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A LEGAL FRAMEWORK FOR NET ZERO ALIGNED INSURANCE PRODUCTS

FRANZISKA ARNOLD-DWYER*

ABSTRACT

This paper examines how the contractual framework of existing insurance products for consumers and small businesses can be adjusted to help them reduce their net GHG emissions, and thereby facilitate the transition to a sustainable net-zero economy (= Net-Zero Aligned Insurance Products; “NZAIPIs”). NZAIPIs could give rise to legal and regulatory issues, and this paper considers how these issues could be addressed to create a legal environment that provides safe and fair market conditions for NZAIPIs.

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I. INTRODUCTION

The impacts of climate change on the environment and communities worldwide are already felt: heat waves, droughts and flooding, retreating glaciers and ice loss, rising sea levels, more frequent and more severe windstorms, and more frequent compound extreme weather events.¹ All of these observed changes have been scientifically linked to the warming of the climate system as a result of human activity, and in particular, anthropogenic greenhouse gas (“GHG”) emissions.²

The 2015 Paris Agreement seeks to curb the threat of climate change by setting goals to keep the global temperature rise below 2°C and pursue efforts to limit the temperature increase to 1.5°C, compared to pre-industrial levels.³ Reaching the 1.5°C target requires the “rapid, deep and sustained reductions” in global GHG emissions by 43% by 2030, relative to 2019 levels.⁴ In furtherance of the Paris Agreement goals, the UK government has set a legally binding target to reduce UK net GHG emissions by 100% by 2050,⁵ and a 78% reduction target for 2035 (compared to 1990 levels).⁶ As most of the operative provisions of the Paris Agreement do not set hard or binding targets, its implementation relies on “an enhanced transparency framework” which requires parties to set their own targets and report on progress.⁷ There is widespread recognition that there is no time to rely on an international agreement alone. Additionally, achieving the Paris Agreement

¹ Intergovernmental Panel on Climate Change, *Climate Change 2021: The Physical Science Basis*, ¶¶ A.2–A.3.5 (2021).

² *Id.* at ¶ A.4.1.

³ Paris Agreement to the United Nations Framework Convention on Climate Change, art. 2, ¶ 1, Dec. 12, 2015, T.I.A.S. No. 16-1104 [hereinafter Paris Agreement].

⁴ Sharm el-Sheikh Climate Change Conference, *Sharm el-Sheikh Implementation Plan*, ¶ 15 (Nov. 22, 2022) [hereinafter *Sharm el-Sheikh Implementation Plan*].

⁵ Climate Change Act 2008, SI 2019/1056, § 1 (UK).

⁶ Press Release, Dep’t for Bus. Indust. Strategy, UK Enshrines New Target in Law to Slash Emissions by 78% by 2035, U.N. Press Release (April 20, 2021), <https://www.gov.uk/government/news/uk-enshrines-new-target-in-law-to-slash-emissions-by-78-by-2035>.

⁷ Paris Agreement, *supra* note 3, at art. 13, ¶¶ 1, 2, 7(b).

goals requires bottom-up action from sub-state actors, businesses, investors, and financial institutions.⁸

Many large corporations now make publicly available information about their strategies for climate-related risks in accordance with the TCFD Recommendations,⁹ and some have pledged to pursue decarbonising strategies. Yet, there is little information or practical support for consumers and small businesses on how they can make better-informed choices and take greater responsibility in transitioning to a net-zero economy.

Drawing on their risk management expertise, the insurance industry can do more to support policyholders, their business partners in the insurance value chain, other stakeholders, and wider society in reducing GHG emissions and transitioning to a net-zero economy in a fair and sustainable way. Some insurance companies are already engaged in climate impact investment and stewardship. In 2021 a group of the world's leading insurers launched the UN-convened Net-Zero Insurance Alliance, committing to transition their underwriting portfolios to net-zero GHG emissions by 2050.¹⁰ By shifting the focus from the insurance industry's traditional post-disaster reaction approach to a proactive climate change risk mitigation approach that extends to consumers and small businesses, the insurance industry could make an even stronger contribution.

This paper will discuss the contractual framework and the legal and regulatory environment that are needed to develop and operate insurance products that help consumers and small businesses reduce their net GHG emissions, thereby facilitating the transition to a sustainable net-zero economy (= Net-Zero Aligned Insurance Products; "NZAIPs").

This paper does not propose the invention of insurance products that cover new risks; rather, it will examine how the design of existing insurance products for consumers and small businesses can be adjusted to achieve a positive contribution to the reduction of GHG emissions. This paper is structured as follows: Chapter 2 considers the legal relationship between

⁸ See U.N. Climate Change, Race to Zero Campaign, <https://unfccc.int/climate-action/race-to-zero-campaign> (last visited Oct. 10, 2022); see also Jonathan R. Macey, *ESG Investing: Why Here? Why Now?*, GEO. MASON CAPITALISM RULE L. PROJECT 1, 22 (2022).

⁹ See generally RECOMMENDATIONS OF THE TASK FORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES, TCFD (2017), <https://assets.bbhub.io/company/sites/60/2021/10/FINAL-2017-TCFD-Report.pdf>.

¹⁰ U.N. Env't Programme, The Net-Zero Insurance Alliance: Statement of Commitment by Signatory Companies, <https://www.unepfi.org/psi/wp-content/uploads/2021/07/NZIA-Commitment.pdf> (last visited Oct. 10, 2022) [hereinafter Net-Zero Insurance Alliance].

insurers and policyholders, the purpose and functions of insurance contracts, and the role of insurers in a just transition to a net-zero economy; Chapter 3 discusses the contractual design for NZAIPs; Chapter 4 highlights some of the legal and regulatory issues that NZAIPs could give rise to, and how they might be addressed to create a legal environment conducive to NZAIPs; and Chapter 5 seeks to place NZAIPs within the wider context of sustainable development.

II. THE ROLE OF INSURANCE AND INSURERS

A. NATURE OF INSURANCE

The legal relationship between an individual policyholder and an insurer is based on an insurance contract, which is a contract to transfer risk from the policyholder (the insured) to the insurer. Generally speaking,¹¹ the insurer undertakes to pay the insured an indemnity (or to provide a corresponding benefit) upon the occurrence of the insured event that is adverse to the interests of the insured in return for the payment of a premium by the insured.¹² The policyholder transforms its risk of a large financial loss resulting from the loss of, or damage to, an asset, or the risk of incurring liability to a third party, into the certainty of “losing” a relatively small amount by way of premium payments. In return for paying premiums, the policyholder gains peace of mind that, in the event of a loss covered by the insurance contract, it will be indemnified for that loss by the insurer.¹³ The insurer is able to absorb the risk more efficiently (1) as a result of the law of large numbers, (2) because of risk diversification, and (3) because an insurer can pool and invest the premium income more profitably compared to an

¹¹ Not all contracts of insurance are contracts of indemnity insurance (i.e., compensating for an actual loss suffered as a result of an insured event). Some contracts of insurance are contingency contracts where the insurer provides for the payment of a predetermined sum of money upon the occurrence of a contingent event.

¹² *Prudential Ins. Co. v. Comm’r of Inland Revenue*, [1904] 2 KB 658, 663.

¹³ Behavioural economics theory has it that most people are “risk adverse.” In the insurance context that means that they have a preference for the certainty of paying a (small) premium over the uncertainty of a large future financial loss. See Ronen Avraham, *The Economics of Insurance Law—A Primer*, 19 CONN. INS. L. J. 29, 37 (2012).

insured investing his premium saving if he does not buy insurance for a particular risk.¹⁴

Thus, insurance is a mechanism for transferring and pooling risk. The process of assessing risks to be transferred and calculating a premium that is reflective of the specific risk and the underwriting pool is called “underwriting.” There is an overall social gain as the aggregate exposure to the risk of all policyholders participating in that pool is mitigated.¹⁵ Insurance also has a wider societal benefit in that it provides fast compensation to victims of disasters, accidents, torts, and income security in retirement or ill-health, easing the burden on tax-funded benefits and compensation schemes.¹⁶

Additionally, insurance companies act as investors: to protect the value of the premium income against inflation, insurers invest the premiums into assets that generate a return. For certain life insurance products, the investment return on the premium is a core component of the pay-out to the policyholder or its beneficiaries (“insurance-based investment products”). In those instances, insurers act as asset managers: the insurer invests (some of) the premium, on behalf of the policyholder or beneficiary, in specified investments funds which the insurer manages. The pay-out on maturity varies according to the investment performance of the fund (and the underlying assets) in which the premium has been invested.

B. CLIMATE CHANGE-RELATED RISKS

The insurance industry itself is exposed to climate change-related risks that could impact an insurer’s business model and financial stability. They fall into three broad categories: (1) physical risks, (2) transition risks, and (3) liability risk.¹⁷ Physical risk materializes through the impact of climate change on physical assets which insurers may insure, and in relation

¹⁴ See generally Eric A. Posner & E. Glen Weyl, *An FDA for Financial Innovation: Applying the Insurable Interest Doctrine to Twenty-First-Century Financial Markets*, 107 NW. U. L. REV. 1307, 1308, 1314 (2013).

¹⁵ *Id.* at 37. See also Lloyd R. Cohen & Michelle E. Boardman, *Methodology: Applying Economics to Insurance Law—an Introduction*, in RESEARCH HANDBOOK ON INTERNATIONAL INSURANCE LAW AND REGULATION 19, 22–23 (Julian Burling & Kevin Lazarus eds., 2011).

¹⁶ Avraham, *supra* note 13, at 41.

¹⁷ The three categories of climate change-related risks were first introduced by Mark Carney, the former Governor of the Bank of England and U.N. Special Envoy on Climate Action. See Mark Carney, *Breaking the Tragedy of the Horizon—Climate Change and Financial Stability*, in BANK OF ENG. (Sept. 29, 2015).

to which they may become liable to pay claims, and in which insurers may invest. Transition risk has several sub-categories: (i) the strategic and market risk arising from the contraction of the carbon sector, related industries, and technical innovations; (ii) the investment risk in relation to stranded assets which can affect the valuation and profitability of investment portfolios; and (iii) the reputational risk arising from not transitioning to low carbon or net-zero operations in a timely and meaningful manner. Finally, the liability risk for insurers arises from (1) actions brought against insurers directly relating to the consideration of climate change in investment decision-making or inadequate disclosure of climate change risks in public documents or product information and, (2) liability insurance coverage they provide to their insureds, indemnifying them for damages and defense costs to third parties contributing to climate change, failing to mitigate or adapt to climate change, non-compliance, non-disclosure and corporate governance failures relating to climate change.

C. IMPACT UNDERWRITING AND IMPACT INVESTMENT

How can insurers play a role in the transition to a net-zero economy? They can do so primarily through “impact underwriting” and “impact investment,” as well as by reducing GHG emissions in their operations. “Impact underwriting” generally refers to using insurance to promote economic, social, and environmental sustainability for the benefit of society as a whole. The United Nations Environment Programme (“UNEP”) Finance Initiative (“FI”) Principles for Sustainable Insurance (“PSI”), Principle 1 requires insurers to “[d]evelop products and services which reduce risk, have a positive impact on ESG issues and encourage better risk management.”¹⁸ Broadly speaking, this can be done by (1) supporting sustainable activities by providing insurance coverage; (2) developing insurance products and services that that shift non-sustainable behavior and processes of policyholders in a more sustainable direction; and (3) reducing underwriting activities that harm sustainability.¹⁹ The challenge for insurers to engage with environmental impact underwriting was set by António Guterres, Secretary General of the United Nations, in 2021: “We need net-zero commitments to

¹⁸ *The Principles*, U.N. Env’t Programme, <https://www.unepfi.org/insurance/insurance/> (last visited Oct. 10, 2022). The PSI are aspirational, and not binding on the signatories. “ESG issues” stands for environmental, social, and governance issues.

¹⁹ See, e.g., Race to Zero Campaign, *supra* note 8.

cover your underwriting portfolios, and this should include the underwriting of coal -- and all fossil fuels.”²⁰

“Impact investment” is an investment approach that, in addition to financial returns, pursues ethical or societal goals that benefit a wider group of stakeholders or society as a whole. Impact investment with a focus on sustainability has been on the horizon since the late 1990s and has been more firmly placed on the agenda of policymakers, regulators, and financial markets since the launch of the Principles for Responsible Investment²¹ in 2006 and the adoption of the Sustainable Development Goals (“SDGs”)²² by the United Nations in 2015. Impact investment with environmental objectives can involve (1) the divesting of carbon-intense assets from sectors detrimental to environmental considerations; (2) refraining or limiting fresh investment in those assets and sectors; (3) investing in companies engaged in reducing their carbon footprint; and (4) directing investments at economic activities aimed at climate risk reduction.

D. ROLE OF INSURERS

As this paper focuses on NZAIPs insurance products, more detailed consideration needs to be given to whether and why insurers should engage in impact underwriting. There are a number of risks. Impact underwriting could reduce an insurer’s profits and competitiveness and create protection gaps if, for example, the insurer stops insuring coal and fossil businesses. Providing insurance for “green” technologies, assets, and projects can be more expensive as they tend to be innovative and are often untested (as a result, there is insufficient data for risk modelling and pricing)²³ and

²⁰ António Guterres, Secretary-General of the U.N., Closing Remarks to Insurance Development Forum (June 8, 2021), <https://www.un.org/sg/en/content/sg/speeches/2021-06-08/closing-remarks-insurance-development-forum>.

²¹ *The Six Principles for Responsible Investment Offer a Menu of Possible Actions for Incorporating ESG Issues into Investment Practice.*, PRINCIPLES RESPONSIBLE INV., <https://www.unpri.org/about-us/what-are-the-principles-for-responsible-investment> (last visited Oct. 10, 2022).

²² G.A. Res. 70/1, Transforming Our World: The 2030 Agenda for Sustainable Development, ¶ 59 (Oct. 21, 2015).

²³ Maryam Golnaraghi, *Investing in Climate-Resilient Decarbonized Infrastructure to Meet Socio-Economic and Climate Change Goals*, GENEVA ASS’N 1, 3–4 (Dec. 10, 2019), <https://www.asiainsurancereview.com/Magazine/ReadMagazineArticle?aid=43145>

sometimes their physical characteristics can pose higher risks than their conventional equivalents (e.g., their location in vulnerable geographies, the materials used are more susceptible to physical damage, and the reliance on emerging technologies).

NZAIPs pose their own challenges: a combination of inertia, insufficient customer demand, potentially high research and development costs (which in the UK requires a formal internal approval and testing process),²⁴ the risk of free riders, and the regulatory focus to date being the financial risks from climate change,²⁵ all of which may be limiting insurers' current appetite and capacity for developing NZAIPs.

NZAIPs also raise jurisprudential questions as to whether it is appropriate for insurers to seek to influence the behavior of their policyholders. There is existing scholarship on the conception of insurance as “governance,” and insurers as “quasi-regulators,”²⁶ where insurance is conceived as a tool to control policyholders' behavior or achieve specific outcomes. Arguably, in motor insurance and health insurance, insurers have been taking this role for some time by giving preferential terms and better premium rates to policyholders who drive safely (as evidenced by a clean driving record) and lead a healthy lifestyle (in health insurance, the pre-contractual questionnaire often includes questions about smoking, alcohol consumption, and exercise). Just like governments make laws, the insurance contract imposes obligations on policyholders to govern their behavior throughout the term of the contract and, like law enforcement agencies, the insurance industry uses sophisticated inspection and audit systems to ensure that policyholders comply.²⁷ This “governance” function of insurance has been criticized because insurers assume regulatory functions that a governmental body could perform without being subject to the standards we expect from, and the limitations placed upon, governmental authority²⁸ such as transparency, due process, and acting *intra vires* and reasonably.

²⁴ Fin. Conduct Auth.[FCA], *Product Intervention and Product Governance Sourcebook*, ¶ 4.2 (Jan. 2023) [hereinafter PROD].

²⁵ Bank Eng. Prudential Regul. Auth. [PRA], *Enhancing Banks' and Insurers' Approaches to Managing the Financial Risks from Climate Change*, ¶¶ 1.2, 2, SS3/19 (Apr. 2019).

²⁶ See generally, RICHARD V. ERICSON, AARON DOYLE & DEAN BARRY, *INSURANCE AS GOVERNANCE* (2003). See Carol A. Heimer, *Insuring More, Ensuring Less: The Costs and Benefits of Private Regulation Through Insurance*, in *EMBRACING RISK* 116, 116–145 (Tom Baker & Jonathan Simon eds., 2002).

²⁷ ERICSON ET AL., *supra* note 26, at 361.

²⁸ Kenneth S. Abraham, *Four Conceptions of Insurance*, 161 U. PA. L. REV. 653, 685–91 (2013).

Moreover, it has been noted that in contrast to laws and regulations aimed at reducing risks to the public, insurers only “regulate” out of self-interest to reduce their own liability.²⁹

This rather sinister conception of insurers as quasi-regulators is not appropriate for NZAIPs, which aim to help consumers and small businesses transition to a net-zero economy. Accordingly, the contractual design discussed in Chapter 3 sees insurers as enablers that nudge consumer and small business policyholders towards emission-reducing or carbon-neutral activities. Contract law is used to incentivize commitment to reducing GHG emissions.³⁰ A similar idea has been put forward in relation to investors who can use the “green pill” of contract law to incentivize and enforce net-zero commitments of their investee companies.³¹

While insurers have not yet widely adopted the role of net-zero enablers, they will increasingly be incentivized to consider it as customer demand for NZAIPs rise. In addition, as voluntary sustainability and climate disclosure frameworks harden into mandatory disclosure requirements,³² there will be increasing pressure from investors, shareholders, and other stakeholders on insurers to engage in climate impact underwriting. UN-convened insurance industry frameworks such as the PSI³³ and the Net-Zero Insurance Alliance set expectations for transitioning underwriting portfolios to net-zero GHG emissions.³⁴

²⁹ Kenneth S. Abraham & Daniel Schwarcz, *The Limits of Regulation by Insurance*, 98 IND. L. J. 215, 227 (2022).

³⁰ See *infra* Chapter 3.

³¹ John Armour, Luca Enriques & Thom Wetzer, *Green Pills: Making Corporate Climate Commitments Credible* 1, 39–53 (ECGI Working Papers Series in L., Paper No. 657, 2022).

³² See Bank Eng. Prudential Regul. Auth. [PRA], *supra* note 25, at ¶ 3.20 (In the UK all insurers must engage with the TCFD Recommendations); Fin. Cond. Auth., *Proposals to Enhance Climate-Related Disclosures by Listed Issuers and Clarification of Existing Disclosure Obligations*, ¶ 1.13, PS20/17 (Dec. 2020); Fin. Cond. Auth., *Listing Rules*, ¶ 9.8.6(8)(a), LR 9/33 (Jan. 2023) (premium-listed insurers must include a compliance statement in their annual financial report, stating whether they have made disclosures consistent with the TCFD recommendations or providing an explanation if they have not done so); see also Companies Act 2006, ¶¶ 414CA–414CB (UK) (insurers that are traded companies must prepare an annual “Strategic Report” including information on their environmental impact and strategies, and products that are environmentally harmful.).

³³ *The Principles*, *supra* note 18.

³⁴ Net-Zero Insurance Alliance, *supra* note 10.

The role of insurers as “net-zero enablers” is in line with emerging theoretical frameworks on “stakeholder capitalism,”³⁵ “environmental stewardship,”³⁶ and a wider meaning of “corporate purpose,”³⁷ which see the role of corporations as not just optimizing short-term profits for shareholders, but maximizing long term shareholder value creation, by taking into account the needs of all their stakeholders and society at large. This includes taking responsibility for protecting the environment. The EU Commission has put forward a proposal for a directive on corporate sustainability due diligence, which will require companies that fall within its scope to, inter alia, address the adverse environmental impacts of their actions, including their value chains inside and outside Europe.³⁸ The UNFCCC COP27 Sharm el-Sheikh Implementation Plan affirms that sustainable and just solutions to the climate crisis require “social dialogue and participation of all stakeholders,” and, in particular, financing from financial institutions and institutional investors for a global transition to a net-zero economy.³⁹ As a carrier of climate change-related risks,⁴⁰ it would ultimately be in the insurance industry’s own mid-term interest to support their customers in reducing net GHG emissions. Although “impact underwriting” is a newly coined term, the insurance business model is inextricably linked to requiring or encouraging (better) risk management by policyholders.

³⁵ See generally Klaus Schwab, *Davos Manifesto 2020: The Universal Purpose of a Company in the Fourth Industrial Revolution*, WORLD ECON. F. (Dec. 2, 2019), <https://www.weforum.org/agenda/2019/12/davos-manifesto-2020-the-universal-purpose-of-a-company-in-the-fourth-industrial-revolution/>; KLAUS SCHWAB, *STAKEHOLDER CAPITALISM: A GLOBAL ECONOMY THAT WORKS FOR PROGRESS, PEOPLE AND PLANET* (2021).

³⁶ See generally Nathan J. Bennett, Tara S. Whitty, Elena Finkbeiner, Jeremy Pittman, Hannah Bassett, Stefan Gelcich & Edward H. Allison, *Environmental Stewardship: A Conceptual Review and Analytical Framework*, 61 ENV’T MGMT. 597 (2018).

³⁷ See *Principles for Purposeful Business: How to Deliver the Framework for the Future of the Corporation*, BRIT. ACAD. (Nov. 2019), <https://www.thebritishacademy.ac.uk/publications/future-of-the-corporation-principles-for-purposeful-business>.

³⁸ *Proposal for a Directive of the European Parliament and of the Council on Corporate Sustainability Due Diligence and Amending Directive*, at 1–2, COM (2022) 71 final (Feb. 23, 2022).

³⁹ *Sharm el-Sheikh Implementation Plan*, *supra* note 4, at ¶ 28, ¶ 30.

⁴⁰ See *supra* Chapter 2.2.

III. CONTRACTUAL DESIGN OF NZAIPS

To date, the insurance industry's climate change focus has been on managing the financial risks of climate change. In practical terms, insurance for weather-related risks associated with climate change (e.g., property damage and business interruption losses caused by windstorms, floods, or wildfire) and climate-related liability claims offers policyholders financial protection against the impact of loss. This can build resilience of individuals and government budgets to the financial impact of climate change risks. However, it does not prevent the loss from climate change risks, and it does not address the root cause of climate change (i.e., GHG emissions). Moreover, as extreme weather events become more frequent and severe, certain climate change-related risks are, or are becoming, uninsurable.⁴¹ It is clear from initiatives such as the PSI and the Net-Zero Insurance Alliance,⁴² that the insurance industry recognizes that it must bring about a paradigm shift from a post-disaster reaction approach towards a comprehensive and integrated climate risk mitigation and risk management approach to climate change risks. NZAIPs are part of this process.

This paper will consider four interconnected areas within the design of a contract of insurance —pre-contractual negotiations, pricing, terms and claims—that lend themselves to influencing choices by policyholders aimed at reducing their net GHG emissions.

A. PRE-CONTRACTUAL NEGOTIATIONS

As noted above, the legal relationship between an individual policyholder and an insurer is based on an insurance contract. Under English law, this relationship pre-dates the point of entering into the contract. The insurer will ask a prospective consumer-policyholder questions about the risk to be insured in order to determine whether to take the risk and, if so, on what terms. The prospective consumer-policyholder is under a pre-contractual duty to take reasonable care not to make a misrepresentation to

⁴¹ For example, in California some homeowners can no longer buy any property insurance covering for wildfires, whilst others can no longer afford to buy insurance because of spiraling premium prices. See Mary W. Walsh, *How Wildfires Are Making Some California Homes Uninsurable*, N.Y. TIMES (Nov. 20, 2018), <https://www.nytimes.com/2018/11/20/business/california-fires-insurance.html>; see also Opinion on Sustainability within Solvency II, ¶ 5.52, EIOPA-BoS-19/241 (Sept. 30, 2019).

