, working conditions and health and pension" benefits for its members.[209]

Those in charge of movies and television shows are very familiar with the salary cap-like implications of their projects: working talent salaries under budgets. While the comparison is not completely apples-to-apples, there is a logical nexus between the salary caps in sports and the budgets that film and television producers must work under.[210] The sums of money paid to television and film talent—including a specialized film industry salary that involves a portion of the profits of a film—is said to be "Hollywood's version of a salary cap."[211] Similar to sports contracts, there are a number of

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203 *See id.*

204 *See id.*

205 *See id.*

206 *Id.*

207 *About*, SAG-AFTRA, http://www.sagaftra.org/about [http://perma.cc/8EAL-52CB] (last visited Apr. 17, 2020).

208 *Id.*

209 SAG-AFTRA, Constitution of the Screen Actors Guild – American Federation of Television and Radio Artists, 1 (Oct. 11, 2019), https://www.sagaftra.org/files/sa_documents/2019%20Constitution%20-%20Updated%20Rules%202020%201214.pdf [http://perma.cc/N7Z8-4Z5F].

210 Tim Ryan, *Who's who on a film set?*, TAR PROD., http://tarproductions.com/whos-who-on-a-film-set/ [http://perma.cc/D4RU-AQGG] (last visited May 4, 2020).

211 John Horn, *Hollywood Studios Rewriting Pay System for Their Talent*, L.A. TIMES (Jan. 13, 2006), http://www.latimes.com/archives/la-xpm-2006-jan-13-fi-gross13-story.html [http://perma.cc/955S-CTHZ].

additional benefits that can be negotiated into an actor's contract.[212] Much like securing a top-end sports talent can favor a franchise on the field or at the gate, "[s]ecuring a proven movie star is one way to guarantee ticket sales."[213]

One major difference between SAG-AFTRA and the NFL/NFLPA and NHL/NHLPA collective bargaining agreements deals with compensation. Article XI of the SAG-AFTRA Constitution deals with collective bargaining.[214] Despite the fact that SAG-AFTRA represents union members that must abide by the financial restrictions imposed by television and film budgets, there is a provision in the union constitution that explicitly prevents the union from artificially capping the amount of money to be made by a member: Subsection D Article XI states that "[t]he Union shall not negotiate or seek to regulate the maximum compensation that may be earned by any member under any collective bargaining agreement."[215] This is in direct contrast to what is present in both the NFL/NFLPA and NHL/NHLPA collective bargaining agreements.[216] Similar to television and film budgets that may vary from project to project, the NFL and NHL agreements are both silent on the exact salary cap figure on a year-to-year basis.[217] However, these agreements both specifically limit what certain members of their respective unions—rookies or entry-level players—are permitted to make,[218] while providing minimum amounts that preferred members of their unions—veteran members—are required to make.[219]

An ancillary benefit of allowing rookie or entry-level compensation to be negotiated on a case-by-case basis allows the players to account for income tax considerations.[220] Tax implications are a necessary evil of all professional sports contracts, but mandating that players be required to earn a predetermined amount, regardless of location, does an injustice

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212 Margaret Heidenry, *How Hollywood Salaries Really Work*, VANITY FAIR (Feb. 12, 2018), http://www.vanityfair.com/hollywood/2018/02/hollywood-movie-salaries-wage-gap-equality [http://perma.cc/LD8T-TV4P].

213 *Id.*

214 SAG-AFTRA, *supra* note 209, at 37.

215 *Id.* at 38.

216 *See generally* Nat'l Football League, *supra* note 135; Nat'l Hockey League, *supra* note 72.

217 *See* Nat'l Football League, *supra* note 135, at art. 13; Nat'l Hockey League, *supra* note 72, at art. 50.

218 *See* Nat'l Football League, *supra* note 135, at art. 7; Nat'l Hockey League, *supra* note 72, at art. 9.

219 *See* Nat'l Football League, *supra* note 135, at art. 9; Nat'l Hockey League, *supra* note 72, at art. 10.