⁴² *The Principles*, *supra* note 18; Net-Zero Insurance Alliance, *supra* note 10.

the insurer.⁴³ A prospective non-consumer policyholder owes the insurer a pre-contractual duty to give a fair presentation of all circumstances material to the risk.⁴⁴ Information about the prospective policyholder's carbon-intense assets and activities, or its decarbonizing activities, can be material to the insurer's underwriting assessment.⁴⁵ At the pre-contractual stage, insurers can influence prospective policyholders' behavior by offering different levels of coverage and different levels of premiums depending on the existing risk management measures and risk attitude of the prospective policyholder.

UNEP FI has published guidance on how ESG factors can be integrated into insurers' risk assessment frameworks applicable to their underwriting portfolios.⁴⁶ For larger businesses, some brokers and insurers have already started to use pre-contractual ESG risk assessments that seek to identify the ESG issues faced by prospective policyholders. For example, leading insurance broker Marsh offers an ESG risk assessment in which the prospective policyholder is awarded an ESG rating, which then informs the scope of coverage for directors and officers insurance and, in particular, eligibility for add-on cover for investigation costs related to climate-related financial disclosures.⁴⁷ The ESG risk assessment and rating might prompt the policyholder to choose pathways for mitigating ESG risks and set targets for improving its ESG rating.

In relation to consumers and small businesses, it is unlikely that insurers would want to incur the expense of a GHG emission assessment of property and business operations as it would be of limited direct relevance to the risk assessment for property and business insurance. The level of GHG emissions cannot (yet) be linked to the risk of loss of or damage to buildings, personal property, business assets, and business operations. There is no legal duty on consumers and small businesses to reduce or disclose GHG emissions, to which liability would attach on breach. However, insurers could use this point of contact and information exchange to make available

⁴³ Consumer Insurance (Disclosure and Representations) Act 2012, c. 6, § 2(2) (UK).

⁴⁴ Insurance Act 2015, c. 4, §§ 3(1), 3(4) (UK).

⁴⁵ *Id.* at § 7(3).

⁴⁶ Env't Programme, *Managing Environmental, Social and Governance Risks in Non-Life Insurance Business* (June 2020), <https://www.unepfi.org/insurance/insurance/>.

⁴⁷ *Delta Side D: Cover for investigation costs related to TCFD reporting*, MARSH, <https://www.marsh.com/uk/services/financial-professional-liability/products/delta-side-d-cover-investigation-costs-tcf-reporting.html> (last visited Oct. 10, 2022).

standardized information on (1) the likely GHG emissions of the property by reference to its size, type of heating, and EPC rating; (2) reducing GHG emissions of buildings and in transport, for example by reference to the recommendations of the UK's Climate Change Committee;⁴⁸ and (3) available government schemes and grants aimed at reducing GHG emissions.⁴⁹ By raising awareness on these matters, insurers can enable consumer and small business policyholders to make better-informed choices on these matters.

Insurers, too, have pre-contractual information obligations, as set out in the Financial Conduct Authority ("FCA") Handbook ICOBS Insurance: Conduct of Business Sourcebook ("ICOBS"), which range from information about itself, its services, and the insurance product in question. The ICOBS obligations will be discussed in Chapter 4.

B. PRICING

Pricing in insurance means the level of premium payable by the insured. The premium is calculated by the insurer by reference to the level of risk that is transferred and the costs of the insurer associated with assuming the risk. Given the crowded consumer insurance and commoditized business insurance markets, premiums need to be competitive and yet be capable of generating a profit for insurers. If premiums are too high and become unaffordable, policyholders may decide to remain uninsured, and this will create protection gaps. Pricing is primarily a commercial matter, but there are also some legal considerations. The product design requirement for "fair value" and whether premium discounts are consistent with "corporate purpose" will be discussed in Chapter 4. In addition, under the UK insurance solvency regulatory regime,⁵⁰ an insurer must set premiums so that the insurer continues to have enough funds for its

⁴⁸ Climate Change Comm. [CCC], *The Sixth Carbon Budget: Buildings*, (Dec. 9, 2022).

⁴⁹ See *infra* Chapter 3.4.

⁵⁰ The UK's current insurance solvency regime is based on the EU Solvency II Directive 2009/138/EC (recast) which was implemented in the UK with the Solvency 2 Regulations 2015 (2015/575). Council Directive 2009/138, 2009 O.J. (L 335) (EC); Solvency 2 Regulations 2015, SI No. 575 (UK). With the UK's withdrawal from the EU, the EU Solvency II regime was "onshored" into the UK domestic law, such that it continues to apply with the relevant adjustments to insurers and reinsurers with head offices in the UK. This process of "onshoring" was effected by the European Union (Withdrawal) Act 2018. European Union (Withdrawal) Act 2018, c. 16 (UK).

technical provisions⁵¹ and to match or exceed its solvency capital requirements.⁵²

How can premium pricing affect GHG emissions? Insurers could use pricing structures that penalize carbon-intense activities or reward net GHG emission reducing activities. Coal companies are already facing premium rate increases of up to 40%,⁵³ although the increase is more likely to result from restricted underwriting capacity following a growing number of insurers exiting the coal market. For small businesses and consumers, the level of GHG emissions could be made a pricing factor. However, unless an increase in premiums for higher GHG emissions can be linked to the risk insured, there is a risk that to do so would be in breach of the “fair value” principle.⁵⁴

In regard to rewards, in the US, some home insurers already offer premium discounts for LEED-certified homes.⁵⁵ In the UK, an Energy Performance Certificate (EPC) is already required when a property is being built, sold, or rented. The UK Government is consulting on plans that would require mortgage lenders to take a property’s EPC rating into account in their lending decision and offer financial rewards (lower interest rates, cash-back, and extended mortgages) to facilitate improvements to a home’s energy efficiency.⁵⁶ These plans could be extended to property insurers, so that

⁵¹ Bank Eng. Prudential Regul. Auth. [PRA], *Technical Provisions*, ¶ 2.1 (Jan. 1, 2016).

⁵² Bank Eng. Prudential Regul. Auth. [PRA], *Solvency Capital Requirement – General Provisions*, ¶ 2.1 (Jan. 1, 2016).

⁵³ *Managing the Transition: Mining Risk Review 2020*, WILLISTOWERSWATSON (2020), <https://willistowerswatson.turtl.co/story/mining-risk-review-2020-ungated/page/3/2>.

⁵⁴ See *infra* Section 4.1.

⁵⁵ LEED (Leadership in Energy and Environmental Design Green Building Rating System) is a system developed by the U.S. Green Building Council that is a recognized environmental standard in the building world and has high efficiency and sustainability standards. See *Green insurance: Being kind to the environment can save you money on your policies*, INS. INFO. INST., <https://www.iii.org/article/green-insurance> (last visited Oct. 10, 2020).

⁵⁶ The UK Government is proposing the annual disclosure of portfolio-wide Energy Performance Certificate (EPC) data and the gross value of lending for energy performance improvement works by mortgage lenders. See Dep’t for Bus., Energy & Indus. Strategy, *Improving Home Energy Performance Through Lenders*, at 19 (Feb. 12, 2021), https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/936276/improving-home-energy-performance-through-lenders-consultation.pdf.

premium rebates might be offered in relation to insured properties that improve their energy performance in prescribed ways (e.g., carrying out energy efficiency retrofitting or installing low-carbon heating) during the policy term.

Could motor insurers discount the premiums for hybrid and electric cars? Until recently, motor insurance for hybrid and electric cars has been more expensive compared to petrol or diesel cars, as insurers have had scant historical data to price repairs.⁵⁷ The risk of injuring third parties is the same, but it has been reported that electric cars are considered to be a lower theft risk because of their limited range and still limited charging infrastructure.⁵⁸ As more data has become available, premium levels for hybrid and electric cars have been adjusted, and some motor insurers have offered premium discounts to electric car owners as an incentive to new customers.⁵⁹ Although the practice of “price walking”—giving premium discounts to new customers but not to existing customers—has been banned for consumer motor and home insurance since January 1, 2022,⁶⁰ motor insurers could consider a one-off premium discount for existing customers switching from a petrol or diesel car to an electric or hybrid car. For businesses, insurers could consider packages at attractive premium rates for electric and hybrid car fleets. As the shift to zero-emission vehicles is part of the UK Government’s “Ten Point Plan for a Green Industrial Revolution,”⁶¹ motor insurers should give consideration to how they could contribute by offering attractive premium rates for electric cars.

Motor policies that offer “Pay as You Drive” coverage could incentivize the policyholder to drive less; a telematic device that is installed in the car tracks the miles driven, and the policyholder is charged a premium on a per-mile basis.⁶² Less driving means less risk, which in turn means lower premiums, less fuel consumption, and reduced GHG emissions. Although

⁵⁷ *Choosing an electric or hybrid car: The basics of low-emission vehicles*, AVIVA (Jan. 23, 2020), <https://www.aviva.co.uk/insurance/motor/car-insurance/electric-and-hybrid-cars/>.

⁵⁸ *Are electric cars more expensive to insure?*, WHAT CAR? (Nov. 4, 2019), <https://www.whatcar.com/advice/owning/are-electric-cars-more-expensive-to-insure/n18043>.

⁵⁹ *Id.*

⁶⁰ Fin. Conduct Auth. [FCA], *General Insurance Pricing Practices Market Study: Feedback to CP20/19 and Final Rules*, ¶ 3.2, PS21/5 (May 2021).

⁶¹ HM Gov’t, *The Ten Point Plan for a Green Industrial Revolution*, ¶ 4 (Nov. 18, 2020), <https://www.gov.uk/government/publications/the-ten-point-plan-for-a-green-industrial-revolution/title>.

⁶² *See, e.g.*, BY MILES., <https://www.bymiles.co.uk/> (last visited Oct. 10, 2022).

this is an example of incidentally enabling an environmental goal, usage-based premium mechanisms could be marshalled to reduce GHG emissions.

Other pricing benefits that could be considered—depending on their suitability in the policy context—are lowering deductibles and increasing or reinstating sub-limits of liability that become applicable if the policyholder takes or refrains from taking specified actions.

C. TERMS (OTHER THAN PRICING AND CLAIMS)

For consumers and small businesses, insurance contracts are contracts of adhesion that are offered with standardized terms on a “take it or leave it” basis.⁶³ If the terms are too onerous, a prospective policyholder’s only other options are to buy insurance from another insurer who offers better terms or not insure at all.

What kind of contractual terms can influence the policyholder’s behavior and enable them to reduce the GHG emissions of its assets and activities (“green term” will be used as shorthand)? Before discussing specific examples, let us consider the characteristics of a well-drafted green term. First, if the green term imposes an obligation on the policyholder, it should be an action or inaction within the control of the policyholder and an obligation that the policyholder is realistically able to fulfill without imposing a disproportionate burden. Secondly, the substance of the green term (whether it is an obligation or an exclusion) must have a degree of salience—it must be relevant to the commercial purpose of the insurance contract in question, which is the risk transfer in relation to the insured subject matter. The difficulty is how this can be translated into meaningful green terms, given that climate change itself is a relatively abstract concept and that GHG emissions may not have direct salience to the insurance policy in question. Thirdly, if the term is an exclusion from coverage, the excluded risks must be well-defined and must not obliterate the cover.⁶⁴ Fourthly, as will be discussed below, terms in consumer (insurance) contracts are required to be fair. A green term will not stand up to legal and regulatory scrutiny,⁶⁵ unless these basic requirements are met.

⁶³ Kenneth S. Abraham, *Four Conceptions of Insurance*, 161 U. PA. L. REV. 653, 660 (2013).

⁶⁴ *Fin. Conduct Auth. v. Arch Ins. (UK) Ltd.*, Judgment, [2021] UKSC 1, [78].

⁶⁵ See *infra* Chapter 4.

Policyholders' motivation to take climate action is undermined by the "tragedy of the commons"⁶⁶: individual acts by a consumer or a small business do not halt or reverse climate change, so they are likely to act according to their own self-interest without consideration of the impact on the common good. Therefore, to influence the policyholder's behavior effectively, good behavior should be rewarded, and bad behavior should be penalized. Bounded rational choice theory holds that a rational decision-maker decides on a preferred course of action that maximizes their personal advantage by balancing costs against benefits based on the knowledge and information available to them,⁶⁷ and prospect theory tells us that people's loss aversion tends to be greater than the prospect of a gain.⁶⁸ Applied to insurance contract law, compliance with a green term should trigger a contractual benefit to be conferred upon the policyholder by the insurer, and/or breach or non-compliance with a green term should trigger a remedy or have another negative contractual consequences. An exclusion in an insurance contract means that the excluded risk remains outside the scope of the cover, and a policyholder is thus put on notice that specified perils, assets, and activities remain at their own risk and do not attract insurance protection.

The primary benefit for the policyholder under an insurance contract is the claims payment in the event of a loss or insured event. What additional benefits could an insurer offer to reward compliance with a green term? In relation to health insurance, insurers are already offering additional benefits (such as vouchers for, or subsidized, gym memberships) to support a healthy lifestyle. Nudge theory suggests that incentives should be coupled with good information or feedback to enable better decisions going forward.⁶⁹ Thus, to be effective, the additional benefit would not just be a "perk" for the policyholder but would also be capable of reducing GHG emissions or have another positive effect on the environment, thereby benefitting the policyholder or society at large. For example, this could be a credits system or cash-back system for replacing a fossil fuel appliance or energy source

⁶⁶ *Tragedy of the commons*, OXFORD DICTIONARY OF ECONOMICS (5th ed. 2017).

⁶⁷ See generally GARY S. BECKER, *THE ECONOMIC APPROACH TO HUMAN BEHAVIOR* (Univ. Chic. Press, 1976). Daniel Kahneman, *Maps of Bounded Rationality: Psychology for Behavioral Economics*, 93 AM. ECON. REV. 1449, 1449 (2003).

⁶⁸ Daniel Kahneman & Amos Tversky, *Prospect Theory: An Analysis of Decision Under Risk*, 47 *ECONOMETRICA* 263, 268 (1979).

⁶⁹ RICHARD H. THALER & CASS R. SUNSTEIN, *NUDGE: IMPROVING DECISIONS ABOUT HEALTH, WEALTH, AND HAPPINESS* 40–52, 207–14 (2008).

with an electric one,⁷⁰ the installation of a thermostat or light sensors, or a voucher for planting trees.⁷¹ Other benefits that could be considered—depending on their suitability in the policy context—are premium reductions and rebates,⁷² lowering deductibles and increasing or reinstating sub-limits of liability upon the policyholder taking or refraining from specified actions.

Whether a green term has been breached may depend on how compliance is assessed or measured and whether it imposes an absolute obligation on the policyholder (or an obligation to use “best endeavors” or “reasonable endeavors”) to achieve a specified outcome. It is unlikely that there exists (yet) any methodologies for measuring GHG emissions from the operation of small businesses or from private households, but it is conceivable to set other GHG emission-related targets such as improving a specific aspect of energy efficiency (e.g., installing better insulation) or to reduce a specific carbon-intense activity (e.g., ceasing to use coal in fireplaces).

The consequences of breach of, or non-compliance with, a term, depend on the nature of the term in question. Infamously, English insurance contract law does not use the same classification scheme for contractual terms as general contract law.⁷³ This is not the place for a detailed exegesis of breach of insurance contract terms, and reference is made to the standard textbooks in the field.⁷⁴ A remedy in damages for breach of a green term may not be available if that breach itself has not caused any loss to the insurer which meets the contractual remoteness test in *Hadley v Baxendale*.⁷⁵ The insurer cannot decline liability for an insurance claim for breach of certain types of green terms, if the breach has been remedied before the insured loss occurred,⁷⁶ and/or non-compliance with the green term could not have

⁷⁰ It should also be considered how this could be tied in with ‘green reinstatement provisions.’ See *infra* Chapter 3.4.

⁷¹ *Plant a tree*, NAT’L TR., <https://www.nationaltrust.org.uk/features/plant-a-tree> (last visited Oct. 10, 2022).

⁷² See *supra* Section 3.2.

⁷³ ROBERT M. MERKIN, COLINVAUX’S LAW OF INSURANCE, c. 8, ¶ 8-004 (13th ed. 2022).

⁷⁴ See *generally id.* JOHN BIRDS, MACGILLIVRAY ON INSURANCE LAW c.10 (15th ed. 2022); JOHN BIRDS & KATIE RICHARDS, BIRD’S MODERN INSURANCE LAW c.9 (12th ed. 2022).

⁷⁵ *Hadley v. Baxendale*, (1854) 156 Eng. Rep. 145, 147; 9 LR Exch. 341, 344 (UK) (the remoteness rule laid down in this case is that losses are recoverable if they flow naturally from the breach or if they are in the contemplation of both parties at the time of entry into the contract).

⁷⁶ Insurance Act 2015, c.4, § 10(4) (UK) (applying to insurance warranties).

increased the risk of any insured loss which actually occurred in the circumstances in which it occurred.⁷⁷

With the above analysis in mind, set out below are some green term examples (excluding terms relating to claims and premium) collated, or based on clauses, from the Chancery Lane Project⁷⁸ and the Insurance Information Institute:⁷⁹

- Coverage for alternative energy sources: for homeowners who generate their own geothermal, solar, or wind power and sell any surplus energy back to the local power grid, home and contents policies could include add-on cover (at no or low extra premium) to indemnify for the costs of inspection and reconnection, the extra expense of temporarily buying electricity from another source and for the income lost during a power outage, provided the outage is caused by an insured peril.
- The insurer's consent to building works or alterations to the insured property could be made conditional upon using energy-efficient materials and building systems in the new works or alterations (or less stringently, for the policyholder to do so where it is reasonable by reference to costs and efforts).
- A knowledge and information sharing clause that prompts the policyholder to assess climate change risks and impacts and shares this information with the insurers. Further, a provision that requires the insurer to provide a report with insights related to climate-related risks and mitigation of those risks that are relevant to the policyholder during the policy year.
- Setting the policyholder, a (soft) GHG emission reduction target in connection with the insured subject-matter. When the target is met, the insurer will reward credits that can be applied towards a premium discount, towards the costs of carrying out an energy efficiency

⁷⁷ *Id.* at § 11(2). Applies to a term (express or implied) of a contract of insurance, other than a term defining the risk, if compliance with it would tend to reduce the risk of one or more of the following – (a) loss of a particular kind, (b) loss at a particular location, (c) loss at a particular time. *See id.* at § 11(1).

⁷⁸ *Climate clauses: Insurance*, CHANCERY LANE PROJ., <https://chancerylaneproject.org/practice-areas/insurance/> (last visited Oct. 10, 2022).

⁷⁹ *See Green Insurance*, *supra* note 55.

retrofit, or towards a net-zero activity or project benefitting the public. Alternatively, a (small) percentage of the premium could be returned to the policyholder to be used for an GHG emission-reducing measure in relation to the insured subject-matter or for investment in carbon sinks (such as having trees planted).⁸⁰

- Excluding from cover loss or damage caused by, or liability incurred in relation to, specified carbon-intense activities.

These sample green terms could give rise to legal issues, some of which are discussed below. Translating “green term” aspirations into workable clauses for consumer and small business policy wordings presents other challenges too: contracts of general insurance tend to have a one-year policy period which does not lend itself to committing a policyholder to sustained longer-term action. The tragedy of the commons has already been mentioned above, and it is by no means clear whether this challenge is addressed more effectively by green terms that mandate or prohibit prescribed conduct or green terms that take more of a “nudge approach”⁸¹ by rewarding GHG emission reducing behavior or outcomes. A recent insurance study has shown that “nudges” lose effectiveness if the policyholder does not trust the source of information, and if the content of the nudge is inconsistent with pre-existing beliefs.⁸² The substantive content of green terms will evolve as more scientific evidence becomes available as to how GHG can be offset, reduced, or be removed from the atmosphere, and technologies to do so become more widely available. “Green terms” is an area that would benefit from joint research by behavioral economists, environmental scientists, climate technology engineers, underwriters, brokers, and lawyers.

⁸⁰ By way of (non-insurance) example, British Airways offers customers a way to off-set their carbon footprint of the flight by making a donation to verified emission reduction projects, to which British Airways make a proportionate contribution. See *Planet: Protecting our natural environment*, BRITISH AIRWAYS, <https://www.britishairways.com/en-gb/information/about-ba/ba-better-world/planet> (last visited Oct. 10, 2022).

⁸¹ THALER & SUNSTEIN, *supra* note 69, at 72–80.

⁸² Peter J. Robinson & W.J. W. Botzen, *Setting Descriptive Norm Nudges to Promote Demand for Insurance Against Increasing Climate Change Risk*, 47 GENEVA PAPERS RISK & INS. – ISSUES & PRAC., 27, 29, 31 (2021).

D. CLAIMS

If the policyholder has made a valid claim under the contract of insurance, the insurer is required to pay the policyholder (or its beneficiary) a sum of money representing its insured loss (in indemnity insurance) or an agreed sum (in contingency insurance). This is also referred to as “cash settlement.” Subject to the terms of the policy, the policyholder (or beneficiary) can then use the settlement proceeds as it pleases.⁸³ However, property policies frequently contain the basis of settlement clauses providing for the reinstatement or repair of insured buildings or personal property that have been damaged or the replacement of lost items. These reinstatement, replacement, or repair clauses could serve as a powerful precedent for green settlement provisions that mandate or encourage the recipient to apply settlement proceeds towards the reinstatement or repair of property with low carbon materials and lower GHG emission, or the replacement of personal property with recycled or lower emission alternatives (“green reinstatement”). For example:

- Comprehensive motor insurance: after a total loss when a petrol or diesel car is “written off,” the policyholder replaces it with an electric or hybrid car. The sale of new petrol and diesel cars in the UK will be banned by 2030 as part of the UK Government’s ‘Ten Point Plan for a Green Industrial Revolution,’⁸⁴ so insurers could contribute to an earlier phasing out of petrol cars.
- Boiler breakdown insurance cover (as separate insurance or as part of home/property insurance): if a gas boiler breaks down, the policyholder replaces it with a greener alternative. A study by UK insurer More Than has found that amongst homeowners who still have a gas boiler (86%), more than two-fifths (43%) are willing to replace it with an electric one, one in four (27%) want to install a solar water heating system, and almost a fifth (19%) are looking to fit an air source heat pump.⁸⁵
- Business insurance and home insurance: upon damage to a building, the policyholder repairs or refits the building to reduce emissions

⁸³ *Rayner v. Preston* [1881] 18 Ch D 1 at 2 (Eng.).

⁸⁴ *The Ten Point Plan for a Green Industrial Revolution*, *supra* note 61.

⁸⁵ *Homeowners urged to go green as insurance claims for heating breakdowns surge*, RSA INS. (Mar. 23, 2021), <https://www.rsainsurance.co.uk/news/press-releases/2021/homeowners-urged-to-go-green-as-insurance-claims-for-heating-breakdowns-surge/>.

and increase the energy efficiency (e.g., carry out roof repairs with better insulation or replace single-glazed windows with double-glazed windows) and uses sustainable materials to do so to the extent possible.

- Contents cover (as part of business or home insurance) or insurance cover for specific assets: upon loss or damage, the policyholder has the item repaired using sustainable materials to the extent possible or accepts a recycled replacement.

There are several options for how green reinstatement clauses could be drafted in property insurance. The key variables are (1) whether there is a reinstatement (or repair or replacement) alternative to a cash settlement, (2) if there is, which party has the right to elect between a cash settlement and reinstatement (or repair or replacement), and (3) if reinstatement (or repair or replacement) applies, whether the insurer is obliged, or can be required, to affect a green reinstatement. Different options might apply to different types of insured assets within the same property policy.