220 Jeff Bowes, *Major Penalty for High Taxes,* AMS. FOR TAX REFORM 20 (Sept. 2015), http://www.taxpayer.com/media/MajorPenalty-October2015.pdf [http://perma.cc/PH9N-Y6LZ].

to those players who play for teams in states with higher state income tax. For example, taking the CBA-mandated $925,000 entry-level salary for an NHL player drafted in the 2019 NHL Draft, a player drafted to one of the league's three California based teams—the Anaheim Ducks, the Los Angeles Kings, or the San Jose Sharks—would pay a top marginal tax rate of 13.3%[221] and an effective tax rate of roughly 10.6%.[222] When these figures are contrasted to states like Florida, Nevada, and Texas—all of which have NHL teams that have no state income tax—it is calculated that playing in a low or no-tax state can effectively save players that play in those states up to $90,000 per year. The actual computation of an athlete's tax return is much more convoluted than this brief example as athletes must generally file taxes in each state in which they work throughout the year.[223] Nevertheless, the amount an athlete saves in taxes from playing a majority of their games in a low state-tax state is far from negligible and certainly comes into play when veteran free agents consider signing subsequent contracts with teams.[224] Under the proposal that this Article proffers, a player who was selected to play for a team in a state with a higher tax rate would be able to factor that into his—and his agent's—negotiations with a team so that the player was not at a disadvantage relative to his peers in lower-rate states.

Simply put, the proposal that rookie or entry-level contracts should not have an artificially imposed maximum on them forces the team owners to be businessmen and make good business deals. With some, if not most, NFL and NHL owners' net worth being measured in billions as opposed to millions, making good business deals is not out of the question for them. Allowing players the opportunity to earn more than a prescribed maximum does not mean that owners will be forced to empty their bank accounts for unproven rookies each and every time, it merely affords the players who are worth more to earn their fair

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221 *See* Katherin Loughead, *State Individual Income Tax Rates and Brackets for 2021* at 6, TAX FOUND. (Feb. 2021), http://files.taxfoundation.org/20210217114725/State-Individual-Income-Tax-Rates-and-Brackets-for-2021.pdf [http://perma.cc/HP7Z-MKG5].

222 *See, e.g.*, *California Income Tax Calculator*, SMARTASSET, http://smartasset.com/taxes/california-tax-calculator [http://perma.cc/P4FN-A872] (last visited May 6, 2020).

223 *See generally* John Calvin, *Itching for the Jock Tax*, AM. SPECTATOR (June 1, 2016, 12:00 AM), http://spectator.org/itching-for-the-jock-tax/ [http://perma.cc/N2PT-J64G]. This brief tax calculation does not take into account any standard or itemized deductions that might be available to the athlete or if they file jointly with a spouse.

224 *See generally* Bowes, *supra* note 220; Ryan Lake, *Mark Stone Hit The Tax Jackpot With Trade To Vegas Golden Knights*, FORBES (Mar. 7, 2019, 9:00 AM), http://www.forbes.com/sites/ryanlake/2019/03/07/mark-stone-hits-the-tax-jackpot-in-vegas/#6842267c748c [http://perma.cc/DS4G-NUKA].

share faster. In turn, this leads to increased player satisfaction and loyalty, increased productivity on the field of play, and a better feel for fans of the team who do not have to witness their favorite player sitting out. Allowing young players their shot to earn a fair salary ultimately benefits all interested parties.

V. CONCLUSION

Professional athletes have a finite amount of time to cash in on the earning potential that they spent their entire lifetime building. With the developments of modern medicine giving us a glimpse into just how much damage these young men do to their bodies, it is more important than ever that athletes utilize the very limited time they have to the fullest. Rookie or entry-level players that are forced to take less than fair-market value for their services while they earn their places in the league is a disservice to the blood, sweat, and tears that professional athletes put into their careers. The barriers to entry to a career in professional sports are some of the highest in North America on their own, and these barriers should not be made artificially higher due to players' associations negotiating in bad faith and not fairly representing a certain class of members in their unions.