1. The claim is settled by way of cash settlement. However, where applicable, upon payment, the insurer provides information on sustainable reinstatement, replacement, and repair options, including what government schemes and grants (see below) are available.
2. The insurer has the right to elect between (a) cash settlement and (b) reinstatement. If the insurer elects option (b), the insurer is entitled to elect between conventional or green reinstatement.
3. The insurer has the right to elect between (a) cash settlement and (b) reinstatement. If the insurer elects option (b), the policyholder is entitled to elect between conventional or green reinstatement.
4. The insurer has the right to elect between (a) cash settlement and (b) reinstatement. If the insurer elects option (b), the insurer is required to effect green reinstatement.
5. The insurer is obliged to reinstate but is entitled to elect between conventional or green reinstatement.
6. The insurer is obliged to effect green reinstatement.
7. The policyholder has the right to elect between (a) cash settlement and (b) reinstatement. If the policyholder elects option (a), upon payment, the insurer provides information on sustainable reinstatement, replacement, and repair options, including what government schemes and grants (see below) are available. If the

policyholder elections option (b), the insurer is entitled to elect between conventional or green reinstatement.

8. The policyholder has the right to elect between (a) cash settlement and (b) reinstatement. If the policyholder elects option (a), upon payment the insurer provides information on sustainable reinstatement, replacement and repair options, including which government schemes and grants (see below) are available. If the policyholder elects option (b), the policyholder is entitled to choose between conventional or green reinstatement.
9. The policyholder has the right to elect between (a) cash settlement and (b) reinstatement. If the policyholder elects option (a), upon payment the insurer provides information on sustainable reinstatement, replacement and repair options, including what government schemes and grants (see below) are available. If the policyholder elects option (b), the insurer is obliged to effect green reinstatement.

Option 1 is the least onerous for insurers and is also the extent to which insurers have contemplated green reinstatement provisions to date.⁸⁶ Option 8, which gives the policyholder a choice between (1) cash settlement or reinstatement, and (2) conventional or green reinstatement, may be the safest option from an “unfair terms” perspective⁸⁷ because it gives the policyholder the greatest flexibility to choose a course of action that is most favorable to its circumstances. For all options except Option 6, one of the parties can opt for a cash settlement and/or conventional reinstatement, in which case there will be no positive net-zero effect. For all options where the insurer can elect reinstatement, the insurer is reliant on the co-operation of the policyholder to give access and control to the asset to be reinstated, replaced, or repaired and, accordingly, performance of the insurer’s reinstatement obligation should be made conditional upon the policyholder’s co-operation.

Paying for green reinstatement could be more expensive than making a cash settlement or paying for conventional reinstatement depending on the materials and construction techniques used. How should

⁸⁶ *The UK’s insurance and long-term savings industry could potentially contribute one third of the investment needed to meet the UK’s Net Zero target*, ABI (July 7, 2021), <https://www.abi.org.uk/news/news-articles/2021/07/abi-climate-change-roadmap/>.

⁸⁷ *See infra* Chapter 4.4.

additional costs be allocated? In the context of property insurance, the starting point is that the insurer must indemnify the insured for the loss caused by an insured peril to the insured property, but no more than that.⁸⁸ However, the parties are, within certain limits, free to agree on how the indemnity is to be calculated.⁸⁹ The measure of indemnity can be contractually agreed upon by way of valued policies,⁹⁰ or can be reduced by contractual provisions for deductibles, retentions and limits of liability. In relation to insurance on real property, the parties may agree that the measure of indemnity is determined by reference to the cost of reinstatement of the property even if the costs of reinstatement are more than the pre-loss value of the property.⁹¹ Policies insuring personal property may offer “new for old coverage” even if the new item is more valuable than the (old) insured asset.

Thus, it is not unprecedented that insurers absorb additional costs above their liability to indemnify for the loss once they are contractually committed to reinstatement or replacement. These additional costs would then be reflected in rising premiums for all policyholders in that class of insurance or across different pools. For NZAIPs with green reinstatement provisions, this would be a method of socializing some of the costs of transitioning to a net-zero economy. Arguably, it is a relatively inefficient method given the transaction costs of insurance and its limited and contingent reach (it relies on policyholders choosing NZAIPs, that a policyholder suffers an insured loss, has a valid claim, and that green reinstatement is chosen or applies automatically). If premium levels for NZAIPs exceed what policyholders are prepared to pay, there will be no market for NZAIPs and NZAIPs will not have any impact.

On the other hand, green reinstatement is an opportunity to “build back better” with the help of the insurance industry. “Build back better” is the UK Government’s plan to support growth that, inter alia, enables the transition to a net-zero economy in the UK.⁹² Moreover, government schemes and grants available to the policyholder could be used to absorb some of the additional costs. UK environmental schemes currently available

⁸⁸ *Castellain v. Preston* [1883] 11 QBD 380, 386 (Eng.).

⁸⁹ *N. of Eng. Iron Steamship Ins. Ass’n v. Armstrong* [1870] 5 LRQB 244, 250 (Eng.).

⁹⁰ Subject to that the valuation is not fraudulent or so excessive that the policy is in the nature of a wagering contract. *See e.g.*, Marine Insurance Act 1906, c. 41, §§ 27(2), 27(3) (UK); *Lewis v. Rucker* (1761) 2 Eng. Rep. 1167; 97 ER 769 (KB).

⁹¹ MERKIN, *supra* note 73, at ¶¶ 11-159, 11-160.

⁹² HM Treasury, *Build Back Better: Our Plan for Growth*, 12 (Mar. 3, 2021), https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/969275/PfG_Final_print_Plan_for_Growth_Print.pdf.

to eligible consumers are the Boiler Upgrade Scheme⁹³ and the ECO4 Scheme,⁹⁴ and to consumers and small businesses the Smart Export Guarantee,⁹⁵ the Plug-in Vehicle Grant,⁹⁶ and the Plug-in Van and Truck Grant.⁹⁷ The Boiler Upgrade Scheme and the Plug-in Grants are one-off direct grants that are applied on the point of sale or installation.⁹⁸ If green reinstatement provisions apply, they should be supplemented by policy language to the effect that the policyholder must ensure that any rights under those government schemes are preserved and exercised where applicable, and that the policyholder will give all necessary consents and assistance to that effect. The reinstatement or replacement costs of the insurer would thus be reduced by the amount of those grants. The Smart Export Guarantee and ECO4 schemes pay matching benefits for renewable energy generated over a number of years.⁹⁹ It would be more difficult to provide for the insurer to recoup any costs under those schemes, especially as the contractual relationship with the relevant policyholder may be limited to a one-year policy period. However, there are opportunities for insurers to offer add-on cover for renewable energy sources for extra premium.

Could the government give direct grants to insurers to subsidize green reinstatement for NZAIPs to be offered at competitive premium rates? Apart from budgetary constraints, such grants could be regarded as state subsidies in conflict with state aid rules. The UK is no longer bound by EU competition rules, and the WTO's General Agreement on Trade in Services¹⁰⁰ applies primarily to the cross-border flow of services. The Subsidy Control Act 2022 provides the framework for a new, UK-wide,

⁹³ *Boiler Upgrade Scheme (BUS)*,

OFGEM, <https://www.ofgem.gov.uk/environmental-and-social-schemes/boiler-upgrade-scheme-bus> (last visited Oct. 10, 2022).

⁹⁴ *Energy Company Obligation (ECO)*,

OFGEM, <https://www.ofgem.gov.uk/environmental-and-social-schemes/energy-company-obligation-eco> (last visited Oct. 10, 2022).

⁹⁵ *Smart Export Guarantee (SEG)*,

OFGEM, <https://www.ofgem.gov.uk/environmental-and-social-schemes/smart-export-guarantee-seg> (last visited Oct. 10, 2022).

⁹⁶ *Guidance: Using the plug-in vehicle grant portal*, DEP'T TRANSP. & OFF. ZERO EMISSION VEHICLES (June 14, 2022), <https://www.gov.uk/government/publications/plug-in-vehicle-grant-portal-guidance/using-the-plug-in-vehicle-grant-portal>.

⁹⁷ *Id.*

⁹⁸ *Supra* notes 93, 96.

⁹⁹ OFGEM, *supra* note 95.

¹⁰⁰ General Agreement on Trade in Services, art. 1, ¶ 2(a), Jan. 1995.

subsidy control regime which will enable public authorities to grant subsidies aimed, inter alia, at achieving net-zero GHG emissions.¹⁰¹ However, the “energy and environment principles” with which subsidies need to be consistent do not specifically envisage subsidies that achieve an overall reduction in GHG emissions linked to private households and small businesses.¹⁰² It is suggested that it is more efficient to make grants available to policyholders, which an insurer could then take into account when a claim is settled by way of green reinstatement. Beyond the scope of this paper, but an area meriting further exploration, is the potential for public private partnerships, between public authorities and insurance companies, to use the risk management expertise and claims-related infrastructure of insurance companies supplemented by public finance, to deliver climate risk mitigation measures at the consumer level and for small businesses.

On balance, there is a case to be made for insurers adopting green reinstatement provisions in relation to specific categories of assets. At the very least, they raise awareness among consumers and small businesses that their homes and business premises can be rebuilt or repaired with low carbon materials and lower GHG emissions, and that certain types of personal property can be replaced or repaired with recycled or lower emission alternatives. At their most effective, green reinstatement provisions make a concrete contribution to the net-zero transition by enabling policyholders to remedy the loss of or damage to insured property with greener alternatives. Support for green reinstatement provisions can be derived from the Net-Zero Insurance Alliance’s commitment to “[i]mproving claims management in an environmentally sustainable manner to promote a net-zero economy”¹⁰³ and Principle 1 of the PSI which requires insurers to “[i]ntegrate ESG issues into repairs, replacements and other claims services.”¹⁰⁴

IV. LEGAL AND REGULATORY ISSUES OF NZAIPS

The legal and regulatory issues that could arise in relation to NZAIPs are too numerous, therefore this paper will limit itself to discussing the following four issues that have already been alluded to in Chapter 3: NZAIPs product design requirements, the marketing and sale of NZAIPs, corporate

¹⁰¹ Subsidy Control Act 2022, c. 23, § 9 (UK).

¹⁰² *Id.* at sch. 2 (indicating that Principle H may be limited to decarbonization linked to “industrial activities.”).

¹⁰³ Net-Zero Insurance Alliance, *supra* note 10.

¹⁰⁴ Env’t Programme, Principles for Sustainable Insurance, <https://www.unepfi.org/insurance/insurance/> (last visited Oct. 10, 2022).

purpose and shareholder value (Companies Act 2006, § 172)¹⁰⁵ and unfair contract terms (Consumer Rights Act 2015, Part 2).¹⁰⁶ The paper will make some suggestions for changes to the legal and the regulatory environment that are needed to develop and operate NZAIPs, to ensure the protection of policyholder's rights, and to maintain broad access to insurance.

A. NZAIPs PRODUCT DESIGN

The question of how insurance products can be designed or adapted to encourage or require policyholders to reduce GHG emissions and take climate action has received little public attention and scholarship so far.¹⁰⁷ Caldecott argues that, for a financial product to make a difference to the real economy's transition to environmental sustainability, the product must make a clear and measurable difference by either enabling the customer to adopt sustainable practices, or by reducing or increasing the cost of capital for green or polluting activities.¹⁰⁸

UK-regulated insurers must comply with the product design requirements in the FCA Product Intervention and Product Governance Sourcebook (PROD).¹⁰⁹ Primarily, this means that the insurer is required to have in place an internal product approval process to ensure that the design of insurance products or the adaptation of existing insurance products (1) takes into account the objectives, interests, and characteristics of customers, (2) does not adversely affect customers, and (3) prevents or mitigates customer detriment.¹¹⁰ Moreover, the product approval process must identify whether the product provides fair value to customers in the target market, including whether it will continue to do so for a reasonably foreseeable period (including following renewal).¹¹¹ In addition, insurers must test their insurance products appropriately, by assessing whether the

¹⁰⁵ Companies Act 2006, c.46, § 172 (UK).

¹⁰⁶ Consumer Rights Act 2015, c.15, §§ 61–76 (UK).

¹⁰⁷ Insurance-based investment products where the premium is invested in environmentally sustainable investments are already available. It is suggested that they are an example of “impact investment,” rather than “impact unwriting” with the objective of policyholders reducing their GHG emissions.

¹⁰⁸ Ben Caldecott, *Aligning Finance for the Net Zero Economy: New Ideas from Leading Thinkers*, CLIMATE-KIC 3 (Sep. 2020), https://www.unepfi.org/wordpress/wp-content/uploads/2020/08/200915_J932-CKIC-UNEP-ThoughtLeadershipSeries-DrBenCaldecott-11.pdf.

¹⁰⁹ PROD, *supra* note 24,

¹¹⁰ *Id.* at ¶ 4.2.8.

¹¹¹ *Id.* at ¶ 4.2.14A.

insurance product over its lifetime meets the identified needs, objectives, and characteristics of the target market before bringing that product to the market.¹¹² The product design requirements are going to be underpinned by a new “consumer duty”—to come into force on 31 July 2023—which will require insurers to deliver good outcomes for consumers, including ensuring that consumers (1) receive fair prices and quality, (2) receive suitable products and good treatment, and (3) have access to products meeting their needs.¹¹³

Thus, if the target markets for NZAIPs are consumers and small businesses, insurers need to consider their respective needs, objectives, interests, and characteristics as they relate to the type of insurance (e.g., home and content, property, motor, and business insurance). It may be necessary to granularize the target market further to focus on shared characteristics in relation to the risk profile, experience and expertise, expectations, and the needs of specific market segments.

The PROD rules and guidance do not require insurers to consider whether the insurance product as a whole has beneficial or detrimental impacts on the environment. There is no explicit requirement that an insurer must take into account the target market’s environmental objectives, if any, at the product design stage. If insurers are not prompted to consider environmental design features and the target market’s appetite for insurance products with an environmental objective, they are less likely explore the design of, and demand for, NZAIPs, and are ultimately less likely to bring NZAIPs to market. If customers do not have access to NZAIPs or other sustainable insurance products, or are not aware of them as alternatives to regular insurance products, a NZAIPs’ market is unlikely to develop any time soon.

This vicious circle of lack of supply and demand is aggravated further by the absence of a meaningful system of labeling of (insurance) products as “net-zero,” “net-zero aligned,” “green,” or “environmentally sustainable.” Without a transparent and comparable system of definitions and classification—a “Green Taxonomy”—there is yet little customer trust and confidence in those products’ green credentials.¹¹⁴ This lack of

¹¹² *Id.* at ¶ 4.2.22.

¹¹³ Fin. Conduct Auth., *A New Consumer Duty: Feedback to CP21/36 and Final Rules*, ¶ 1.19, PS22/9 (July 2022) [hereinafter *A New Consumer Duty*].

¹¹⁴ See e.g., Regulation (EU) 2020/852 of the European Parliament and of the Council of 18 June 2020 on the Establishment of a Framework to Facilitate Sustainable Investment, and Amending Regulation (EU) 2019/2088, 2020 OJ (L 198) 13, 14; Fin. Conduct Auth., *Sustainability Disclosure Requirements (SDR) and Investment Labels*, ¶ 1.3, CP22/20 (October 2022) [hereinafter SDR].

confidence affects market appetite. Ultimately, insurers are not permitted to bring insurance products to the market if the results of the product testing show that the products do not meet the identified needs, objectives, and characteristics of the target market.¹¹⁵

The PROD rules for insurance product design could be amended to integrate into the product design and approval process environmental sustainability factors and consideration of the target market's environmental objectives. By way of example, the proposed EU Insurance Distribution Directive Delegated Regulation will require insurers to: “*only design and market insurance products that are compatible with the needs, characteristics and objectives, **including any sustainability-related objectives**, of the customers belonging to the target market.*” (emphasis added; “sustainability-related objectives” include environmental objectives).¹¹⁶

A similar amendment could be made to the PROD rules. However, clarification would be needed as to the meaning of “sustainability-related objectives,” or any alternative label used (e.g., “environmental objective”). The EU has already started to address the need for a common classification system for environmentally sustainable economic activities with the EU Taxonomy Regulation.¹¹⁷ For an economic activity to qualify as environmentally sustainable, four overarching conditions must be met:

1. It contributes substantially to one or more of the six environmental objectives (see below);
2. It does not significantly harm any of the six environmental objectives;
3. It is carried out in compliance with the specified minimum safeguards;¹¹⁸ and

¹¹⁵ PROD, *supra* note 110, at ¶¶ 4.2.22R, 4.2.24R.

¹¹⁶ Commission Delegated Regulation (EU) 2021/1257 of 21 April 2021 Amending Delegated Regulations (EU) 2017/2358 and (EU) 2017/2359 as Regards the Integration of Sustainability Factors, Risks and Preferences into the Product Oversight and Governance Requirements for Insurance Undertakings and Insurance Distributors and into the Rules on Conduct of Business and Investment Advice for Insurance-based Investment Products, art. 1, 2021 OJ (L 277) 18, 20 [hereinafter Regulation 2021/1257].

¹¹⁷ See *generally* Regulation 2020/852, *supra* note 114.

¹¹⁸ These are, essentially, ensuring the alignment with the OECD Guidelines for Multinational Enterprises and the UN Guiding Principles on Business and Human Rights, including the principles and rights set out in the eight fundamental

4. It complies with technical screening criteria that have been established by the European Commission.¹¹⁹

The six environmental objectives are: (1) climate change mitigation, (2) climate change adaptation, (3) the sustainable use and protection of water and marine resources, (4) the transition to a circular economy, (5) pollution prevention and control, and (6) the protection and restoration of biodiversity and ecosystems.¹²⁰

In contrast, the FCA is proposing to introduce “sustainable investment labels” to classify and label investment products according to whether “they aim to invest”:

1. In assets that are environmentally and/or socially sustainable (“sustainable focus”);
2. To improve the environmental and/or social sustainability of assets over time, including in response to the stewardship influence of the firm (“sustainable improvers”);
3. In solutions to environmental or social problems, to achieve positive, real-world impact (“sustainable impact”).¹²¹

Under the proposals, the sustainable investment labels would not apply NZAIPs under consideration in this paper (as they are not investment products marketed by investment funds).¹²² Instead, as will be discussed below,¹²³ under the FCA proposals, a general “anti-greenwashing” rule will apply to all regulated firms, including UK insurers.

Determining whether NZAIPs provide “fair value” entails looking at the relationship between the overall price to the customer and the quality of the product and services provided, and the overall costs to the insurer.¹²⁴

conventions identified in the Declaration of the International Labour Organisation on Fundamental Principles and Rights at Work and the International Bill of Human Rights.

¹¹⁹ Regulation 2020/852, *supra* note 114, at art. 3. The technical screening criteria are intended to provide further detail on which economic activities by making a substantial contribution to the EU’s environmental goals and are set by the European Commission through delegated acts. Insurance products and activities are not amongst the economic activities for which criteria have been provided.

¹²⁰ Regulation 2020/852, *supra* note 114, at art. 9.

¹²¹ SDR, *supra* note 114, at ¶¶ 3.2, 4.3.

¹²² *Id.* at ¶ 3.5.

¹²³ *See infra* Chapter 4.2.

¹²⁴ PROD, *supra* note 110, at ¶ 4.2.14 E.

Where the difference between the risk price to the insurer and the total price paid by the customer bears no reasonable relationship to the actual costs incurred by the insurer (or any another person involved in the distribution arrangements), the quality of any benefits or the quality of any other services provided, there is a presumption that the product does not provide “fair value.”¹²⁵ Thus, if NZAIPs are too heavily reliant on exclusions¹²⁶ (e.g., for cover for carbon intense assets and activities) the remaining insurance protection might provide poor cover and is unlikely to be “fair value.” Similarly, if the level of GHG emissions of the policyholder is made a pricing factor, but the increase in premium for higher GHG emissions cannot be linked to the risk insured, there is a risk that to do so would be contrary to the “fair value” principle. Higher premium rates for NZAIPs compared to the equivalent type of conventional insurance could still provide “fair value” if the NZAIPs cover provides additional benefits and services, such as green reinstatement and risk management and advice on climate change risks and reducing emissions. However, “fighting climate change” or “reducing GHG emissions” are not in themselves (non-financial) factors relevant to the “fair value” principle.

Instead of charging higher premiums, to promote NZAIPs and to encourage GHG emission reducing behavior or outcomes within the terms of the contract of insurance, premium reductions or rebates may be needed which, as will be discussed below, presents different challenges. Where the NZAIPs design takes a modular approach to coverage—by including cover for additional risks for additional premium—the product design and product information should make this clear.¹²⁷

In addition, distribution channels and distributors must be appropriate for policyholders in the target market and must be monitored by insurers accordingly. However, as this chapter is concerned with contractual design, the governance of distribution is beyond its scope.

B. THE MARKETING AND SALE OF NZAIPs

In the UK, the marketing and sale of insurance is governed by rules and guidelines in ICOBS.¹²⁸ The key requirements are that the insurance product must be suitable for the policyholder (product suitability) and that prospective policyholders are provided with sufficient and accurate

¹²⁵ *Id.* at 4.2.14M.

¹²⁶ *See supra* Chapter 3.3.

¹²⁷ PROD, *supra* note 110, at ¶ 4.2.25.

¹²⁸ ICOBS, *supra* note 122.

information about the insurance product so that they can make an informed decision about whether to buy it (product disclosure).¹²⁹

Product Suitability: An insurer must take reasonable steps to ensure that a customer (whether the customer is a consumer or business insured) only buys an insurance policy under which he is eligible to claim benefits.¹³⁰ For example, a NZAIPs' motor policy providing cover for an electric vehicle would be unsuitable for an owner of a petrol fuel vehicle.

Prior to the conclusion of an insurance contract, an insurance distributor¹³¹ must obtain information from the customer in order to establish the customer's demands and needs for insurance.¹³² The insurance distributor must then ensure that the contract of insurance offered is consistent with these demands and needs.¹³³ In an advised sale, the insurance distributor must take reasonable care to ensure the suitability of its advice for any customer who is entitled to rely upon its judgment.¹³⁴ The customer's demands and needs in respect of their environmental preferences may be obvious from the subject-matter to be insured. For example, if the customer wants to buy motor insurance for an electric car, the insurance cover must be suitable for that risk. Conversely, if the asset to be insured is a coal plant, business property insurance that excludes cover for carbon-intense activities would be unsuitable. In other instances, the prospective customer's demands and needs in respect of environmental objectives may not be apparent, and more likely, there may be a lack of awareness that NZAIPs (or other green insurance alternatives) are available or of the benefits they offer.

Yet, under the current ICOBS product suitability rules, there is no requirement to make a suitability assessment on the customer's demands and needs in relation to environmental objectives. If consideration of the customer's environmental objectives and preferences is not part of the sales process, there is risk that such preferences will be overlooked. There is also a risk that insurance products that do not have environmental features are sold to customers who have environmental objectives, or vice versa. The proposed EU Insurance Distribution Directive Delegated Regulation¹³⁵ will

¹²⁹ *Id.*

¹³⁰ Fin. Conduct Auth., *Insurance Conduct of Business Sourcebook*, ¶ 5.1.1 (Jan. 2023) [hereinafter ICOBS].

¹³¹ An insurance distributor is an insurance intermediary selling insurance on behalf of an insurance company, or an insurer selling insurance directly to a customer. Fin. Conduct Auth., *Glossary*, 17 (Feb. 2023).

¹³² ICOBS, *supra* note 122, at ¶ 5.2.2.

¹³³ *Id.* at ¶ 5.2.2B.

¹³⁴ *Id.* at ¶ 5.3.1.

¹³⁵ Regulation 2021/1257, *supra* note 116, at art. 2(1).

require EU insurers to ascertain, as part of the suitability assessment in relation to insurance-based investment products, the (potential) customer's "sustainability preferences" which includes asking questions about whether they wish to invest in an economic activity that contributes to an environmental objective, as defined by the EU Taxonomy Regulation.¹³⁶ The EU Insurance Distribution Directive Delegated Regulation is limited to insurance-based investment products and will not apply to UK insurance distributors.

The FCA consulted on whether there should be an equivalent UK requirement that advisers should consider sustainability matters in their investment advice and ensure that their advice is suitable for consumer sustainability-related needs and preferences,¹³⁷ but this suggestion has not been included in the finalized proposals.¹³⁸ The reason for this omission may be that there are not yet, enough sustainable insurance products that would meet sustainability-related needs and preferences of customers. Yet, ascertaining such preferences at the marketing stage—e.g., by asking the customer questions in person or by way of a questionnaire prior to any contract of insurance being proposed¹³⁹—could assist in testing market appetite, collecting information on potential target markets for sustainable insurance products (which would be useful for new NZAIPs product design¹⁴⁰), and providing an opportunity for insurance distributors to raise customer awareness of sustainable product alternatives. A customer may decide against a sustainable product option on the first occasion it is offered, but knowing that such options exist, he or she may go for it the next time. Of course, if a customer has expressed a preference for a NZAIP, or another sustainable insurance product, but none of the insurance distributor's insurance products meet the prospective customer's preferences, the insurance distributor should not make any recommendation for those products,¹⁴¹ and should explain the reasons for not doing so.¹⁴²

Product Disclosure: An insurer is responsible for producing, and an insurance distributor is responsible for providing to a prospective

¹³⁶ See generally Regulation 2020/852, *supra* note 114.

¹³⁷ Fin. Conduct Auth., *Sustainability Disclosure Requirements (SDR) and Investment Labels*, ¶ 5.5, DP21/4 (Nov. 2021).

¹³⁸ See *id.*

¹³⁹ ICOBS, *supra* note 130, at ¶ 5.2.2A.

¹⁴⁰ See *supra* Chapter 4.1.130

¹⁴¹ ICOBS, *supra* note 130, at ¶ 5.2.2B.

¹⁴² This will be a requirement in relation insurance-based investment products under the amended EU Insurance Distribution Directive Delegated Regulation. See Regulation 2021/1257, *supra* note 116, at art. 2(3)(c).

customer, information about the insurance policy before the contract of insurance is concluded.¹⁴³ The customer must be given appropriate information about a policy in good time and in a comprehensible form. This must take into account the complexity of the policy and the type of customer, so that the customer can (1) make an informed decision about the arrangements proposed,¹⁴⁴ and (2) compare the insurance product to the insurance products of other providers.

In ICOBS, there are different sets of pre-contractual product information requirements for different types of insurance contracts.¹⁴⁵ However, none of them contain a specific product disclosure requirements to provide information on whether the policy pursues environmental objectives, or contains any other green or sustainability-related features. However, some of the more general information categories may be relevant to NZAIPs:

1. Significant features and benefits¹⁴⁶ or a summary of the insurance cover, including its main terms:¹⁴⁷ this could be the basis for including information on NZAIPs terms that provide for premium rebates or green reinstatement, or relate to insurance coverage for GHG emission reducing assets.
2. Significant or unusual exclusions or limitations:¹⁴⁸ this disclosure requirement could be relevant to an exclusion that places specified carbon-intense activities outside the scope of the policy cover, or deductions or sub-limits of liability relating to losses caused by carbon-intense activities. Either kind of term might be considered “unusual” if it is not one that is not normally found in comparable

¹⁴³ ICOBS, *supra* note 130, at 6.-1.1, 6.2.

¹⁴⁴ *Id.* at 6.1.5, 6.1.6B.

¹⁴⁵ *Id.* at 6.1.7-A (a policy summary for commercial customers); *id.* at 6.1.10A (an insurance product information document (“IPID”) for consumers in relation to general insurance contracts); *id.* at 6.3.1 (a disclosure statement for pure protection contracts); Fin. Conduct Auth., *Conduct of Business Sourcebook*, 13 Annex 1 (Feb. 2023) [hereinafter COBS]; *id.* at 14.2.1 (a disclosure statement for life insurance contracts).

¹⁴⁶ ICOBS, *supra* note 130, at 6 Annex 2 (pure protection contracts and/or commercial customers); COBS, *supra* note 145, at 13 Annex 1 (life insurance).

¹⁴⁷ ICOBS, *supra* note 130, at 6 Annex 3 (consumer contracts other than pure protection contracts and life insurance).

¹⁴⁸ *Id.* at 6 Annex 2 (pure protection contracts and/or commercial customers); *id.* at 6 Annex 3 (consumer contracts other than pure protection contracts and life insurance).

contracts, and also “significant” if it would tend to affect the decision of customers generally to buy.

3. Obligations at the start and during the term of the contract:¹⁴⁹ this disclosure requirement might be relevant to terms imposing a contractual obligation on the policyholder to put in place a particular GHG emission reducing measures at the start of the contract (e.g., installation of better insulation) or a continuing obligation to take such measures or to refrain/reduce certain carbon-intensive activities.
4. Obligations in the event claims are made:¹⁵⁰ this disclosure requirement could be relevant to green reinstatement provisions. For example, if property damage claims are settled by way of sustainable repairs and reinstatement, this would require the property owner’s cooperation and it is therefore important that the customer is provided with information on these matters before the contract is concluded.
5. Pricing information:¹⁵¹ it has already been noted that as “manufacturers of insurance products,” insurers must consider a product’s pricing structure and the value it provides to customers. Where an insurance policy has modular coverage sections, they should be priced separately so that it is transparent to the customer what s/he is being charged for. If a premium discount is available, there should be information as to when and to whom it applies. However, factors that are part of the general risk assessment for pricing the premium do not be priced and disclosed separately.

The FCA’s proposals for specific consumer-facing disclosure and pre-contractual product disclosure requirements are limited to investment products. NZAIPs that are not investment-based insurance products would not fall within the scope of these disclosure requirements.¹⁵² However, the FCA also proposes to introduce a new general “anti-greenwashing” rule that would apply to all financial products and services in the UK. Green-washing is a practice of gaining an unfair competitive advantage by selling a product

¹⁴⁹ ICOBS, *supra* note 130, at 6 Annex 3 (consumer contracts other than pure protection contracts and life insurance).

¹⁵⁰ *Id.* (consumer contracts other than pure protection contracts and life insurance).

¹⁵¹ *Id.* at 6 Annex 2 (pure protection contracts and / or commercial customers); *id.* at 6 Annex 3 (consumer contracts other than pure protection contracts and life insurance).

¹⁵² SDR, *supra* note 114, at ¶¶ 3.5, 5.

representing that it has environmentally friendly or sustainable characteristic, when in fact that product does not meet basic environmental or other sustainability-related standards.¹⁵³ The “anti-greenwashing” rule would require all UK regulated financial firms (including insurers) to ensure that the naming and marketing of their financial products and services “is clear, fair and not misleading, and consistent with the sustainability profile of the product or services”¹⁵⁴ Any sustainability-related claims must be proportionate to the sustainability profile of the product or services and not exaggerated. The FCA has stated that it will use this new rule to challenge firms that it considers to be potentially greenwashing their products or services, and to take enforcement action if necessary, in order to ensure better outcomes for consumers, in line with the new consumer duty.¹⁵⁵

It is suggested that, in the absence of specific sustainability-related disclosure requirements for NZAIPs that are not investment-based insurance products, an inclusive and proportionate approach to providing information on environmental objectives and green product features would be in line with the spirit of the general requirement that, when insurance distributors communicate information to a customer, they must ensure that is clear, fair, and not misleading.¹⁵⁶ Any claims that NZAIPs facilitate the reduction of GHG emissions must be evidence-based and proportionate. As discussed below, this approach may also be advisable to reduce the risk that green terms in consumer insurance contracts are found to be unfair under the Consumer Rights Act 2015, §§ 62 and 64.

Yet, given that there is no UK taxonomy that defines the meaning of “net-zero,” “environmentally sustainable,” or “green” in a consistent, transparent, and comparable way. Insurers may be reluctant to label an insurance product as NZAIPs or provide information that suggests that the product pursues environmental objectives so as not to be accused of “greenwashing.” Could the proposed “sustainable investment labels” give guidance on, or be adapted to, insurance products by analogy? The category description and criteria for each of the three “sustainable investment labels” are centered around the investment objective being sustainable. Therefore, it is not directly transferrable to insurance products. However, some of the “Principles” that have to be met to qualify for the sustainable investment labels could be applied *mutatis mutandis* to insurance products. For example:

¹⁵³ Regulation 2021/1257, *supra* note 116, at ¶ 13.

¹⁵⁴ SDR, *supra* note 114, at ¶ 6.9.

¹⁵⁵ *Id.* at ¶ 6.10. For the “consumer duty” see *supra* Chapter 4.1.

¹⁵⁶ ICOBS, *supra* note 130, at ¶ 2.2.2.

- Principle 1, Sustainability Objective: “A sustainable investment product must have an explicit environmental and/or social sustainability objective”¹⁵⁷—could be applied to insurance products that have an explicit environmental and/or social sustainability objective.
- Principle 3, Key Performance Indicators: “A firm must specify credible, rigorous, and evidence-based KPIs that measure a sustainable investment product’s ongoing performance towards achieving its sustainability objective”¹⁵⁸—could be applied to insurance products if the key performance indicators are adjusted appropriately.
- Principle 4, Resources and Governance: “A firm must apply and maintain appropriate resources, governance and organisational arrangements commensurate with the delivery of the sustainable investment product’s sustainability objective”¹⁵⁹—could be applied to insurance products.

As insurers develop NZAIPs and other green insurance products, it would be useful to extend the FCA’s sustainability labels regime to insurance products other than insurance-based investment products. This would help customers to understand better, and develop trust in, insurance products with sustainable characteristics. In line with the new “consumer duty,”¹⁶⁰ insurers should take responsibility for establishing an environment in which consumers can act in their own interests and make informed choices; good product design, a more probing product suitability assessment, and more informative product disclosure would enable consumers to do so.

¹⁵⁷ SDR, *supra* note 114, at ¶ 4.55.

¹⁵⁸ *Id.* at ¶ 4.57.

¹⁵⁹ *Id.* at ¶ 4.61.

¹⁶⁰ *See supra* Chapter 4.1; *see also A New Consumer Duty*, *supra* note 113, at ¶ 1.2.

C. CORPORATE PURPOSE: THE DUTY TO PROMOTE THE SUCCESS OF THE COMPANY

The predominant view in Anglo-American scholarship is that the purpose of a company is to create value for its shareholders.¹⁶¹ Reflecting that purpose is the common law duty of the directors of a company to act in a way to promote the success of the company. Under the Companies Act 2006, § 172(1), a director of a UK (insurance) company has a statutory duty to: “act in the way he considers, in good faith, to be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard (amongst other matters) to [amongst other matters] . . . (d) the impact of the company's operations on the community and the environment” (hereinafter the “s.172 duty”).

The § 172 duty raises questions as to the extent of which directors of an insurance company would be permitted to forego higher profits of the company by giving premium discounts, or incurring additional costs, in relation to NZAIPs. The § 172 duty is owed by the directors to the company for the benefit of its members as a whole, but not to other stakeholders (such as policyholders). Promoting the success of the company means, primarily, to create value from which shareholders will benefit.¹⁶²

As § 172(1)(d) indicates, the impact of the company’s operations on the environment is a consideration for promoting the success of the company. Accordingly, a director of an insurance company could be expected to consider the company’s strategic approach to environmental risks and impacts. As climate change has become a global threat, directors should consider whether and to what extent the company should pro-actively take climate action as part of its defensive strategy (averting reputational harm and reducing litigation risk), and as part of its offensive strategy (building a competitive advantage by developing new products meeting environmental objectives, enhancing customer loyalty and attracting talented employees

¹⁶¹ PAUL L. DAVIS, SARAH WORTHINGTON & CHRISTOPHER HARE, *PRINCIPLES OF MODERN COMPANY LAW* 249–50 (Sweet & Maxwell, 11th ed., 2021); BEATE SJÄFJELL & BENJAMIN J. RICHARDSON, *COMPANY LAW AND SUSTAINABILITY: LEGAL BARRIERS AND OPPORTUNITIES* 79–147 (Cambridge Univ. Press, 2015); Martin Gelter, *The Dark Side of Shareholder Influence: Managerial Autonomy and Stakeholder Orientation in Comparative Corporate Governance* 50 HARV. INT’L L.J. 129, 131 (2009); MATHIAS M. SIEMS, *CONVERGENCE IN SHAREHOLDER LAW* 176–78 (Cambridge Univ. Press, 2008).

¹⁶² DAVIS & WORTHINGTON, *supra* note 161.

and investment).¹⁶³ Most UK insurers (by virtue of being large UK-authorized insurance companies) are subject to a public disclosure regime that requires an annual Strategic Report, with a § 172(2) statement and a non-financial information statement.¹⁶⁴ The key reporting requirement in respect of an insurer's underwriting and investment activities is "a description of ... products and services which are likely to cause adverse impacts on the environment."¹⁶⁵ This should require disclosure in general terms of insurance coverage and/or investment provided for carbon-intense activities and assets. Although a description of products and services with a positive impact on the environment is not expressly required, a small sample survey of the most recent annual reports of Aviva,¹⁶⁶ Beazley,¹⁶⁷ Direct Line Insurance Group,¹⁶⁸ Hiscox Ltd,¹⁶⁹ Legal & General,¹⁷⁰ and RSA¹⁷¹, would suggest that insurers also report on products, services, and activities with positive impacts on the environment. Such information would tend to show that the directors have discharged their § 172 duty with regard to the impact of the company's operations on the environment. Insurers who fail to put strategies in place for climate action in their operations and through their products and services

¹⁶³ See generally DANIEL BRENNAN ET. AL., CORPORATE SOCIAL RESPONSIBILITY - THE CORPORATE GOVERNANCE RESPONSIBILITY OF THE 21ST CENTURY (Ramon Mullerat ed., Wolters Kluwer L. & Bus., 2d ed., 2011).

¹⁶⁴ See generally Companies Act 2006, c.46 (UK).

¹⁶⁵ *Id.* at § 414CB(2)(d)(i).

¹⁶⁶ See e.g., *Aviva plc: Annual Report and Accounts 2021*, AVIVA, <https://static.aviva.io/content/dam/aviva-corporate/documents/investors/pdfs/reports/2021/aviva-plc-annual-report-and-accounts-2021.pdf> (last visited Oct. 10, 2022).

¹⁶⁷ See e.g., *Annual Report and Accounts 2021*, BEAZLEY, <https://reports.beazley.com/2021-annual/static/pdf/beazley-annual-report-2021.bba23f4c.pdf> (last visited Oct. 10, 2022).

¹⁶⁸ See e.g., *Annual Report 2021*, DIRECTLINE GRP., https://www.directlinegroup.co.uk/content/dam/dlg/corporate/Documents/sustainability/sustainability-report-2021/DLG_2021_Sustainability_Report.pdf (last visited Oct. 10, 2022).

¹⁶⁹ See e.g., *2021 Annual Report*, HISCOX, LTD., https://www.hiscoxgroup.com/sites/group/files/2022-03/Hiscox_report_and_accounts_2021_0.pdf (last visited Oct. 10, 2022).

¹⁷⁰ See e.g., *2021 Annual Report*, LEGAL&GEN., <https://group.legalandgeneral.com/media/fx3kkujx/l-g-2021-annual-report-and-accounts.pdf> (last visited Oct. 10, 2022).

¹⁷¹ See e.g., *RSA Annual Report and Accounts 2021*, RSA INS., <https://static.rsagroup.com/rsa/investors/company-performance/annual-reports/rsa-annual-report-and-accounts-2021.pdf> (last visited Oct. 10, 2022).

may suffer reputational harm, compare unfavourably to their competitors, and be the subject of negative publicity, resulting in loss of market share and creating a strategic risk to overall business viability.¹⁷² Ultimately, these reputational, operational, and strategic risks could negatively reflect in the value of company and thus affect the shareholders' return on equity.

However, the § 172 duty does not permit directors to promote environmental goals at the expense of shareholders. Nor does § 172 take a "pluralist approach" whereby the directors must balance the interests of the members with those of the stakeholders.¹⁷³ The literature describes the § 172 duty as representing a philosophy of "enlightened shareholder value" where shareholders' interests are paramount, but the interests of stakeholders (including communities and the environment) are to be taken into account when determining the best way of promoting the company's success.¹⁷⁴

Is an NZAIPs underwriting strategy, that envisages premium discounts outside a corporate purpose, focused on the benefit to shareholders and value creation? The answer could be yes if "shareholder value" is seen exclusively in terms of profit maximisation for shareholders. However, public debate and scholarship is starting to shift the corporate focus from "shareholder primacy" to a wider view of engagement with stakeholders and society.¹⁷⁵ Advocates of a wider corporate purpose argue that societal issues such as climate change cannot be addressed, and can even be made worse, by companies that solely focus on (short-term) financial performance since they ignore the longer-term, economy-and-society wide negative externalities that result, by placing them outside the realm of their business

¹⁷² *Issues Paper on Climate Change Risks to the Insurance Sector*, IAIS, 1, 16 tbl.1 (July 2018), https://www.insurancejournal.com/research/app/uploads/2018/08/IAIS_and_SIF_Issues_Paper_on_Climate_Change_Risks_to_the_Insurance_Sector_-1.pdf; Maryam Golnaraghi, *Climate Change Risk Assessment for the Insurance Industry*, GENEVA ASSOC., 1, 16–19 (Feb. 2021), https://www.genevaassociation.org/sites/default/files/climate_risk_web_final_250221.pdf.

¹⁷³ DAVIS & WORTHINGTON, *supra* note 161, at 420.

¹⁷⁴ *Id.*

¹⁷⁵ For an overview of the public, political and academic debate on 'corporate purpose' see Edward B. Rock, *For Whom Is the Corporation Managed in 2020? The Debate over Corporate Purpose*, 76 BUS. LAW. 363, 363 (2021); see also SJÄFELL & RICHARDSON, *supra* note 161; FREDERICK H. ALEXANDER, *BENEFIT CORPORATION LAW AND GOVERNANCE: PURSUING PROFIT WITH PURPOSE* (Berrett-Koehler Publishers, Inc., 1st ed., 2018).

decisions.¹⁷⁶ Some jurisdictions legally recognize benefit corporations—companies whose corporate form and constitution allow them to consider other interests.¹⁷⁷ Reference is made to the discussion above on the role of insurers as net-zero enablers in line with emerging theoretical frameworks on “stakeholder capitalism,” “environmental stewardship,” and a wider meaning of “corporate purpose.”¹⁷⁸

However, even if the corporate purpose debate is moving towards a more pluralist view that envisages a link between benefitting society more widely and long-term corporate growth, this is not the legal position under the § 172 duty. Moreover, there are market practices and company constitutional issues that put pressure on directors to maximise shareholder value within a short-term horizon, rather than engaging with sustainable corporate governance practices. A study carried out by EY for the European Commission identified a number of key drivers for board short-termism, including pressure from investors with short-term investment goals; board remuneration structures that incentivise the focus on short-term shareholder value rather than long-term value creation for the company; current corporate governance frameworks and practices that do not sufficiently voice the long-term interests of stakeholders; and the limited enforcement of directors’

¹⁷⁶ *Principles for Purposeful Business*, BRITISH ACAD. 1, 8 (Nov. 2019), <https://www.thebritishacademy.ac.uk/documents/224/future-of-the-corporation-principles-purposeful-business.pdf>; Marco Rubio, *American Investment In The 21st Century: Project For Strong Labor Markets And National Development*, 1, 22 (May 15, 2019), https://www.rubio.senate.gov/public/_cache/files/9f25139a-6039-465a-9cf1-feb5567aebb7/4526E9620A9A7DB74267ABEA5881022F.5.15.2019.-final-project-report-american-investment.pdf.

¹⁷⁷ A company can register as a benefit corporation in some of the US States. See Sean Peek, *A Complete Guide to Starting a B Corp*, CO (May 5, 2020), <https://www.uschamber.com/co/start/strategy/b-corp-advantages-and-requirements>. In France, a company can register as or change its status to ‘Société à Mission’ under the Loi PACTE 2019. See *The PACTE law: for the growth and transformation of companies*, MINISTRY FIN. ECON. & INDUS. & DIGIT. SOVEREIGNTY (Sep. 11, 2019), <https://www.economie.gouv.fr/loi-pacte-croissance-transformation-entreprises#>. In the UK, a company can register as a community interest company, a special type of limited company which exists to benefit the community rather than private shareholders. Companies Act 2006, c.46, § 6 (UK). In addition, a mainstream company can formulate its corporate purpose more widely, so as to promote the success of the company for the benefit of its members by achieving those wider or other purposes. *Id.* at § 172(2) (this may protect to some extent against liability in shareholder actions).

¹⁷⁸ See *supra* Chapter 2.4; see also *supra* notes 34–36.

duties in the long-term interest of the company.¹⁷⁹ Moreover, insurance companies cannot ignore short-term performance as their regulatory solvency capital requirements are calibrated at a level to ensure their assets will be able to cover liabilities over the following 12 month period.¹⁸⁰

Insurers must therefore be careful to limit premium discounts and costs associated with NZAIPs to levels that do not negatively impact shareholder value. For insurance companies designing NZAIPs that envisage premium discounts if the policyholder achieves GHG emission reductions, it would be prudent to correlate any premium discounts to a reduction in the underwriting risk, i.e., the risk of loss or adverse change in relation to the insured subject-matter. If no data is available to support such a correlation, it might also be helpful to show a link between the premium discount and a reduction in the insurance company's wider operational, strategic, or reputational risk in order to align its NZAIPs to its primary purpose of creating shareholder value.

Insurers must engage with their shareholders to foster stewardship and to ensure their support for the creation of sustainable value for shareholders that considers the wider interests of society in stemming climate change. It has been noted that a growing number of investors are “prosocial” and would prefer their investee companies to reduce socially harmful activities connected to its business, even if this might reduce profits.¹⁸¹ Climate-conscious investors see value in their investee companies reducing GHG emissions, while improving the company's share value by taking climate action.¹⁸²

There will come a tipping point where the maximization of shareholder value is aligned with insurance business models that have clear net-zero targets to be achieved with impact underwriting—including NZAIPs—and impact investment. This tipping point will be reached when the rising costs of climate-related risks and the business opportunities of

¹⁷⁹ Rep. of the Eur. Comm'n, *Study on Director's Duties and Sustainable Corporate Governance*, ¶ 4.1 (July 29, 2020), <https://op.europa.eu/en/publication-detail/-/publication/e47928a2-d20b-11ea-adf7-01aa75ed71a1/language-en>.

¹⁸⁰ Bank Eng. Prudential Regul. Auth. [PRA], *Solvency Capital Requirement – General Provisions*, ¶ 3.3 (Jan. 1, 2016).

¹⁸¹ Oliver Hart & Luigi Zingales, *Companies Should Maximize Shareholder Welfare Not Market Value*, 2 J.L. FIN. & ACCT. 247, 250 (2017).

¹⁸² John Armour, Luca Enriques & Thom Wetzer, *Green Pills: Making Corporate Climate Commitments Credible*, 18–20 (Eur. Corp. Governance Inst., Working Paper No. 657/2022, 2022), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4190268#.

product innovation and decarbonized or decarbonizing investments can no longer be ignored.¹⁸³

As noted above, insurer’s corporate reporting should (and in the case of UK premium listed insurance companies must) include a description of its environmental policies, products, and environmental matters arising in connection with its operations.¹⁸⁴ Reporting on these matters should include clear information on an insurer’s NZAIPs offering. One of the reporting challenges is that there are still significant gaps in the analytics and data available that account for GHG emissions and reductions in underwriting portfolios.¹⁸⁵ In the absence of clear numerical data quantifying the GHG emission reductions brought about by an insurer’s NZAIPs portfolio, it is important not to overstate the GHG emission reducing impact of NZAIPs, and instead focus on the support provided for consumers and small businesses in their transition to a net-zero economy.