Although recent holdouts have been met with mixed results from critics,[225] it is clear that the players who make the calculated risk to sit out for days, weeks, or months at a time are doing so with the notion that the value of services they provide to their respective teams is vastly underappreciated by ownership. Simply put, these players deserve better. They deserve better from team owners and they especially deserve better from their players' associations—the very people that are supposed to be in their corner, fighting for their best interests.

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225 *Compare* Jesse Washington, *Le'Veon Bell is smarter than you think*, UNDEFEATED (Nov. 14, 2018), http://theundefeated.com/features/leveon-bell-pittsburgh-steelers-is-smarter-than-you-think/ [http://perma.cc/9V7W-KZHE], with Mike Tanier, *Le'Veon Bell's Holdout Has Become a Historic Disaster…for Le'Veon Bell*, BLEACHER REP. (Nov. 6, 2018), http://bleacherreport.com/articles/2804597-leveon-bells-holdout-has-become-a-historic-disasterfor-leveon-bell [http://perma.cc/8PUQ-8SWH].

Appendix A

Salary Inequality and Parity Comparison in Major Professional Sports[226]

League	"Fairness Metric" Rank	"Fairness Metric" Raw Ratio
NFL[227]	5 of 18	1.38:1
NBA[228]	6 of 18	1.98:1
NHL[229]	7 of 18	2.30:1
MLB[230]	9 of 18	3.53:1
Premier League (England)[231]	12 of 18	6.82:1
Serie A (Italy)[232]	13 of 18	16:1
La Liga (Spain)[233]	15 of 18	19:1
Bundesliga (Germany)[234]	16 of 18	20.5:1
Ligue 1 (France)[235]	18 of 18	26.6:1

226 *See generally Global Sports Salaries Survey 2018*, *supra* note 51.
227 *Id.* at 58.
228 *Id.* at 42.
229 *Id.* at 66.
230 *Id.* at 50.
231 *Id.* at 54.
232 *Id.* at 70.
233 *Id.* at 62.
234 *Id.* at 74.
235 *Id.* at 78.

Appendix B

1995 NHL CBA Entry-Level Compensation by Draft Year[236]

Draft Year	NHL Compensation
1995	US$ 850,000
1996	US$ 875,000
1997	US$ 925,000
1998	US$ 975,000
1999	US$ 1,025,000
2000	US$ 1,075,000
2001	US$ 1,130,000
2002	US$ 1,185,000
2003	US$ 1,240,000
2004	US$ 1,295,000

Appendix C

2005 NHL CBA Entry-Level Compensation by Draft Year[237]

Draft Year	NHL Compensation
2005	US$ 850,000
2006	US$ 850,000
2007	US$ 875,000
2008	US$ 875,000
2009	US$ 900,000
2010	US$ 900,000
2011	US$ 925,000
2012[238]	US$ 925,000

236 Nat'l Hockey League, *supra* note 85, at art. 9.3(a).

237 Nat'l Hockey League, *supra* note 94, at art. 9.3(a).

238 *Id.* ("If the NHLPA exercises its right to extend this Agreement until 2012, the maximum annual aggregate Paragraph 1 NHL Salary . . . shall be U.S. $925,000.").

Appendix D[239]

NFLPA Player Representatives

Team	Player Representative	Years in League[240]
Arizona Cardinals	Corey Peters	10 years
Atlanta Falcons	Josh Harris	8 years
Baltimore Ravens	Ronnie Stanley	4 years
Buffalo Bills	Patrick DiMarco	8 years
Carolina Panthers	Greg Van Roten	8 years
Chicago Bears	Chase Daniel	10 years
Cincinnati Bengals	Geno Atkins	10 years
Cleveland Browns	Jarvis Landry	6 years
Dallas Cowboys	Byron Jones	5 years
Denver Broncos	Brandon McManus	6 years
Detroit Lions	Devon Kennard	6 years
Green Bay Packers	Aaron Rodgers	15 years
Houston Texans	Brennan Scarlett	4 years
Indianapolis Colts	Clayton Geathers	5 years
Jacksonville Jaguars	Calais Campbell[241]	12 years
Kansas City Chiefs	Dustin Colquitt	15 years
Las Vegas Raiders	Rodney Hudson	9 years
Los Angeles Chargers	Mike Pouncey	9 years
Los Angeles Rams	Todd Gurley[242]	5 years
Miami Dolphins	Christian Wilkins	1 year
Minnesota Vikings	Adam Thielen	6 years
New England Patriots	Matt Slater	12 years
New Orleans Saints	Craig Robertson	8 years
New York Giants	Nate Solder	9 years
New York Jets	Quincy Enunwa	6 years
Philadelphia Eagles	Malcolm Jenkins	11 years