D. UNFAIR CONTRACT TERMS

To what extent could the green terms found in NZAIPs be at risk of unenforceability for being “unfair” to the policyholder? Unfairness of contractual term is addressed in (1) the Consumer Rights Act 2015 (“CRA 2015”), Part 2, which only applies to consumer contracts,¹⁸⁶ and (2) the Unfair Contract Terms Act 1977, which does apply to non-consumer contracts but not to insurance contracts.¹⁸⁷ Accordingly, the discussion below is limited to green terms in consumer NZAIPs.

Under the CRA 2015, an unfair term of a consumer contract is not binding on the consumer,¹⁸⁸ although the contract will continue to have effect, so far as practicable, without the unfair term.¹⁸⁹ A term is unfair if, contrary to the requirement of good faith, it causes a significant imbalance in the parties’ rights and obligations under the contract to the detriment of the consumer.¹⁹⁰ However, core terms of the CRA 2015—those that deal with

¹⁸³ *Id.* at 11.

¹⁸⁴ Companies Act 2006, c.46, § 414CB (UK).

¹⁸⁵ Maryam Golnaraghi, *Anchoring Climate Change Risk Assessment in Core Business Decisions in Insurance*, GENEVA ASS’N, 38–39 (Sep. 2022), https://www.genevaassociation.org/sites/default/files/2022-10/Climate%20Risk%203_web.pdf.

¹⁸⁶ Consumer Rights Act 2015, c.15, § 61(1) (UK).

¹⁸⁷ Unfair Contract Terms Act 1977, c.50, § 1(a), sch. 1.

¹⁸⁸ Consumer Rights Act 2015, c.15, § 62(1) (UK).

¹⁸⁹ Consumer Rights Act 2015, c.15, § 67 (UK).

¹⁹⁰ Consumer Rights Act 2015, c.15, § 62(4) (UK).

the main subject of the contract and the adequacy of the contract price—are not subject to the fairness assessment,¹⁹¹ provided such core terms are transparent and prominent.¹⁹²

Applied to consumer insurance contracts, the core term exception means that the fairness of the insuring clause, the premium level, deductible and limits, and policy exclusions cannot be challenged, provided the policy terms are transparent and prominent.¹⁹³ For the purposes of the unfair terms provisions in the CRA 2015, a term is transparent if it is expressed in plain and intelligible language and (in the case of a written term) is legible; while a term is prominent if it is brought to the consumer’s attention in such a way that an average consumer would be aware of the term.¹⁹⁴ Given that green terms are not yet widely used and an average consumer would not be aware of them, exclusions and specific deductibles and limits applying to carbon-intense activities should not be buried in the policy wording. In particular, exclusions should explain or define environmental terms and any ambiguous terms in plain and intelligible language. Otherwise, the insurer could face the risk that (1) the exclusion might be subject to the fairness assessment, and (2) the meaning most favorable to the consumer would prevail and the exclusion might not apply.¹⁹⁵

In contrast, green reinstatement provisions are unlikely to be regarded as core terms: in *Crash Services Ltd v. AXA Insurance Ltd*, the court held that a “preferred repairer clause” in a motor policy, giving the policyholder a choice of having her car repaired by an AXA approved repairer or an unapproved repairer, but where choosing the latter would mean fewer benefits and a higher excess, was a not a core term because it merely “sets out some of the detail and practicality as to how the indemnity term [being the core term] is to be satisfied.”¹⁹⁶ Similarly, in *Bankers Insurance Co Ltd v. South*,¹⁹⁷ a claims condition was held to be a non-core term.

Core terms that do not meet the “transparency and prominence” tests and non-core terms are both assessed for “fairness” with the two key ingredients of unfairness being “contrary to good faith” and “significant imbalance.” In *Makdessi v. Cavendish Square Holdings BV Parking Eye Ltd*.

¹⁹¹ Consumer Rights Act 2015, c.15, § 64(1) (UK).

¹⁹² Consumer Rights Act 2015, c.15, § 64(2) (UK).

¹⁹³ Cour de cassation [Cass] [the court of cessation] Nice, 3e civ., Feb. 26, 2014, C-96/14, obs. V. Tourrès (Fr.).

¹⁹⁴ Consumer Rights Act 2015, c.15, § 64(4) (UK).

¹⁹⁵ Consumer Rights Act 2015, c.15, § 69 (UK).

¹⁹⁶ *Crash Servs. Ltd. v AXA Ins. Ltd.* [2018] NICty 3 [101] (N. Ir.).

¹⁹⁷ *Bankers Ins. Co. Ltd. v. S. & Anor* [2003] EWHC 380, [32],[33],[35],[36] (QB).

v. Beavis,¹⁹⁸ the Supreme Court applied the following tests established by the European Court of Justice in *Aziz v. Caixa d'Estalvis de Catalunya, Tarragona i Manresa*.¹⁹⁹

1. The question whether there is a “significant imbalance in the parties' rights” depends mainly on whether the consumer is being deprived of an advantage which he would enjoy under national law in the absence of the contractual provision. In other words, this element of the test is concerned with provisions derogating from the legal position of the consumer under national law.
2. The imbalance must arise “contrary to the requirements of good faith.” That will depend on whether the seller or supplier, dealing fairly and equitably with the consumer, could reasonably assume that the consumer would have agreed to such a term in individual contract negotiations.

How would these tests be applied to a green reinstatement provision? Green reinstatement provisions do not *prima facie* fall into any of the categories of terms that are potentially unfair set out in the “grey list” in the CRA 2015, Schedule 2.

Significant Imbalance in the Parties' Rights: In indemnity insurance, the insurer undertakes to hold the insured harmless against loss by an insured peril or perils specified in the policy.²⁰⁰ Without the green reinstatement provisions, the insurer would pay the policyholder (or its beneficiary) a sum of money representing its insured loss and the insured can then use the settlement proceeds as s/he pleases.²⁰¹ In that sense, a green reinstatement provision is a derogation from (English) insurance contract law, but it is not necessarily a derogation that deprives the consumer policyholder of any advantage s/he would have had. A green reinstatement provision is arguably just another way of fulfilling the insurer's primary obligation to indemnify—to “hold harmless”—for loss. Standard property policies frequently contain basis of settlement clauses providing for the

¹⁹⁸ *Cavendish Square Holding BV v. Talal El Makdessi* [2015] UKSC 67, [105] (appeal taken from EWCA Civ.).

¹⁹⁹ Case C-415/11, *Mohamed Aziz v. Caixa d'Estalvis de Catalunya, Tarragona i Manresa (Catalunyacaixa)*, 2013 E.C.R. 164.

²⁰⁰ *Sprung v Royal Ins. (UK) Ltd.* [1996] C.L.C. 70, 75, 80 (Eng.); *Ventouris v Mountain* [1992] 2 Lloyd's Rep. 281 (Eng.).

²⁰¹ *Rayner v Preston* [1881] 18 Ch D 1 at 6–7 (UK).

reinstatement or repair of insured buildings or personal property that have been damaged, or the replacement of lost items.

A green reinstatement provision where the insured can elect between (a) cash settlement or (b) reinstatement, replacement, and repair (Options 7, 8, and 9 in Section 3.4 above), do not give rise to a disadvantage which the consumer insured would have enjoyed in the absence of the provision as the consumer insured has a choice.²⁰² On the other hand, a green reinstatement provision where the insured has no right to choose between either (a) cash settlement or (b) reinstatement, replacement, and repair, could be disadvantageous to the consumer insured if s/he has to wait longer for a reinstatement, replacement, or repair of property compared to a cash settlement. If the damaged property is the consumer insured's place of living, s/he may need alternative accommodation during the period the property is reinstated or repaired. Most consumer home insurance policies already contain provisions to that effect. A green reinstatement provision could also be disadvantageous if the consumer insured would incur costs as a result of the reinstatement, replacement, or repair that s/he would not have incurred or could have chosen not to incur upon a cash settlement. Thus, a well-drafted green cash settlement provision must not make the consumer insured liable for any part of the costs of reinstatement, replacement, or repair (by way of contribution or by applying a limit of liability) even if the costs exceed the economic loss suffered by the consumer insured.

Good faith: Even if the green reinstatement provision derogates from the legal position of the consumer insured under insurance contract law, it would not necessarily be treated as unfair. The imbalance must arise "contrary to the requirement of good faith."²⁰³ Applied to green reinstatement provisions, the question is whether an insurer, dealing fairly and equitably with the consumer insured, could reasonably assume that a consumer insured would have agreed to such a term in individual contract negotiations. In determining this question, the courts will take into account whether the term in question is common in that type of contract, whether there is an objective reason for the term, and whether, despite the imbalance it causes, the consumer is not left without protection.²⁰⁴ Green reinstatement provisions are not yet frequently used. "Dealing fairly and equitably with the

²⁰² This was the reasoning of District Judge Gilipin in *Crash Servs. Ltd. v. AXA Ins. Ltd.* [2018] NICty 3 [170] (N. Ir.) in relation to a preferred repairer clause which gave the insured a choice between approved and unapproved repairers.

²⁰³ *Makdessi v Cavendish Square Holdings BV Parking Eye Ltd. v. Beavis* [2015] UKSC 67 [105] (appeal taken from EWCA).

²⁰⁴ *Id.* at [106].

consumer” is therefore likely to require that the term is prominently and clearly set out or summarised in the pre-contractual product information provided to the consumer insured.²⁰⁵ There is an objective reason for green reinstatement provisions which is to hold policyholders harmless from loss in relation to their insured property, and to do so by reducing harmful impacts on the environment. The consumer insured is not left without protection as its insured loss is still indemnified, albeit, not by way of cash settlement.

Although the concept of a negotiated agreement in relation to standard terms is rather artificial, it is a helpful test for looking at what a reasonable consumer would have done.²⁰⁶ Objectively, a consumer insured might have reason to accept a green reinstatement provision given that any insured loss suffered is still indemnified, and arguably, a consumer insured might even be “over-compensated” if one subscribes to the view that sustainable reinstatement, replacement, or repair is “building back better.” However, this may not be the case where a consumer insured might incur additional costs as a result of the reinstatement, replacement, or repair.

If a green reinstatement provision was found to be unfair it would not be binding on the consumer insured.²⁰⁷ In relation to traditional reinstatement clauses, it has been said that if reinstatement is physically or legally impossible before the insurer (or the policyholder, as the case may be) makes his election, any purported election is void and, subject to any other terms of the policy, the insurer’s obligation reverts to making a cash settlement.²⁰⁸ If the effect of a non-binding green reinstatement provision is that the insurer’s obligation is to revert to making a cash settlement, the contract of insurance would still be capable of having effect without the green reinstatement provision and would, accordingly, continue to have effect.²⁰⁹

From the example of green reinstatement terms, some more general observations can be made: for terms not to fall foul of the fairness requirements, it is preferable to use green terms that encourage, rather than mandate, GHG emission reducing behavior, and to use rewards (premium rebates or discounts) instead of contractual penalties for non-compliance. Regardless of whether green terms fall with the core terms category, given that they are novel and probably not yet well-known and understood, it

²⁰⁵ CRA, s 64(2)

²⁰⁶ *Makdessi v Cavendish Square Holdings BV Parking Eye Ltd. v. Beavis* [2015] UKSC 67, [108] (appeal taken from EWCA).

²⁰⁷ Consumer Rights Act 2015, c.15, § 62(1) (UK).

²⁰⁸ *Anderson v. Com. Union Assurance Corp.* [1885] 55 QBD 146 at 150 (Eng.).

²⁰⁹ Consumer Rights Act 2015, c.15, § 67 (UK).

would be good practice to draw them to the policyholder's attention before the contract is concluded. That should, in any event, be the course of action of insurance distributors if requirements to ascertain a customer's sustainability preferences and to disclose sustainable product features were to be introduced.²¹⁰

There are, of course, many other legal and regulatory issues which remain to be examined in another paper, including the competition issues that could arise if insurers agree upon standard green terms and premium levels for NZAIPs, and questions as to what extent insurers' solvency capital requirements should allow capital incentives for climate risk mitigation action by insurers (or penalize underwriting and investment activities in carbon intense activities) for reasons that are not directly linked to the regulatory objectives set out in the UK Financial Services and Markets Act 2000.²¹¹

V. SUSTAINABLE DEVELOPMENT

It was noted above that insurance is a mechanism for transferring and pooling risk, and ultimately, socializing the costs of risk. NZAIPs go further by seeking to reduce climate risk (by reducing GHG emissions) and to encourage better climate risk management at the policyholder level. NZAIPs can help policyholders make more informed choices and take greater ownership in their transition to a net-zero economy. The net-zero transition pathway for consumers and small businesses can be made more "just" if they receive financial, logistical, and advisory support from the insurance industry in relation to existing insurance products that already have good market penetration and are known to consumers and small businesses. However, as explained above, insurance companies have to deliver value for their shareholders and cannot spend unlimited resources on incentivizing and subsidizing the climate risk mitigation activities of their policyholders. To socialize the costs of the net-zero transition fairly and effectively, insurance companies should be able to access government schemes and grants

²¹⁰ See *supra* Chapter 4.2.

²¹¹ See Financial Services and Markets Act 2000, c.8, §§ 2B, 2C (UK). The Governor of the Bank of England, Andrew Bailey, said that he saw no case yet for setting additional capital requirements for climate change risks, or allow capital incentives for climate risk mitigation, for reasons that are not directly linked to the PRA's regulatory objectives. William Schomberg & David Milliken, *Bank of England's Bailey unconvinced by carbon capital rules*, REUTERS (June 1 2021, 4:45 PM), <https://www.reuters.com/business/sustainable-business/reuters-events-bank-englands-bailey-unconvinced-by-carbon-capital-rules-2021-06-01/>.

available to their policyholders, aimed at reducing GHG emissions, and work in partnership with public authorities to enable consumer and small business policyholders to implement climate mitigation activities in a sustainable manner.

It is also important to remember that “climate change mitigation” is just one aspect of addressing climate change;²¹² that addressing climate change is just one of several environmental objectives;²¹³ and that addressing environmental objectives is merely a part of the SDGs in the 2030 Agenda for Sustainable Development.²¹⁴ Inevitably, there will be conflicts and complex trade-offs between different objectives and different SDGs at global and national levels, as well as in the strategic decision-making processes of businesses. Insurers who consider the development of NZAIPs must make sure that these products do not create protection gaps by increasing premiums to unaffordable levels or by excluding coverage for carbon-intense assets and activities where consumer or small business policyholders have no real choice or control over reducing GHG emissions associated with their assets and activities. Protection gaps are contrary to the principle of sustainable development because they can result in a significant financial burden for uninsured losses on affected individuals and business. Governments will be under pressure to step in and offer financial relief (with consequential effects on the taxes that need to be raised). Protection gaps

²¹² The approaches to combating climate change identified in the 2015 Paris Agreement are climate change mitigation, climate change adaptation and building loss resilience. Paris Agreement art. 4, ¶ 1, Apr. 22, 2016, T.I.A.S. No. 16-1104; *id.* at art.7, ¶ 1; *id.* at art. 8 ¶ 1.

²¹³ The environmental objectives are set out in Art.9 of the EU Taxonomy Regulation. Regulation (EU) 2020/852 of the European Parliament and of the Council of 18 June 2020 on the Establishment of a Framework to Facilitate Sustainable Investment, and Amending Regulation (EU) 2019/2088, art.9, 2020 OJ (L 198); *see also* G.A. Res. 70/1, ¶ 13, Transforming our world: the 2030 Agenda for Sustainable Development (Oct. 21, 2015) (take climate action); *id.* at ¶ 14 (conserve and sustainably use the oceans, seas and marine resources); *id.* at ¶ 15 (protect, restore and promote sustainable use of terrestrial ecosystems, sustainably manage forests, combat desertification, and halt and reverse land degradation and halt biodiversity loss).

²¹⁴ There are 17 SDGs in the 2030 Agenda for Sustainable Development setting out a route map for peace and prosperity interlinked to globally shared strategies that improve health, education, equality, inclusivity, and security. Further, they give access to natural resources; promote economic growth and innovation; stem climate change, and preserve biodiversity and ecosystems. *See generally* G.A. Res. 70/1, Transforming our world: the 2030 Agenda for Sustainable Development (Oct. 21, 2015).

may have a cascading effect on economic activities, supply chains, and the performance of loans and investments across the financial system.²¹⁵

On the other hand, if an insurer's sustainability strategy for products and investments focus too heavily on social goals, it could constrain, delay, and reduce the available resources for the development of NZAIPs. The Intergovernmental Panel on Climate Change ("IPCC") has adopted the concept of "climate resilient development" ("CRD"), which is a strategy of coordinated and integrated implementation of climate change adaptation and mitigation solutions on a fair and equitable basis, which will improve social, economic, and environmental outcomes in line with the SDGs.²¹⁶ There is no single preferred pathway or best combination of adaptation, mitigation, and other sustainable development strategies, rather:

The climate resilient development concept helps assess the extent to which solutions currently exist to meet societal goals or the extent to which an expanded solution space is required. The concept also helps assess the role of various actors, including governments, citizens, civil society, knowledge institutions, media, investors and businesses as well as assessing the need for arenas of engagement in which they can interact.²¹⁷

CRD approaches are founded in recent interdisciplinary research,²¹⁸ and have been accompanied by a shift in international policies as evidenced in the Paris Agreement, which explicitly links its objectives of climate change mitigation, adaptation, and resilience to "the context of sustainable development."²¹⁹ There are diverging views, coloured by ideological positions on economic theory, about whether "sustainable development" and CRD are different, albeit, connected concepts. For some commentators, CRD merely constitutes an extension of the language of sustainable development to give greater emphasis to the role of climate action and

²¹⁵ *Issues Paper on Climate Change Risks to the Insurance Sector*, *supra* note 172, at 14.

²¹⁶ Intergovernmental Panel on Climate Change [IPCC], *Climate Change 2022: Impacts, Adaptation and Vulnerability*, at 175, (2022), https://report.ipcc.ch/ar6/wg2/IPCC_AR6_WGII_FullReport.pdf; *id.* at 2655–2769.

²¹⁷ *Id.* at 171.

²¹⁸ For a comprehensive literature review, see *id.* at 2660.

²¹⁹ Paris Agreement, *supra* note 212, at art. 2, ¶ 1. See also *Sharm el-Sheikh Implementation Plan*, *supra* note 4, at ¶ 39

environmental protection in enhancing human and ecological well-being.²²⁰ Other commentators suggest that CRD is an enabling condition or process to achieve sustainable development,²²¹ and some view CRD and sustainable development as separate concepts with different objectives.²²²

For an insurer, a CRD approach to overall strategy and risk management (including product development) would need to be consistent with an effective system of governance and risk management, which provides for sound and prudent management of its business proportionate to the nature, scale, and complexity of its operations.²²³ “Sustainability” and “climate resilience” are not just lofty concepts that apply to current and future generations of mankind, but have a more practical and concrete meaning for insurers who need to manage their businesses in a way that delivers value for shareholders,²²⁴ guarantees their financial stability, and ensures that liabilities owed to its policyholders can be discharged.²²⁵ As risk carriers of climate change related risks,²²⁶ it would ultimately be in the insurance industry’s own long-term interest to act as enablers to the transition to a net-zero economy.

VI. CONCLUSION

The Geneva Association, a leading insurance think tank, recently provided guidance to insurers for anchoring climate change-related decisions and risk assessment holistically into their strategic decision-making processes.²²⁷ This is an “exploratory, iterative, and adaptive process . . . aspiring to a holistic approach with a view to both sides of the balance

²²⁰ Peter Ferguson & Linda Wollersheim, *The World Bank’s Resilience Discourse: Reactive Environmental Norm Diffusion and the Crisis of Global Climate Governance*, in *RETHINKING MULTILATERALISM IN FOREIGN AID* 160, 160 (1st ed., 2020).

²²¹ Intergovernmental Panel on Climate Change, *supra* note 216, at 171.

²²² See e.g., *Climate-Resilient Development: A Framework for Understanding and Addressing Climate Change*, USAID (Mar. 2014), https://pdf.usaid.gov/pdf_docs/PBAAA245.pdf.

²²³ Bank Eng. Prudential Regul. Auth. [PRA], *Conditions Governing Business*, ¶ 2.1 (Dec. 31, 2020).

²²⁴ See *supra* Chapter 4.3.

²²⁵ Bank Eng. Prudential Regul. Auth. [PRA], *Solvency Capital Requirements - General Provisions*, ¶ 2.1 (Jan. 1, 2016); Bank Eng. Prudential Regul. Auth. [PRA], *Technical Provisions*, ¶ 2.1 (Jan. 1, 2016).

²²⁶ Physical, transition and liability risk, see *supra* Chapter 2.2.

²²⁷ Maryam Golnaraghi, *supra* note 177, at 38–39.

sheet.”²²⁸ NZAIPs could be an important part of this approach as they have the potential, if designed appropriately, to support consumers and small businesses in their transition to a net-zero economy in a fair and sustainable manner. There remain significant legal and regulatory issues relating to the development, sale, and performance of NZAIPs, but the evolving legal landscape is already looking for ways to address some of these issues, and this paper has highlighted some possible solutions and areas that require further (interdisciplinary) research. NZAIPs directly support the SDG and the PSI and allow insurers to take an enabling role in a just and sustainable transition to a net-zero global economy, and it is hoped that they will take off in the next few years to deliver on their promise.

²²⁸ *Id.* at 40.

WHAT CAN'T BE INSURED: THE POLICYHOLDER'S OWN BAD ACTS

TRAVIS LUIS PANTIN*

ABSTRACT

From its early eighteenth-century beginnings, modern insurance law has been governed by what can be described as a “non-responsibility” requirement: the insured cannot recover for losses that it caused through its own misbehavior. Although this principle might seem intuitive—you should not be able intentionally to burn down your own home and then get paid for it—scholars continue to debate both the range of the principle’s application and its underlying rationale. Current theories of the requirement tend to argue that instrumental goals, such as the minimization of moral hazard or the maximization of victim compensation, ought to determine whether an insured can get coverage for its own bad acts. Yet these approaches fail to describe insurance law as it currently exists.

This Article advances a new framework that corrects this deficiency. The framework identifies two distinct elements of the “non-responsibility” requirement: (1) the insured must have had substantial control over the act that caused the loss; and (2) the insured’s act must be something that is generally regarded as inherently wrong, rather than merely prohibited. When an insurer can demonstrate both elements, coverage is almost always disallowed.

In making this argument, the Article aims to explore and articulate insurance law’s internal logic, rather than study it from the perspective of an external discipline. There are multiple benefits to this approach. First, it more accurately describes insurance law as it exists today, as well as its historical evolution. Second, it provides a normatively attractive account of the “non-responsibility” requirement’s central role in contemporary insurance law. Finally, the internalist theory of insurance law can help us better predict and justify extensions of private insurance-law concepts into vital policy areas such as healthcare and unemployment.

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I. INTRODUCTION

It is a settled principle of insurance law that “[t]here can be no valid insurance coverage which will protect or indemnify the insured or indemnitee against a loss . . . which may arise from his immoral . . . conduct.”¹ Thus, if an insured homeowner douses her house in gasoline and then sets it aflame, she cannot expect her insurer to pay for the loss.² This principle applies not just to property insurance, but to insurance generally—including policies of life insurance and liability insurance. It often prevents an insured from recovering from her insurer even when the written terms of her insurance policy would appear to protect against losses for which she was responsible.³

But what sort of “immoral . . . conduct”⁴ is sufficient to render coverage invalid? That question has been a source of controversy since the dawn of modern insurance in England at the turn of the eighteenth century. It has often been suggested that insurance cannot cover losses that the insured “intentionally” caused, or that were the result of the insured’s “illegal” acts.⁵ But these refinements offer little additional guidance. What if the insured intended the act, but not the harmful effect? What if the insured’s agents acted illegally, but not the insured herself? And what if the act was “illegal” but not immoral—as in the case of a driver who accidentally breaks a speed limit? Disputes of this kind have persisted in nearly every corner of insurance law, often becoming the linchpin questions in coverage disputes that have real consequences for policyholders and those caught in their wake.

¹ *Fidelity-Phenix Fire Ins. Co. v. Murphy*, 146 So. 387, 390 (Ala. 1933). *See e.g.*, *Solo Cup Co. v. Fed. Ins. Co.*, 619 F.2d 1178, 1187 (7th Cir. 1980) (“It is well settled that a contract of insurance to indemnify a person for damages resulting from his own intentional misconduct is void as against public policy and the courts will not construe a contract to provide such coverage.” (internal citations and quotation marks omitted)).

² *See, e.g.*, *Checkley v. Ill. Cent. R.R. Co.*, 100 N.E. 942, 944 (Ill. 1913) (“A fire insurance policy issued to anyone, which purported to insure his property against his own willful and intentional burning of the same would manifestly be condemned by all courts as contrary to a sound public policy . . .”).

³ *See infra* Section I.A.

⁴ *Fidelity-Phenix Fire Ins. Co.*, 146 So. at 390.

⁵ *See, e.g.*, Mary Coate McNeely, *Illegality as a Factor in Liability Insurance*, 41 COLUM. L. REV. 26, 27–29 (1941) (reviewing the history of prohibitions against insuring intentional or illegal acts).

The principle of insurance law that one cannot be insured against the results of one's own bad acts raises profound questions. Applying it requires making determinations about which acts are "bad" in the legally-relevant sense. One must also determine whether a particular bad act is legally attributable to the insured, and thus non-insurable, or whether it was the result of a causal chain for which we do not ultimately hold her legally responsible. These issues mirror canonical issues in other areas of law. Tort law, for example, frequently holds that a but-for cause is not "proximate" enough to a loss to allow for the assignment of legal responsibility.⁶ Criminal law makes similar distinctions; the state of mind of the actor determines whether she may be punished for her deeds.⁷ The legal frameworks that structure these areas of the law reflect, and reinforce, deeply-contestable value judgments about which kinds of risks, costs, and harms are attributable to whom. Is it, for example, the driver of a car who runs the risk of hitting a pedestrian, or is it the pedestrian who runs the risk of getting hit by an out-of-control car?⁸ As Guido Calabresi famously and enigmatically put it, the law helps us structure our shared understanding of "what-is-the-cost-of-what."⁹

This Article analyzes the multiple and overlapping sources of insurance law to show that the American legal tradition provides us with an internally coherent and normatively appealing framework for determining when an insured's own bad acts ought to preclude her from getting coverage. In practice, the framework contains two legally and conceptually distinct elements: (1) the insured must have had *substantial control* over the act that caused the loss; and (2) the insured's act must be something that is generally regarded as *inherently wrong*, rather than merely prohibited. If both of these elements can be demonstrated, typically by the insurer, then coverage is

⁶ See Jules Coleman & Arthur Ripstein, *Mischief and Misfortune*, 41 MCGILL L.J. 91, 104 (1995).

⁷ 1 WAYNE R. LAFAVE, SUBSTANTIVE CRIMINAL LAW § 5.1 (3d ed. 2017).

⁸ Cf. Coleman & Ripstein, *supra* note 6, at 104 ("Ronald Coase and Guido Calabresi independently invented law and economics when they realized that both injurer and victim cause any injury. . . . In all but the most bizarre cases, the accident could have been prevented had the victim stayed home, taken a different route, or whatever. Thus, any injury is always a joint product, which must somehow be divided between the parties." (footnotes omitted)). *Id.* at 94 ("[B]oth tort law and the institutions of distributive justice can be understood as responses to the question: who owns which of life's misfortunes?").

⁹ GUIDO CALABRESI, THE COST OF ACCIDENTS: A LEGAL AND ECONOMIC ANALYSIS 133 (1970).

almost always disallowed on the grounds that the insured was responsible for her own loss as far as insurance law is concerned. And if either of these two elements cannot be demonstrated, then a given loss generally is deemed legally insurable so long as the policy grants coverage.

Thus, for example, insurance for damages caused by the insured's own negligence is generally allowed.¹⁰ Mere negligence is not, today, considered to be something blameworthy enough to prevent the insured from getting coverage for its consequences.¹¹ But coverage for intentional torts like battery, when committed by the insured, is generally disallowed¹² on the grounds that it "would be contrary to public policy to indemnify a person for a loss incurred as a result of his own willful wrongdoing."¹³ As a result, if the policy does not contain an explicit carve-out for such coverage, courts will generally imply one.¹⁴ Note, however, that if the insured's agents—such as his employees—are the ones who commit the bad act, then insurance coverage is permitted for vicarious liability that the insured incurs.¹⁵ So long as the insured did not himself exercise direct control over his agents' bad acts, courts generally allow him to use his insurance coverage to defray the ramifications of those acts.¹⁶

¹⁰ See McNeely, *supra* note 5, at 33.

¹¹ See *infra* Section II.B.1.

¹² See, e.g., *Vt. Mut. Ins. Co. v. Ben-Ami*, 193 A.3d 178 (Me. 2018) (holding that intentional assault is not covered); *Mut. Serv. Cas. Ins. Co. v. McGehee*, 711 P.2d 826 (Mont. 1985) (holding that striking another is an intentional act within the meaning of the policy's intentional acts exclusion).

¹³ *Malanga v. Mfrs. Cas. Ins. Co.*, 146 A.2d 105, 108 (N.J. 1958). See e.g., *Thomas v. Benchmark Ins. Co.*, 179 P.3d 421, 425 (Kan. 2008) ("Kansas public policy prohibits insurance coverage for intentional acts: '[A]n individual should not be exempt from the financial consequences of his own intentional injury to another.'"); *Chiquita Brands Int'l, Inc. v. Nat'l Union Fire Ins. Co.*, 988 N.E.2d 897, 900 (Ohio Ct. App. 2013) ("Ohio public policy generally prohibits obtaining insurance to cover damages caused by intentional torts. . . . 'Liability insurance does not exist to relieve wrongdoers of liability for intentional, antisocial or criminal conduct.'" (internal citations omitted)).

¹⁴ See *infra* Section II.A.

¹⁵ See RESTATEMENT OF THE L. OF LIAB. INS. § 45 cmt. e (AM. L. INST. 2019) ("Courts generally permit insurance coverage of liabilities that are assessed vicariously, even in situations in which the liability of the primary actor would be uninsurable in the jurisdiction")

¹⁶ See, e.g., *New Amsterdam Cas. Co. v. Jones*, 135 F.2d 191, 195–96 (6th Cir. 1943).

The inner logic of this area of insurance law has generally eluded theorization by legal commentators, who have approached it through two competing frameworks. On one side are those who study insurance law from an economic standpoint. From this perspective, moral hazard concerns ought to be the primary determinant of whether a loss caused by the insured should be insurable: if allowing coverage would produce inefficient moral hazard, then coverage generally ought to be denied; if it would not, then coverage ought to be allowed so long as the parties agree to its terms.¹⁷ On the other side are those who are concerned with protecting victims of insureds' misdeeds. From this view, coverage ought to be allowed whenever doing so would benefit innocent parties—even in the situation, for example, where the insured is sued for his own intentional torts.¹⁸ Both of these frameworks analyze insurance coverage disputes from an instrumentalist perspective: coverage ought to be granted, or denied, according to whether doing so would achieve external goals.

The problem is that neither of these two frameworks accurately capture the insurance law on the books. Although courts often weigh such instrumental goals, the majority of them seldom allow an insured to receive coverage when he appears to be individually morally responsible for the relevant harm or loss he has caused.¹⁹ Because the general rules of insurance law cannot be coherently explained in terms of instrumental goals,²⁰ coverage disputes are resolved in ways that frequently appear inefficient or frustratingly formalistic, or that leave innocent victims painfully emptyhanded.

While the predominant approach to insurance law may be puzzling from the perspectives that emphasize either moral hazard or victim compensation, this Article offers a solution to the puzzle. It suggests that the majority of jurisdictions, in the majority of insurance contexts, decide coverage disputes involving a policyholder's bad acts based on a distinct conception of legal responsibility that is analogous to conceptions of legal

¹⁷ See, e.g., George L. Priest, *Insurability and Punitive Damages*, 40 ALA. L. REV. 1009, 1026 (1989). See *infra* Section III.C.1.

¹⁸ See, e.g., Christopher C. French, *Debunking the Myth that Insurance Coverage is Not Available or Allowed for Intentional Torts or Damages*, 8 HASTINGS BUS. L.J. 65 (2012). See *infra* Section III.C.2.

¹⁹ See *infra* Section I.A.

²⁰ But see *infra* notes 53–55 and accompanying text (describing some discrete types of insurance—such as mandatory medical malpractice insurance—which legislatures have explicitly reformed to prioritize victim-compensation).

responsibility applied in tort or criminal law.²¹ Understanding the conceptual and normative logic of insurance law in this way can help one to rationalize, and to predict, decisions rendered in coverage disputes of this kind.²² It can also help reformers gain a clearer picture of the legal architecture that would need to be reframed in service of alternative goals.²³

The argument proceeds in four parts. Part I describes how insurance law addresses the insurability of losses occasioned by an insured's bad acts. It begins by noting that the various sources of insurance law demonstrate a sustained commitment to allowing insurance only to cover losses for which the insured was not morally responsible—a principle that this Article will call the “non-responsibility” requirement.²⁴ It then focuses on how the

²¹ Tom Baker has distinguished at least five conceptions of “responsibility” at use in the insurance context. See TOM BAKER & KYLE D. LOGUE, *INSURANCE LAW AND POLICY: CASES AND MATERIALS* 20–24 (2017) (describing the conceptions of responsibility as “trustworthiness, accountability, causality, freedom, and solidarity”). In this Article, I use the phrase “individual responsibility” in the narrow “causal” sense of the term: A is “responsible” for x because A “caused” x, in a particular legally-relevant sense. Although the conception of causation-responsibility at work in insurance law, like the concept of proximate causation at work in tort law, draws upon popular understandings of responsibility, the two are not identical. See *infra* Section II.A.

²² Methodologically, this Article follows in the scholarly tradition that has been dubbed the “New Private Law,” in the sense that it aims to understand insurance law from an “internal perspective,” and “on its own terms.” For a description of the features of the New Private Law tradition, see Andrew S. Gold, *Internal and External Perspectives: On the New Private Law Methodology*, in *THE OXFORD HANDBOOK OF THE NEW PRIVATE LAW* 3 (Andrew S. Gold et al. eds., 2021) (“If there is a common feature that cuts across New Private Law scholarship, it is an interest in the internal point of view. Theorists want to better understand what is sometimes called private law’s self-understanding, and they seek to grasp private law concepts from that perspective.” (internal citations omitted)); John C.P. Goldberg, *Introduction: Pragmatism and Private Law*, 125 *HARV. L. REV.* 1640, 1651–63 (2012). See also William Lucy, *Method and Fit: Two Problems for Contemporary Philosophies of Tort Law*, 52 *MCGILL L.J.* 605 (2007) (listing several critiques of the New Private Law method).

²³ See *infra* Section II.A.

²⁴ The goal in choosing this term is to show that this principle is of similar importance to other equally foundational principles of insurance law, particularly the “insurable interest” requirement and the “indemnity” requirement. See ROBERT

requirement is applied in one area of insurance law that is currently a source of heated dispute. Contemporary liability insurance policies typically carve out coverage for property loss or injuries that were “expected or intended from the standpoint of the insured.”²⁵ This phrase has been interpreted in roughly three ways by U.S. courts, with important implications for disputants. I suggest that although the two prominent instrumentalist frameworks for thinking about this problem can explain the two minority positions, neither can explain the third, majority rule.

Part II aims to succeed where other scholarly treatments of this area have failed. It lays out a theory of the non-responsibility requirement, and fleshes out what insurance law generally means when it asks whether an insured exercised substantial control over an act, and whether the act was inherently wrong (*i.e.*, a *malum in se* rather than a *malum prohibitum*). It shows that insurance law’s own conception of individual responsibility can make sense of the outcomes that usually result when courts deal with coverage disputes involving the insured’s own misbehavior. It fits the law that we have on the books.

Part II also shows that the normative open-endedness of the non-responsibility analysis gives this area of insurance law a distinctive dynamism. It traces the history of three types of insurance coverage that were once disallowed but today are permitted. As social understandings of these types of acts evolved, insurance coverage was able to evolve with them in order to keep insurance law in sync with broader social understandings of the distinction between misbehavior and misfortune. Thus, for example, in the nineteenth century, suicide was considered to be such a heinous act that it necessarily voided any life insurance coverage—even if the policy did not explicitly exclude it as a cause of death. Over time, social perceptions of suicide changed, such that it gradually came to be regarded as the result of mental illness. Courts and legislatures recognized this shift and re-interpreted the non-responsibility requirement accordingly to allow for suicide coverage. With some exceptions, suicide remains insurable today.

Part III offers a normative argument in favor of the non-responsibility requirement. It suggests that deciding insurance coverage cases on the basis of a conception of individual responsibility is justifiable

E. KEETON & ALAN I. WIDISS, INSURANCE LAW: A GUIDE TO FUNDAMENTAL PRINCIPLES, LEGAL DOCTRINES, AND COMMERCIAL PRACTICES § 3.1 (Practitioner’s ed.1988); Kenneth S. Abraham, *Peril and Fortuity in Property and Liability Insurance*, 36 TORT & INS. L.J. 777, 780 (2001).

²⁵ See *infra* note 59 and accompanying text. See generally *infra* Section I.B.

against the backdrop of a more general commitment to a liberal-egalitarian political philosophy. It also suggests that our current institutional arrangement—with its delegation of different roles to insurers, insureds, and courts—is defensible given the various parties' competencies. The two main alternative instrumental theories, by contrast, are not well-suited to a legal process of dispute resolution centered on courts.

Finally, Part IV elaborates on the practical implications of the legal, conceptual, and normative framework described in this Article, especially as it relates to the recently-published *Restatement of the Law, Liability Insurance* (“*RLLI*”).²⁶ It also shows how an understanding of the inner logic of this part of insurance law can be informative for those who would seek to revise insurance law—either to reduce moral hazard or to increase the likelihood that innocent third-parties will be compensated.

Before proceeding, it is worth addressing a potential objection that might be raised at the outset. It could be argued that the insurance law principle I am here calling the non-responsibility requirement ought to be understood as merely one application of a more general principle that traverses various fields of law: that a wrongdoer ought not to profit from his own wrong. This idea is stated particularly clearly in the 1889 New York Court of Appeals case of *Riggs v. Palmer*,²⁷ which was recently made famous by Ronald Dworkin in his discussion of legal positivism.²⁸

²⁶ See generally *RESTATEMENT OF THE L. OF LIAB. INS.* (AM. L. INST. 2019).

²⁷ *Riggs v. Palmer*, 22 N.E. 188 (N.Y. 1889). The facts in *Riggs* are simple. Elmer Palmer murdered his grandfather in order to prevent him from changing his will in a way that would prevent Elmer from inheriting the bulk of his grandfather's estate. *Id.* at 188–89. Elmer was then convicted and imprisoned for the murder. *Id.* at 191. Elmer's aunts, Mrs. Riggs and Mrs. Preston, sued to prevent Elmer from inheriting under the will. *Id.* They argued that Elmer should be denied his inheritance for equitable reasons, even though nothing in the plain language of New York's statute of wills prevented a murderer from inheriting his victim's estate. *Id.* at 189. The New York court of appeals split, with the majority, led by Judge Earl, holding for Elmer's aunts. *Id.* at 191.

²⁸ In *Riggs*, the court declared it to be a “fundamental maxim[] of the common law [that no] one shall be permitted to profit by his own fraud, or to take advantage of his own wrong, or to found any claim upon his own iniquity, or to acquire property by his own crime.” *Id.* at 190. The court further argued that such “maxims are dictated by public policy, have their foundation in universal law administered in all civilized countries, and have nowhere been superseded by statutes.” *Id.*

It is certainly true that this “maxim”²⁹ is recognized and applied beyond the context of insurance law—*Riggs* was a dispute about wills, not insurance. But the meaning of this maxim has been particularly well-explored in the context of insurance coverage disputes, such that it is properly regarded as a principle of *insurance* law.³⁰ In practice, this is evidenced by the fact that disputes over insurance coverage for an insured’s own bad acts almost never cite cases beyond the insurance context, whereas such insurance disputes often serve as paradigmatic cases for applications and restatements of the “maxim” beyond the field of insurance. Indeed, the *Riggs* court’s declaration of the universal principle relied principally on a life

Dworkin uses “Elmer’s Case” to argue several points, “the most important” of which is that “the dispute about Elmer was not about whether judges should follow the law or adjust it in the interests of justice. . . . It was a dispute about what the law was, about what the real statute the legislators enacted really said.” RONALD DWORKIN, *LAW’S EMPIRE* 20 (1986). *See also id.* at 15–20, 36–44 (discussing *Riggs*); RONALD DWORKIN, *TAKING RIGHTS SERIOUSLY* 23–45 (1977) (discussing *Riggs*); Charles Silver, *Elmer’s Case: A Legal Positivist Replies to Dworkin*, 6 L. & PHIL. 381 (1987) (discussing Dworkin’s treatment of *Riggs*); Rodger Beehler, *Legal Positivism, Social Rules, and Riggs v. Palmer*, 9 L. & PHIL. 285 (1990) (discussing Dworkin’s treatment of *Riggs*).

²⁹ *Riggs*, 22 N.E. at 190–91. *Cf.* *Columbia Ins. Co. of Alexandria v. Lawrence*, 35 U.S. 507, 518 (1836) (“Fraudulent losses are necessarily excepted upon principles of general policy and morals; for no man can be permitted, in a court of justice, to allege his own turpitude as a ground of recovery in a suit.”).

³⁰ Several such reasons are available. First, insurance presents one of the few legal mechanisms whereby an everyday citizen can get financial “leverage” on his misdeeds, and so it is particularly likely to produce disputes that turn on this maxim. Second, principles of insurance contract interpretation prompt courts to construe ambiguities in insurance policies in favor of coverage. *See infra* notes 36–37 and accompanying text (discussing these interpretive doctrines). This allows misbehaving insureds to slip through insurers’ attempts to craft policy terms to deny them coverage. Such situations increase insurance law’s tendency to decide coverage disputes on the basis of general principles, rather than specific policy provisions. Third, because the insurance business is often regarded as a “vital service labeled quasi-public in nature,” *Egan v. Mut. of Omaha Ins. Co.*, 620 P.2d 141, 147 (Cal. 1979), courts are particularly prone to resolving coverage disputes on the basis of general principles rather than specific contract provisions. *See generally* *Carter v. Carter*, 88 So. 2d 153, 157 (Fla. 1956) (discussing the particular salience to insurance of the “axiom of the common law, supported by admirable concepts of common justice, that no person should be permitted to benefit from his own wrong.”).

insurance case.³¹ Insurance law's particularly rich internal development of this maxim thus enables it to illuminate other areas of the law and to help us understand the maxim's meaning more precisely. As the paradigmatic application of this principle, the non-responsibility requirement warrants, and can sustain, focused analytical study.

II. THE PUZZLE OF THE NON-RESPONSIBILITY REQUIREMENT

This Part begins, in Section A, with a brief survey of the manifestations of the non-responsibility requirement in insurance law. It shows that the principle is present in the law governing multiple different types of insurance and that it is also present across different sources of insurance law—including the common law, statutes, and standardized insurance policy forms.

Section B illustrates the types of debates to which this principle gives rise in practice, by focusing on one contemporary split in legal authority. States are divided over how to interpret standard liability insurance policy language that denies coverage for injuries or property damages that were “expected or intended from the standpoint of the insured.”³² The meaning that courts give to this language matters, because it often determines whether insureds are covered for harms they have inflicted on third parties, and thus, whether the third parties are able to receive compensation from an otherwise judgment-proof insured.³³

Section C shows how the two prominent theoretical frameworks for thinking about the non-responsibility requirement generally fail to capture the position that the majority of courts have taken on the question discussed in Section B. This suggests that insurance law, as it exists in practice, has developed a separate analytical framework for deciding these cases.

³¹ *Riggs*, 22 N.E. at 190 (citing *N.Y. Mut. Life Ins. Co. v. Armstrong*, 117 U.S. 591 (1886) (holding that a person who procured a policy upon the life of another, and then murdered him, could not recover under the policy)).

³² See *infra* note 59 and accompanying text.

³³ See Stephen G. Gilles, *The Judgment-Proof Society*, 63 WASH. & LEE L. REV. 603 (2006).

A. THE NON-RESPONSIBILITY REQUIREMENT IN INSURANCE LAW

It has long been held as a matter of common law that there are certain types of wrongful conduct for which an insured cannot be indemnified— notwithstanding provisions in his written insurance policy that could be interpreted to the contrary.³⁴

In practice, this doctrine arises when an insurer raises it as a defense to an insured's claim for coverage. Thus, for example, an insured might intentionally burn his own property and demand that the insurer cover the loss because their written agreement did not clearly carve-out coverage for *intentional* fires. In response, the insurer argues that common law doctrine implies such a carve-out into every insurance agreement.³⁵ Courts have often allowed the insurer to prevail in such disputes.³⁶ In doing so, they depart from the more general tendency in U.S. insurance law to resolve disagreements between insurers and insureds in the insureds' favor.³⁷ Thus,

³⁴ See Sean W. Gallagher, Note, *The Public Policy Exclusion and Insurance for Intentional Employment Discrimination*, 92 MICH. L. REV. 1256, 1256–62 (1994); McNeely, *supra* note 5, at 31–32; Edwin H. Abbot, Jr., *The Meaning of Fire in an Insurance Policy Against Loss or Damage by Fire*, 24 HARV. L. REV. 119, 120 (1910).

³⁵ Cf. *Ambassador Ins. Co. v. Montes*, 388 A.2d 603 (N.J. 1978).

³⁶ See, e.g., *Checkley v. Ill. Cent. R.R. Co.*, 100 N.E. 942, 944 (Ill. 1913) (“A fire insurance policy issued to any one which purported to insure his property against his own willful and intentional burning of the same would manifestly be condemned by all courts as contrary to a sound public policy . . .”). See also 10A STEVEN PLITT ET AL., COUCH ON INSURANCE § 149:45 (3d ed., Westlaw, database updated Nov. 2022) (“It is firmly and indisputably established that an insured under a fire policy who personally burns the property, or causes the property to be burned, may not recover under the policy.” (citing cases)); 1 WARREN FREEDMAN, RICHARDS ON THE LAW OF INSURANCE § 1:13 (6th ed. 1990) (“[T]he insured who intentionally burns his own barn is not entitled to collect the insurance on it!”). But see *Montes*, 388 A.2d at 607–08.

³⁷ For example, courts usually put a thumb on the insureds' side of the scale by interpreting any ambiguities in an insurance contract *contra proferentem*—“against the offeror,” which is almost always the insurer—and so in a manner that expands, rather than limits, coverage. On the insurance law rules that are explicitly policyholder friendly, see Kenneth S. Abraham, *A Theory of Insurance Policy Interpretation*, 95 MICH. L. REV. 531 (1996). Such rules have been in place since at least the mid-nineteenth century. See, e.g., CHARLES JOHN BUNYON, THE LAW OF FIRE INSURANCE 53 (London, Charles & Edwin Layton 1867) (discussing *contra*

although the common law generally takes steps to protect insureds against stingy insurers, when this tendency conflicts with the more specific common law doctrine against indemnifying the insureds' own wrongful conduct, the latter generally wins.³⁸

The doctrine was first developed in England in disputes involving the two oldest forms of insurance: marine insurance and fire insurance.³⁹ If

proferentem); *Moulor v. Am. Life Ins. Co.*, 111 U.S. 335, 341–42 (1884) (doctrine making the transition from fire insurance to life insurance).