239 *Board of Player Representatives*, *supra* note 173.

240 *See, e.g.*, *2020 NFL Players*, FOX SPORTS (last visited May 16, 2020), http://www.foxsports.com/nfl/players [http://perma.cc/P9NJ-XB46] (showing experience calculations conducted by the author accurate as of the conclusion of the 2019 NFL season).

241 *See* Nick Shook, *Jaguars to trade DE Calais Campbell to* Ravens, NFL (Mar. 15, 2020, 2:38 AM), http://www.nfl.com/news/jaguars-to-trade-de-calais-campbell-to-ravens-0ap3000001106265 [http://perma.cc/ETF7-SNFZ].

242 *See* Kevin Patra, *Rams release former OPOY, standout Todd* Gurley, NFL (Mar. 19, 2020, 5:48 AM), http://www.nfl.com/news/rams-release-former-opoy-standout-todd-gurley-0ap3000001107050 [http://perma.cc/9MH4-XDV5].

Pittsburgh Steelers	Ramon Foster	11 years
San Francisco 49ers	Richard Sherman	9 years
Seattle Seahawks	K.J. Wright	9 years
Tampa Bay Buccaneers	Ali Marpet	5 years
Tennessee Titans	Wesley Woodyard	12 years
Washington Redskins	Nick Sundberg	10 years

Appendix E[243]
NHLPA Player Representatives

Team	Player Representative	Years in League[244]
Anaheim Ducks	Josh Manson	6 years
Arizona Coyotes	Derek Stepan	10 years
Boston Bruins	Brandon Carlo	4 years
Buffalo Sabres	Jake McCabe	7 years
Calgary Flames	Mikael Backlund	11 years
Carolina Hurricanes	Jordan Martinook	8 years
Chicago Blackhawks	Jonathan Toews	13 years
Colorado Avalanche	Ian Cole	10 years
Columbus Blue Jackets	David Savard	10 years
Dallas Stars	Jason Dickinson	5 years
Detroit Red Wings	Luke Glendening	7 years
Edmonton Oilers	Darnell Nurse	5 years
Florida Panthers	Michael Matheson	5 years
Los Angeles Kings	Matt Roy	3 years
Minnesota Wild	Devan Dubnyk	11 years
Montreal Canadiens	Paul Byron	11 years
Nashville Predators	Yannick Weber	12 years
New Jersey Devils	Kyle Palmieri	10 years
New York Islanders	Anders Lee	8 years
New York Rangers	Jacob Trouba	7 years
Ottawa Senators	Brady Tkachuk	2 years
Philadelphia Flyers	James Van Riemsdyk	11 years
Pittsburgh Penguins	Kristopher Letang	13 years
San Jose Sharks	Logan Couture	11 years
St. Louis Blues	Colton Parayko	5 years
Tampa Bay Lightning	Alexander Killorn	8 years
Toronto Maple Leafs	Zach Hyman	5 years
Vancouver Canucks	Bo Horvat	6 years
Vegas Golden Knights	Nate Schmidt	8 years
Washington Capitals	Thomas Wilson	7 years
Winnipeg Jets	Adam Lowry	7 years

243 *Executive Board*, *supra* note 173.

244 CAPFRIENDLY, http://www.capfriendly.com [http://perma.cc/W5VA-CBNT] (last visited Apr. 1, 2020). At the time of this writing, the 2019–20 NHL season was on hiatus due to the COVID-19 pandemic. Years of experience data accurate counting the 2019–20 season as a full year.