³⁸ The cases in support of this proposition are too numerous to cite but are well-referenced in the many insurance law treatises that restate this proposition. *See, e.g.*, 7 PLITT ET AL., *supra* note 36, at § 101:22 (“Public policy generally requires that the policy be read as implicitly excluding coverage for intentional acts”); *Grinnell Mut. Reins. Co. v. Jungling*, 654 N.W. 530, 537–38 (Iowa 2002) (quoting 7 PLITT ET AL., *supra* note 36, at § 102:22 to identify the general rule in insurance law) (“[e]ven where the insurance policy ‘is silent as to intentional wrongs and merely states positive coverage in terms sufficiently broad to encompass intentional conduct, public policy general requires that the policy be read as implicitly excluding coverage for intentional acts.’”); 4 ERIC MILLS HOLMES, *HOLMES’ APPLEMAN ON INSURANCE* § 23.4, at 504 (2d ed., LEXIS, database updated Jan. 2010) (“Public policy will not permit an insured to benefit from his or her own intentional wrongdoing.”); *id.* § 116.1 (“The general insurance rule is that harm intentionally caused by an insured is *not covered* by *any* liability insurance policy. . . . [T]he general rule is that an insured’s intentionally caused harm to another would not be covered by a liability insurance policy.” (emphasis in text)); 44 C.J.S. *Insurance* § 490, Westlaw (database updated March 2022) (“In general insurance to indemnify insured against his own violation of law is void as against public policy.”); WILLIAM R. VANCE, *HANDBOOK ON THE LAW OF INSURANCE* 90–91 (Bust M. Anderson ed., 3d ed. 1951) (“The contract does not contemplate granting indemnity for a loss which is due to the intentional act of the insured, for one of the requisites of insurance is that the risk shall not be subject in any wise to the control of the parties. Upon this principle . . . the insurer is not required to indemnify the insured for a loss that has been caused by his own wrongful act. The insured may not recover for the loss of a ship which he has scuttled, or of a building that has been burned by himself while sane” (citations omitted)). *But see Jungling*, 654 N.W.2d at 541 (finding that public policy did not require barring coverage for intentional acts by the insured and describing this as “the emerging exception” to “the general rule”).

³⁹ *See* Mary Coate McNeely, *The Genealogy of Liability Insurance Law*, 7 U. PITT. L. REV. 169, 169–71 (1941) (on the difficulty of selecting a historical beginning point for insurance, but noting that marine insurance had existed in some form since at least the thirteenth century, that fire insurance arose following the

an owner of a marine insurance policy intentionally scuttled his ship, courts permitted the underwriter to refuse to pay.⁴⁰ Life insurance, the third-oldest form of insurance,⁴¹ applied a similar rule: if the policyholder committed suicide while sane, his coverage would be void.⁴² Newer types of insurance have also generally been held not to provide coverage for the insured's own wrongdoing. Liability insurance, for example, which arose only at the end of the nineteenth century, has long limited coverage to personal injury or property damage that was "caused by accident."⁴³

In the United States, insurance law was originally governed by state law, and for historical reasons, remains relatively free from federal regulation.⁴⁴ Common law rules have had a strong influence on state statutes that govern the business of insurance. Thus, several states have codified the common law principle that precludes insurance coverage for the insured's own bad acts. California Insurance Code § 533, for example, provides that "[a]n insurer is not liable for a loss caused by the willful act of the insured . . ."⁴⁵ Massachusetts law states that "no company may insure any

Great Fire of London in 1666, that life insurance "was little recognized before 1750," and that liability insurance "is a phenomenon of the past few decades"). *See also* KENNETH S. ABRAHAM, *INSURANCE LAW AND REGULATION: CASES AND MATERIALS* 576 (2005); MORTON J. HORWITZ, *THE TRANSFORMATION OF AMERICAN LAW, 1780-1860* 226-37 (1977).

⁴⁰ *See* *Nw. Mut. Life Ins. Co. v. Linard*, 498 F.2d 556, 561 (2d Cir. 1974) (reviewing English law decisions).

⁴¹ *See* *McNeely*, *supra* note 39, at 171 (noting that life insurance "was little recognized before 1750.").

⁴² *See, e.g.*, *Ritter v. Mut. Life Ins. Co.*, 169 U.S. 139, 160 (1898); *Supreme Commandery of Knights of the Golden Rule v. Ainsworth*, 71 Ala. 436 (1882). *See also infra* Section II.B.2 (discussing history of insurability of suicide).

⁴³ *See* Sam P. Rynearson, *Exclusion of Expected or Intended Personal Injury or Property Damage Under the Occurrence Definition of the Standard Comprehensive General Liability Policy*, 19 *FORUM* 513, 514 (1984). For a discussion of more recent language, see *infra* Section I.B. *See also* *McNeely*, *supra* note 5 (discussing early forms of liability insurance and their limitations of coverage for intentional harms).

Health insurance has similarly been held to not be available for self-inflicted injuries. *See, e.g.*, *Hussar v. Girard Life Ins. Co.*, 252 So. 2d 374, 374 (Fla. Dist. Ct. App. 1971).

⁴⁴ *See* ABRAHAM, *supra* note 39, at 104-17 (discussing history of insurance regulatory structure in the United States).

⁴⁵ CAL. INS. CODE, § 533 (West 2023). *See* *J.C. Penney Cas. Ins. Co. v. M.K.*, 804 P.2d 689, 694 (Cal. 1991) (interpreting § 533 to function as "an implied

person against legal liability for causing injury . . . by his deliberate or intentional crime or wrongdoing”⁴⁶ Many states have also passed statutes prohibiting insurance for punitive damages arising out of intentional conduct.⁴⁷ Insurance policies are interpreted in light of these statutes, in order to preclude misbehaving insureds from receiving coverage.⁴⁸

The common law doctrine is also evidenced in the language of insurance agreements themselves. Because the private insurance relationship is based on a written contract (known, in insurance terminology, as an insurance “policy”) that describes the obligations of the insurer and the

exclusionary clause which by statute is to be read into all insurance policies.”). On California’s § 533 generally, see James M. Fischer, *Accidental or Willful?: The California Insurance Conundrum*, 54 SANTA CLARA L. REV. 69, 82 (2014); Donald F. Farbstein & Francis J. Stillman, *Insurance for the Commission of Intentional Torts*, 20 HASTINGS L.J. 1219, 1245–51 (1969).

Several other states have adopted similar statutes. *See, e.g.*, MONT. CODE ANN. § 28-2-702 (West 2023) (“[A]ll contracts that have for their object, directly or indirectly, to exempt anyone from responsibility for the person’s own fraud, for willful injury to the person or property of another, or for violation of law, whether willful or negligent, are against the policy of the law.”); N.D. CENT. CODE § 26.1-32-04 (2023) (“An insurer is not liable for a loss caused by the willful act of the insured, but the insurer is not exonerated by the negligence of the insured or of the insured’s agents or others.”). *See also* MASS. GEN. LAWS ANN. ch. 175, § 47 (West 2022) (“[N]o company may insure any person against legal liability for causing injury, other than bodily injury, by his deliberate or intentional crime or wrongdoing”). Massachusetts courts have interpreted this statute to disallow coverage for intentional acts. *See, e.g.*, *Rideout v. Crum & Forster Com. Ins.*, 633 N.E.2d 376, 378 (Mass. 1994). It appears that the California, Montana, and North Dakota statutes originated in the Field Code. *See* Farbstein & Stillman, *supra* note 45, at 1245; *Stanley v. Columbia Cas. Co.*, 147 P.2d 627, 630–31 (Cal. Ct. App. 1944) (noting that the 1935 codification of California law worked no significant change to the predecessor of § 22, former Civil Code § 2527).

⁴⁶ MASS. GEN. LAWS ANN. ch. 175, § 47 (West 2022). Massachusetts courts have interpreted this statute to disallow coverage for intentional acts. *See, e.g.*, *Rideout*, 633 N.E.2d at 378.

⁴⁷ *See* Catherine M. Sharkey, *Revisiting the Noninsurable Costs of Accidents*, 64 MD. L. REV. 409, 422–34 (2005).

⁴⁸ Insurers are commonly prevented from agreeing to cover acts that are excluded by these statutes. *See, e.g.*, *Shell Oil Co. v. Winterthur Swiss Ins. Co.*, 15 Cal. Rptr. 2d 815, 830–31 (Cal. Ct. App. 1993); *Ohio Cas. Ins. Co. v. Clark*, 583 N.W.2d 377, 385 (N.D. 1998). On the incorporation of the non-responsibility requirement into state law, see 7 PLITT ET AL., *supra* note 36, at § 101:27.

insured, courts often look to the language in such documents first to resolve disputes between the parties.⁴⁹ Such policies contain language that clearly denies coverage for certain types of losses, and they usually contain language that carves-out coverage for losses that the insured “intended” or are the result of his own fault in some other sense.⁵⁰ When such carve-outs are unambiguous, courts typically end the analysis there and find for the insurer.⁵¹ Because insurance policies generally take the shape of fill-in-the-blank “forms” that have been standardized across insurers and locations, coverage disputes of this type often depend on the interpretation of nearly-identical language.⁵² Such standardized policies thereby exercise a great deal of influence in insurance law and provide helpful evidence of its underlying principles.

Although courts, legislatures, and insurers do not have a discrete name for the doctrine, the various sources of insurance law evidently concur that insurance coverage generally must not be extended to the bad acts of the insured herself. The requirement is often described as arising out of “public policy” considerations that apply to the operation of insurance with special relevance and force.⁵³ This Article carves out a place in insurance law for this proposition as a standalone legal principle. The core of the argument is a concept this Article terms the “non-responsibility requirement.” Although this phrase has not explicitly been used by courts, it captures the underlying logic of their decisions: it is a requisite of coverage that the insured herself was not responsible for the underlying loss. This Article argues that that this concept is at work in both the doctrine and the practice of insurance law. Insurance law is suffused with concern for the responsibility of the insured for her own otherwise-covered losses. I also claim that there are good reasons

⁴⁹ See *infra* Section III.B.2.

⁵⁰ See *infra* Section I.B.

⁵¹ See, e.g., *Freightquote.com, Inc. v. Hartford Cas. Ins. Co.*, 397 F.3d 888, 896 (10th Cir. 2005) (applying Kansas law) (“[I]nsurance policies are to be enforced as written so long as the terms do not conflict with pertinent statutes or public policy.”) (internal quotations omitted); *Farmland Mut. Ins. Co. v. Scruggs*, 886 So. 2d 714 (Miss. 2004).

⁵² The Insurance Services Office (“ISO”) provides standardized policy language to insurance companies across jurisdictions. See *Harford Fire Ins. Co. v. Cal.*, 509 U.S. 764, 772 (1993) (describing the functions of the ISO).

⁵³ See, e.g., *Thomas v. Benchmark Ins. Co.*, 179 P.3d 421, 425 (Kan. 2008) (“Kansas public policy prohibits insurance coverage for intentional acts: ‘[A]n individual should not be exempt from the financial consequences of his own intentional injury to another.’”).

to think this concern, and the resultant denials of coverage, are normatively justifiable. To the extent that academic treatment of insurance law has denied those claims, it has misdescribed insurance law, mistaken the moral situation, or both.

Admittedly, the non-responsibility requirement does not apply with the same strength in all contexts. In certain areas of insurance law, state legislatures or regulators have intervened to override the general common law prohibition against coverage for willful or intentional harms. Historically, such interventions have been made when it was determined that neither private insurance nor tort were providing a legal apparatus capable of appropriately compensating a class of particularly vulnerable victims. Workers' compensation laws, mandatory automobile liability insurance laws, and medical malpractice insurance requirements⁵⁴ can all be viewed as efforts to mandate both that insurance be purchased and that it provide coverage that minimally compensates third-party sufferers.⁵⁵ In such contexts, courts often override insurance law's non-responsibility requirement, as well as policy terms that would seem to reflect it, by averting to the legislature's expressed desire to revise the common law in order to protect victims.⁵⁶ That such legislative intervention is necessary, however,

⁵⁴ The Affordable Care Act's "individual mandate" can be understood along similar lines. See Patient Protection and Affordable Care Act (PPACA), Pub. L. No. 111-148, 124 Stat. 119 (2010) (as amended by the Healthcare and Education Reconciliation Act, Pub. L. No. 111-152, 124 Stat. 1029 (2010)).

⁵⁵ See Erik S. Knutsen, *Auto Insurance as Social Contract: Solving Automobile Insurance Coverage Disputes Through a Public Regulatory Framework*, 48 ALBERTA L. REV. 715, 720 (2011); Fleming James, Jr., *Accident Liability Reconsidered: The Impact of Liability Insurance*, 57 YALE L.J. 549 (1948).

⁵⁶ See, e.g., *Aetna Life & Cas. Co. v. McCabe*, 556 F. Supp. 1342, 1353 (E.D. Pa. 1983) (finding that intentional harm was covered by a medical malpractice liability policy because of Pennsylvania's "strong interest in compensating Pennsylvania victims of malpractice for injuries suffered at the hands of Pennsylvania physicians . . ."); *Nationwide Mut. Ins. Co. v. Roberts*, 134 S.E.2d 654, 659 (N.C. 1964) ("The primary purpose of compulsory motor vehicle liability insurance is to compensate innocent victims who have been injured by financially irresponsible motorists. Its purpose is not, like that of ordinary insurance, to save harmless the tortfeasor himself. Therefore, there is no reason why the victim's right to recover from the insurance carrier should depend upon whether the conduct of its insured was intentional or negligent. . . . The victim's rights against the insurer are

reveals that these areas of insurance law are exceptions that prove the rule. Moreover, as discussed below, because these types of private insurance remain rooted in principles of insurance law generally, they are constantly subjected to a gravitational pull back towards the default rule that an insured cannot be covered for his own bad acts.⁵⁷

B. THE “EXPECTED OR INTENDED” DEBATE IN LIABILITY INSURANCE LAW

Since liability insurance became available in the late nineteenth century, insurers have inserted language into the policies that reflected the non-responsibility requirement.⁵⁸ Such language has evolved over time in response to market forces and judicial interpretations.⁵⁹ Today, the language typically states that coverage will not be allowed for “bodily injury or

not derived through the insured as in the case of voluntary insurance.”); *Wheeler v. O’Connell*, 9 N.E.2d 544, 546–47 (Mass. 1937). *See also* Gallagher, *supra* note 34, at 1275 n.87 (discussing the auto insurance preference for victim compensation at length); KEETON & WIDISS, *supra* note 24, at 517.

When states have declined to make malpractice insurance coverage mandatory, this has weighed against allowing victim compensation concerns to override the non-responsibility requirement. *See, e.g.*, *Am. Home Assurance Co. v. Stone*, 61 F.3d 1321, 1328 (7th Cir. 1995), *as modified* (Aug. 24, 1995).

⁵⁷ *See infra* Section I.C.

⁵⁸ *See* McNeely, *supra* note 5 (discussing such language in the context of different kinds of liability insurance).

⁵⁹ “Prior to the mid-1960s, liability policies typically contained an exclusion that provided that ‘bodily injury or property damage caused intentionally by or at the direction of the insured’ would not be covered.” ROBERT H. JERRY, II, UNDERSTANDING INSURANCE LAW § 63C at 479; Rynearson, *supra* note 43, at 518 (on the history of development of this language). The language was arguably ambiguous, however, with regard to whose viewpoint ought to be used to determine whether a loss was “caused intentionally.” *Id.* at 521–23. Some courts held that the victim’s viewpoint ought to be dispositive—likely in an attempt to provide financial relief for sufferers of intentional harm. *Id.* This perspective effectively eliminated the exclusion because, in almost every case, the victim neither expected nor foresaw the injury. The interpretation was criticized for unjustly allowing the insured to shift onto the insurer the punishment he ought to have received from committing an intentional tort. The current policy language was an attempt to make clear that the relevant perspective is the insured’s. *See* Tom Baker, *Liability Insurance at the Tort-Crime Boundary*, in FAULT LINES: TORT LAW AS CULTURAL PRACTICE 66, 68 (David M. Engel & Michael McCann, eds., 2009).

property damage which is either expected or intended from the standpoint of the insured.”⁶⁰ As discussed above, this language is understood to express an “implicit” exclusion that would necessarily be implied by courts even if it were absent.⁶¹ Courts are divided, however, about the exact content of such an exclusion and thus how this language ought to be interpreted.⁶² Generally speaking, there are three interpretations of the “expected or intended” language, with some state courts following each.⁶³

Under the first (minority) view, the test becomes an objective standard: the insured “expects” and “intends” the natural and probable consequences of her actions.⁶⁴ This resembles the classic tort method of

⁶⁰ This “expected or intended” language is found in ISO’s 1986, 1990, 1993, 1996, and 2006 occurrence-based and claims-made Commercial General Liability Coverage Forms. See Donald S. Malecki & Arthur L. Flitner, *COMMERCIAL GENERAL LIABILITY INSURANCE*, appx. B,C,E,F (8th ed. 2005); Fischer, *supra* note 45, at 73–74.

⁶¹ See *supra* note 38 and accompanying text.

⁶² See 7A PLITT ET AL., *supra* note 36, § 103:25 (“Since their beginning, these clauses have raised disputes over their meaning and breadth, a fact well illustrated by the number of commentaries they have elicited.”); Gallagher, *supra* note 34, at 1271–73 (on different standards among states).

⁶³ See 16 HOLMES, *supra* note 38, § 118.2[D]; James L. Rigelhaupt, Jr., Annotation, *Construction and Application of Provision of Liability Insurance Policy Expressly Excluding Injuries Intended or Expected by Insured*, 31 A.L.R. 4th 957 (1984); JERRY, *supra* note 59, § 63C[a] at 480–82; Erik S. Knutsen, *Fortuity Victims and the Compensation Gap: Re-Envisioning Liability Insurance Coverage for Intentional and Criminal Conduct*, 21 CONN. INS. L.J. 209, 219–21 (2014); Catherine A. Salton, Comment, *Mental Incapacity and Liability Insurance Exclusionary Clauses: The Effect of Insanity upon Intent*, 78 CALIF. L. REV. 1027, 1032–33 (1990); Kristin Wilcox, Note, *Intentional Injury Exclusion Clauses—What is Insurance Intent*, 32 WAYNE L. REV. 1523 (1986). See also *Thomas v. Benchmark Ins. Co.*, 179 P.3d 421, 427–28 (Kan. 2008) (noting the existence of three interpretations); *Home Ins. Co. v. Neilsen*, 332 N.E.2d 240, 242 (Ind. Ct. App. 1975) (interpreting older policy language excluding losses “caused intentionally by or at the direction of the Insured” according to same three methods). But see *Tenn. Farmers Mut. Ins. Co. v. Evans*, 814 S.W.2d 49, 54–55 (Tenn. 1991) (making particularly fine-grained distinctions and thereby identifying up to seven different possible ways that courts could interpret the expected/intended language).

⁶⁴ See, e.g., *Allstate Ins. Co. v. Peasley*, 932 P.2d 1244, 1247 (Wash. 1997) (excluding losses from “any bodily injury which may reasonably be expected to

looking to the foreseeable consequences of an act to determine the actor's intent. At the extreme, this understanding of the non-responsibility requirement suggests that an insurer can refuse coverage for any injury or property damage—even if merely the result of an unintentional tort such as negligence—so long as the insured *should have* expected the injury or damage to occur. As one might expect, this results in a substantial narrowing of coverage, and a higher number of pro-insurer results.⁶⁵

Under the second (also minority) view, the test becomes a subjective standard, “virtually erasing the word ‘expected’ from the contract, [and requiring] an intentional act whose *purpose* is to cause an injury of the kind giving rise to the insured's liability.”⁶⁶ This results in broad coverage, since it is difficult to demonstrate such intent and thereby to deny claims.

result from the intentional or criminal acts of an insured person or which are in fact intended by an insured person.”); *Barnet of Ind., Inc. v. Sec. Ins. Grp.*, 425 N.E.2d 201 (Ind. Ct. App. 1981); *Amco Ins. Co. v. Haht*, 490 N.W.2d 843, 845 (Iowa 1992) (noting that, in Iowa, the term “expected . . . denotes that the actor knew or should have known that there was a substantial probability that certain consequences will result from his actions” and that “[i]ntent may be inferred from the nature of the act and the accompanying reasonable foreseeability of harm.” (internal quotations omitted)). See generally *JERRY*, *supra* note 59, § 63C[a] at 481 (“What the ‘expected’ prong adds to the ‘intended’ prong is an exclusion from coverage in circumstances where the insured’s subjective state of mind with respect to desire is not clear, but the circumstances are such that the insured, even if not clearly desiring to cause harm, should surely have anticipated that harm would result.”); *Rigelhaupt*, *supra* note 63, at § 5[d]; RESTATEMENT OF THE L. OF LIAB. INS. § 32 rep. n.e. (AM. L. INST. 2019).

⁶⁵ *JERRY*, *supra* note 59, § 63C[b]. As then-Judge Cardozo put it, “[t]o restrict insurance to cases where liability is incurred without fault of the insured would reduce indemnity to a shadow.” *Messersmith v. Am. Fid. Co.*, 133 N.E. 432, 432 (N.Y. 1921). See also *Johnstown v. Bankers Standard Ins. Co.*, 877 F.2d 1146, 1150 (2d Cir. 1989) (“[T]o exclude all losses or damages which might in some way have been expected by the insured, could expand the field of exclusion until virtually no recovery could be had on insurance.”); *Domtar, Inc. v. Niagara Fire Ins. Co.*, 563 N.W.2d 724, 735 n.6 (Minn. 1997) (rejecting an objective test as “undermin[ing] coverage for injuries caused by simple negligence, a result we sought to avoid in prior cases.”).

⁶⁶ Thomas A. Gordon & Roger Westendorf, *Liability Coverage for Toxic Tort, Hazardous Waste Disposal and Other Pollution Exposures*, 25 IDAHO L. REV. 567, 591 (1988) (citing *A-1 Sandblasting & Steamcleaning Co. v. Baiden*, 632 P.2d 1377 (Or. Ct. App. 1981), *aff’d*, 643 P.2d 1260 (Or. 1982), and *Asbestos Insurance*

The majority of courts takes a third, intermediate, view.⁶⁷ On this reading, an insured “intended” the injury or damage if she subjectively intended both the act and to cause some kind of injury or damage—although not necessarily the same kind that resulted.⁶⁸ Such subjective intent can be actual, as proven by objective evidence. It can also be inferred from the

Coverage Cases, Phase III, Judicial Counsel Coordination Proceeding No. 1072 (Cal. Super. Ct. May 29, 1977)). *See also* Hecla Mining Co. v. N.H. Ins. Co., 811 P.2d 1083, 1088 (Colo. 1991) (“[T]he phrase ‘neither expected nor intended’ should be read only to exclude those damages that the insured knew would flow directly and immediately from its intentional act.”); *Johnstown v. Bankers Standard Ins. Co.*, 877 F.2d 1146, 1150 (2d Cir. 1989); *State Farm Fire & Cas. Co. v. Muth*, 207 N.W.2d 364, 366 (Neb. 1973) (equating the meaning of “expected” with “intended”); Rigelhaupt, *supra* note 63, at § 5[f].

⁶⁷ The Arizona Supreme Court provided a representative statement of this view in *Farmers Ins. Co. v. Vagnozzi*, 675 P.2d 703, 709 (Ariz. 1983) (“The presumption that a person intends the ordinary consequences of his voluntary actions, used in determining responsibility for the consequences of voluntary acts, has no application to the interpretation of terms used in insurance contracts. The intentional acts provision excludes policy coverage if the insured acts with the intent or expectation that bodily injury will result even though the result is different in character from the injury that was intended. Thus, the trier of fact must inquire into the actor’s subjective intent.” (internal citations omitted)). *See e.g.*, *Am. Fam. Mut. Ins. Co. v. Johnson*, 816 P.2d 952 (Colo. 1991); *Amco Ins. Co. v. Haht*, 490 N.W.2d 843 (Iowa 1992); *Thomas v. Benchmark Ins. Co.*, 179 P.3d 421 (Kan. 2008); Rigelhaupt, *supra* note 63, at § 5[a] (citing additional cases).

Note that the *RLLI* appears to take a position somewhere between the minority “subjective intent” view and the majority intermediate view. It defines “intent” according to the insured-friendly subjective standard. RESTATEMENT OF THE L. OF LIAB. INS. § 32 cmt. d (AM. L. INST. 2019) (“[A]n insured intends harm when *such harm* is the object of the insured’s action . . .” (emphasis added)). But it defines “expected” according to the intermediate view. *Id.* (“[A]n insured expects harm when the insured foresees that harm is practically certain to occur as a result of the insured’s intentional act, even if that harm was not the object of the action.”).

⁶⁸ *See, e.g.*, *SL Indus. Inc. v. Am. Motorists Ins. Co.*, 607 A.2d 1266, 1278 (N.J. 1992) (“[If the insured] subjectively intends or expects to cause some sort of injury, that intent will generally preclude coverage.”); *Brooklyn L. Sch. v. Aetna Cas. & Sur. Co.*, 849 F.2d 788, 789 (2d Cir. 1988) (applying New York law) (“Ordinary negligence does not constitute an intention to cause damage; neither does a calculated risk amount to an expectation of damage. To deny coverage, then, the fact finder must find that the insured intended to cause damage.”) (internal citations omitted). *See generally* Rigelhaupt, *supra* note 63, at § 5[c] (citing additional cases).

nature of the act, especially when the insured's conduct shocks the conscience.⁶⁹ These courts generally give the word "expected" an independent meaning that captures fewer cases than the objective, tort-like, interpretation: an injury or damage is "expected" if the insured was subjectively aware that there was a high probability that it would occur as a consequence of the insured's act.⁷⁰ As the Maine Supreme Court stated, an "expected" injury is that which the insured "in fact subjectively foresaw as practically certain"⁷¹—a more stringent standard than reasonable foreseeability.⁷²

⁶⁹ See, e.g., *Foremost Ins. Co. v. Weetman*, 726 F. Supp. 618 (W.D. Pa. 1989); *Mottolo v. Fireman's Fund Ins. Co.*, 830 F. Supp 658 (D. N.H. 1993); *Farm Bureau Ins. Co. v. Witte*, 594 N.W.2d 574 (Neb. 1999); *State Farm Fire & Cas. Co. v. Davis*, 612 So. 2d 458, 463 (Ala. 1993) (citing *Whitt v. De Leu*, 707 F. Supp 1011, 1016 (W.D. Wis. 1989) (inferring intent to injure in case of sexual abuse of children); *Cont'l W. Ins. Co. v. Toal*, 244 N.W.2d 121 (Minn. 1976) (inferring intent to injure in case of armed robbery resulting in shooting death); *Allstate Ins. Co. v. Foster*, 693 F. Supp. 886, 888 (D. Nev. 1988) ("[D]ecisions of other jurisdictions support a conclusion that intent to harm may be inferred from sexual contact with a minor as a matter of law, regardless of the insured's subjective intent."). See generally Rigelhaupt, *supra* note 63, at § 5[b]; ABRAHAM, *supra* note 39, at 538 ("Sometimes . . . subjective intent or expectation can be inferred from the circumstances, perhaps even as a matter of law."); 3 Martha A. Kersey, *Exclusions Under Coverage A of a Standard CGL Policy*, in NEW APPLEMAN ON INSURANCE LAW § 18.03[2][f] (Jeffrey E. Thomas & Francis J. Mootz eds., Library ed., LEXIS, database updated May 2022) ("Many jurisdictions have recognized that the intent to injure, especially when guns or sexual abuse are involved, can be inferred as a matter of law based on the egregious nature of the act involved and the accompanying foreseeability or certainty of harm.").

⁷⁰ See *Shell Oil Co. v. Winterthur Swiss Ins. Co.*, 15 Cal. Rptr. 2d 815, 836 (Cal. Ct. App. 1993) ("The appropriate test for 'expected' damage is whether the insured knew or believed its conduct was substantially certain or highly likely to result in that kind of damage."). Courts have used different phrases to communicate this idea, including "practically certain," *Honeycomb Sys. Inc. v. Admiral Ins. Co.*, 567 F. Supp. 1400, 1404 (D. Me. 1983) (applying Maine law), "substantial probability," *City of Carter Lake v. Aetna Cas. & Sur. Co.*, 604 F.2d 1052, 1058–59 (8th Cir. 1979) (applying Iowa law), and "substantial certainty," *Quincy Mut. Fire Ins. Co. v. Abernathy*, 469 N.E.2d 797, 800 (Mass. 1984); *United Servs. Auto. Ass'n v. Elitzky*, 517 A.2d 982, 989 (Pa. Super. Ct. 1986).

⁷¹ *Patrons-Oxford Mut. Ins. Co. v. Dodge*, 426 A.2d 888, 892 (Me. 1981).

⁷² See KENNETH S. ABRAHAM, ENVIRONMENTAL LIABILITY INSURANCE LAW: AN ANALYSIS OF TOXIC TORT AND HAZARDOUS WASTE INSURANCE COVERAGE

In practice, given the difficulty of proving subjective intent, the choice among these three interpretations often determines which party prevails in disputes over coverage for losses caused by the insured.⁷³ For example, in “prank” cases—where a practical joke goes wrong and causes real injury—the different approaches often lead to diverging determinations of whether the expected/intended exclusion applies.⁷⁴ Such differences have real consequences because the question whether the insured is covered often determines whether the victim receives anything approaching adequate compensation.⁷⁵

This three-way jurisdictional split over the interpretation of the expected/intended language has led courts and commentators to turn to theories of the underlying goals of insurance law to try to determine the purpose of this particular clause. Generally, two such frameworks dominate, both of which suggest that insurance law ought to be interpreted to further instrumental goals.⁷⁶

On the one hand are those inclined to think about the law using economic frameworks. This perspective suggests that the goal of controlling moral hazard provides an adequate normative model for thinking about the types of insurance coverage disputes described above.⁷⁷ Moral hazard—the tendency of insurance coverage to reduce incentives to prevent or minimize

ISSUES 131 (1991) (noting that, on this standard, “the harm in question may be intended but not expected, or expected but not intended, as well as being both expected and intended.”).

⁷³ See *St. Joe Mins. Corp. v. Zurich Ins. Co.*, 89 Cal Rptr. 2d 101, 108 (Cal. Ct. App. 1999) (describing the choice of a subjective or objective standard as a “vital determination” and often dispositive of recovery).

⁷⁴ See, e.g., *Am. Fam. Ins. Co. v. Walser*, 628 N.W.2d 605 (Minn. 2001); *Vt. Mut. Ins. Co. v. Dalzell*, 218 N.W.2d 52 (Mich. Ct. App. 1974).

⁷⁵ See Knutsen, *supra* note 63; Rick Swedloff, *Uncompensated Torts*, 28 GA. ST. U. L. REV. 721 (2012); Gilles, *supra* note 33.

⁷⁶ See, e.g., James A. Fischer, *The Exclusion from Insurance Coverage of Losses Caused by the Intentional Acts of the Insured: A Policy in Search of a Justification*, 30 SANTA CLARA L. REV. 95, 96 (1990) (describing the two “leading public policy justification[s]” for the intentional act exclusion as “deterrence of socially proscribed conduct” and “compensating persons who have been injured by the insured.”).

⁷⁷ See, e.g., Priest *supra* note 17, at 1011, 1034.

loss⁷⁸—has long been expressed as a public policy concern.⁷⁹ Insurance rules that create moral hazard increase the aggregate amount of loss and also shift the cost of such losses onto others. In doing so, such rules inevitably make insurance coverage more expensive, thereby rendering it unavailable to individuals who could afford it at a lower price.⁸⁰ From this perspective, it is in the public's interest to prohibit the enforcement of insurance claims that would create moral hazard.⁸¹ Insurance policy language generally, and the expected/intended language specifically, therefore ought to be interpreted in order to retain the deterrent effect of tort liability.⁸² This perspective suggests that courts ought to interpret the expected/intended language according to something like the minority-rule "objective" standard.

For those inclined to focus on the ability of insurance to protect against loss, on the other hand, it may be argued that everything possible should be done to interpret policy language to create coverage in each individual case.⁸³ When an insured has coverage, it not only increases the

⁷⁸ See George L. Priest, *The Current Insurance Crisis and Modern Tort Law*, 96 Yale L.J. 1521, 1547 (1987) ("Moral hazard refers to the effect of the existence of insurance itself on the level of insurance claims made by the insured. . . . *Ex ante* moral hazard is the reduction in precautions taken by the insured to prevent the loss, because of the existence of insurance."). For the seminal treatment of the long and fascinating history of the concept of moral hazard, see Tom Baker, *On the Genealogy of Moral Hazard*, 75 TEX. L. REV. 237 (1996).

⁷⁹ See, e.g., *Ritter v. Mut. Life Ins. Co.*, 169 U.S. 139, 154 (1898) (discussing the concern that allowing suicide insurance would "encourage[] the assured to commit suicide in order to make provision for those dependent upon him. . . .").

⁸⁰ See Priest, *supra* note 17, at 1019–25.

⁸¹ See *id.* at 1026.

⁸² See Baker, *supra* note 59, at 72 ("Almost all tort liabilities involve harm that potential defendants can avoid to at least some degree, if only by reducing the extent to which they or people they control engage in activity that may cause harm. Indeed, in economic analysis, loss prevention is the primary justification for tort liability. Thus, to the extent that liability provides an incentive to take care, all liability insurance creates at least the potential for moral hazard." (internal citations omitted)).

⁸³ See, e.g., Knutsen, *supra* note 63, at 229 (describing one of the two purposes of liability insurance as "victim compensation"); French, *supra* note 18, at 73; Baker, *supra* note 59, at 75 ("[L]iability insurance protects victims. If any victims deserve that protection, victims of serious crime-torts like arson and rape surely do."); Willy E. Rice, *Insurance Contracts and Judicial Discord over Whether Liability Insurers Must Defend Insureds' Allegedly Intentional and Immoral Conduct: A Historical*

likelihood that his victims will be able to recover against him. It also often determines whether a suit is brought against him at all, and thus, whether his victims get an opportunity to “at the very least announce the wrong and . . . shame the defendant.”⁸⁴ From this perspective, whenever a policy provision appears designed to remove coverage for the insured’s own fault, it should be construed in favor of coverage to the extent that it contains even the slightest ambiguity.⁸⁵ And when no such policy provision is present, an exclusion ought not to be implied. As one insurance law treatise puts it:

To look at only the insured’s behavior ignores the fact that insurance is also for the benefit of the injured victims of accidents. They are the third party beneficiaries of the insurance contracts and their situation should not be ignored. The interpretation of an insured’s conduct is not only a dispute between the insured and the insurance company.⁸⁶

From this perspective, the narrowest possible reading of the expected/intended language—*i.e.*, the minority-rule subjective view—ought to prevail.⁸⁷

The problem, however, is that the majority of courts appear to be thinking about the problem differently than the above two frameworks—and, as a result, they pick the third interpretation of the expected/intended language. Although courts and litigants often discuss moral hazard concerns and victim compensation goals, the determinative consideration frequently appears to be a different one—*i.e.*, whether finding coverage would allow

and Empirical Review of Federal and State Courts’ Declaratory Judgments—1900-1997, 47 AM. U. L. REV. 1131, 1218 (1998); Fischer, *supra* note 76.

⁸⁴ Baker, *supra* note 59, at 74. See also Swedloff, *supra* note 75, at 737; RESTATEMENT OF THE L. OF LIAB. INS. § 45 cmt. g (AM. L. INST. 2019) (“[T]he presence of liability insurance can promote, rather than hinder, the objectives of tort law, by providing compensation for the victim as well as the means to employ the civil-justice system to name, blame, and shame the defendant.”).

⁸⁵ See French, *supra* note 18, at 79–86 (applying the doctrine of *contra proferentem* and reasonable expectations to suggest that the “expected or intended” language in liability insurance policies is ambiguous and should be interpreted in favor of the insured).

⁸⁶ 16 HOLMES, *supra* note 38, at § 118.2[A]. See also Swedloff, *supra* note 75.

⁸⁷ See, e.g., Knutsen, *supra* note 63, at 220–21, 248.

the insured to avoid being held individually responsible for his own wrongdoing. As the Supreme Court of Oregon put it: “[P]unishment rather than deterrence is the real basis upon which coverage should be excluded. A person should suffer the financial consequences flowing from his intentional conduct and should not be reimbursed for his loss, even though he bargains for it in the form of a contract of insurance.”⁸⁸ Although not all courts state the proposition quite so strongly, an overarching concern with individual responsibility appears to motivate the position that most courts take on this question. This concern with individual moral responsibility explains why, for example, intent is often inferred when the underlying act is particularly abhorrent. Such a move is not justified from either a deterrence or victim-compensation perspective, and commentators have noted the divergence between instrumentalist goals and courts’ decisions.⁸⁹ Such an inference makes sense, however, if one understands insurance law to contain within it an implicit commitment to holding individuals responsible for their own bad acts.

C. CONFLICT WITH INSTRUMENTAL GOALS

This Article suggests that the particular conception of individual responsibility at work in the majority-rule interpretation of the expected/intended language is the same conception that animates the non-responsibility requirement generally. As a preliminary step in the process of unpacking this distinctly legal understanding of what cannot be insured, it is helpful to show the ways that a concern with individual responsibility can conflict with attempts to characterize insurance law’s purpose as the pursuit of instrumental goals. Such conflicts can take two forms.

First, there are situations where an instrumentalist calculus suggests that coverage for the insured’s bad acts ought to be allowed, but an

⁸⁸ *Isenhardt v. Gen. Cas. Co.*, 377 P.2d 26, 28 (Or. 1962).

⁸⁹ *See, e.g., Fischer, supra* note 76, at 99 (“The need to reconcile the often competing goals of deterrence and [victim] compensation, both of which clearly underlie the proper application of the intentional act exclusion, are in many instances ignored by courts in favor of an *ad hoc* retributivist approach that is not in keeping with the rules and principles governing insurance contracts.”); James E. Scheuermann, *Fortuity, Intent, and Causation in Liability Insurance Law*, 9 ELON L. REV. 329, 343 (2017).

It is the argument of this Article, that what Fischer calls the “retributivist approach” *is* in keeping with the rules and principles of insurance law. *Contra* Fischer, *supra* note 76, at 99.

individual-responsibility analysis suggests the opposite. For example, it has been argued that insurance for civil liability arising out of criminal acts should be permitted because criminal penalties are a sufficient deterrent to mitigate moral hazard concerns and because there is a particularly strong public interest in compensating the victims of such acts.⁹⁰ Moreover, to the extent that shielding the insured from civil penalties would undermine the deterrent effect of tort liability, such concerns could be alleviated by allowing the insurer to bring a subrogated claim against the insured in order to recoup its costs.⁹¹ On this “pay-and-then-subrogate” model,⁹² the insured would be covered for civil liabilities arising out of his intentional harms so long as the proceeds of the coverage flowed to the victims rather than to the insured. The insurer would then be able to sue the insured to recoup its costs.⁹³

Proposals of this sort have been made by commentators, and early drafts of the *RLLI* suggested that coverage for the insured’s intentional harms is permissible when paired with the type of subrogation regime described above.⁹⁴ The proposal has not caught on, however. Although one state

⁹⁰ See, e.g., French, *supra* note 18, at 94 (“[W]hen examined, the suggestion that the policyholder would be deterred from engaging in criminal conduct if insurance were not available is suspect . . .”); Knutsen, *supra* note 63, at 244; Baker, *supra* note 59, at 72–75.

⁹¹ See Baker, *supra* note 59, at 73 (“Under this alternative approach, the liability insurance contract would provide coverage for the tort, and the liability insurance company would manage the moral hazard by subrogation—*i.e.*, by going after the insured to recoup the money paid to the victim.”). See also Erin E. Meyers & Joni Hersch, *Employment Practices Liability Insurance and Ex Post Moral Hazard*, 106 *CORNELL L. REV.* 947, 979 (2021) (discussing subrogation).

⁹² Baker, *supra* note 59, at 74.

⁹³ To the extent that allowing victims to recover increases the likelihood that they bring a claim, this would increase, rather than diminish, the deterrent effect of tort liability because insurers would be more able to extract damages from the insureds, given the insurers’ status as repeat-players. See Swedloff, *supra* note 75, at 764–66; Baker, *supra* note 59, at 73 (“Under this . . . approach, the liability insurance contract would provide coverage for the tort, and the liability insurance company would manage the moral hazard by subrogation—*i.e.*, by going after the insured to recoup the money paid to the victim.”); Jennifer Wriggins, *Domestic Violence Torts*, 75 *S. CAL. L. REV.* 121, 165 (2001).

⁹⁴ RESTATEMENT OF THE L. OF LIAB. INS. § 47 cmt. j (AM. L. INST., Preliminary Draft No. 3, 2016) (“Subrogation against the insured provides an alternative to a

supreme court followed the “pay-and-then-subrogate” approach,⁹⁵ the decision has since been confined to its facts,⁹⁶ and the *RLLI*'s proposal was withdrawn from the final draft. As Tom Baker, one of the reporters of the *RLLI*, has put it, concerns with individual responsibility and public morality appear to be the reason why this alternative framework has failed to get traction.⁹⁷ The instrumentalist proposal is met with the “object[ion] . . . that *liability insurance protects defendants* and that some defendants—rapists and arsonists for example—do not deserve protection.”⁹⁸ The failure of instrumentalist perspectives to override such individual-responsibility concerns is stark in cases where the victim is vulnerable and the insured's act is heinous—such as when the insured is accused of child molestation.⁹⁹ Moral hazard is usually not a concern in such cases: the insured's act was not plausibly influenced by the availability of coverage, and criminal punishment serves as a deterrent. The felt need to compensate victims of such heinous acts is also particularly strong.¹⁰⁰ Nor is it easy for insurance companies to show that the insured subjectively intended to cause harm: it often appears, horrifyingly, that the insured thought that he was somehow benefitting his victims.¹⁰¹ Courts nonetheless have generally held that liability insurance does not cover the victims' injuries resulting from sexual molestation or exploitation by an insured.¹⁰²

Second, there are situations where an instrumentalist calculus suggests that certain types of coverage ought to be forbidden, even though individual responsibility considerations do not necessarily require that the insured be prevented from getting coverage. Life insurance coverage for suicide¹⁰³ or liability insurance coverage for losses caused by the insured's

public-policy-based prohibition of insurance for certain liabilities.”). *See* Fischer, *supra* note 76, at 112 (discussing subrogation).

⁹⁵ *Ambassador Ins. Co. v. Montes*, 388 A.2d 603 (N.J. 1978).

⁹⁶ *Allstate Ins. Co. v. Malec*, 514 A.2d 832, 838 (N.J. 1986) (“We are content to give *Ambassador* a narrow reading . . .”).

⁹⁷ *See* Baker, *supra* note 59, at 75.

⁹⁸ *Id.*

⁹⁹ *See infra* note 148 and accompanying text.

¹⁰⁰ Baker, *supra* note 59, at 74–75.

¹⁰¹ *See* JERRY, *supra* note 59, § 63C[b] at 488.

¹⁰² *See id.* *See also* *Allstate Ins. Co. v. Mugavero*, 561 N.Y.S.2d 35, 44–47 (N.Y. App. Div. 1990) (Balleta, J., dissenting) (citing cases), *rev'd*, 589 N.E.2d 365 (N.Y. 1992).

¹⁰³ *See infra* Section II.B.2 (describing the history of controversy regarding whether it was against public policy to insure suicide).

own negligence¹⁰⁴ both fall in this category. Allowing such insurance almost certainly creates moral hazard because it necessarily reduces the insureds' incentives to avoid suicide or negligence.¹⁰⁵ If preventing moral hazard is what matters, then these types of insurance ought to be prohibited.¹⁰⁶

Arguments of this sort have also, generally, failed. As will be described in more detail below, the non-responsibility requirement has long been interpreted by courts and legislatures not to prevent insurance coverage for suicide or for the insured's own negligence—even though such insurance undoubtedly creates moral hazard.¹⁰⁷ This is because, as a general matter, our society does not take the position that suicide or negligence are the sorts of things for which we must hold an insured individually responsible. This suggests that such insurance is permitted not because the moral hazard concern is absent but rather because the moral hazard concern is not enough to make such insurance contrary to public policy.¹⁰⁸ If an insurer is willing to underwrite such a policy, then courts will not interpret background principles to render the coverage invalid—even if the net amount of losses

¹⁰⁴ See *infra* Section II.B.1 (describing the history of controversy regarding whether it was against public policy to insure negligence); McNeely, *supra* note 5, at 33 (“When the validity of liability insurance was attacked as contrary to public policy, the most seriously urged contention was that indemnifying the assured against his own negligence would result in a relaxation of vigilance toward the rights of others.”).

¹⁰⁵ See Priest, *supra* note 17, at 1023 (“Where expected injury costs are lower, the underlying level of activity and the underlying injury rate will increase, a phenomenon known as moral hazard.”).

¹⁰⁶ See Gallagher, *supra* note 34, at 1267 (“Although courts recognize moral hazard and often prohibit those forms of insurance that promote wrongdoing, they do not invalidate all insurance it infects.”).

¹⁰⁷ See *infra* Section II.B (describing the changing social views on these topics).

¹⁰⁸ See, e.g., *Kansas City Stock Yards Co. v. A. Reich & Sons, Inc.*, 250 S.W.2d 692, 698 (Mo. 1952) (noting that insurance against negligence, even if it “by having such insurance the insured might become negligent or careless in protecting the property cannot be said to make the contract void as against public policy.”); see also Gallagher, *supra* note 34, at 1267; Fleming James Jr., *Accident Liability Reconsidered: The Impact of Liability Insurance*, 57 *YALE L.J.* 549, 549 (1948) (noting that the moral hazard concern has been “tempered by a strong counter-desire not unduly to discourage enterprising affirmative activity—even when it was dangerous—because people were very much imbued with the idea that unfettered enterprise and activity in nearly all directions worked out through the laws of competition to promote the general good.”).

across society is thereby increased. This suggests, again, that when the moral hazard concern and the insured non-responsibility principle conflict in the legal context, the non-responsibility principle wins.¹⁰⁹ The moral hazard concern appears to be determinative almost exclusively when courts also believe that the insured's loss was caused by his own bad act—such that he ought not to be able to use insurance to avoid his individual responsibility for it.

III. CONCEPTUAL ANALYSIS

This Article argues that the non-responsibility requirement is a core concept of insurance law and that the concept has its own internal logic and normative structure. Other areas of the common law have similar such concepts. The “duty of care” in tort law, “touch and concern” in property law, and “good faith” in contract law are ready examples.¹¹⁰ As Shyamkrishna Balganes and Gideon Parchomovsky have argued, core legal concepts like these “strike[] a balance between stability and change, both of which are essential to the effective operation of a legal system.”¹¹¹ They perform this task by having a stable “intrinsic”¹¹² (or “jural”¹¹³) meaning, while remaining normatively open-ended.¹¹⁴

¹⁰⁹ See *infra* Section IV.C. (discussing interaction between non-responsibility requirement and moral hazard concerns).

¹¹⁰ See Shyamkrishna Balganes & Gideon Parchomovsky, *Structure and Value in the Common Law*, 163 U. PENN. L. REV. 1241, 1243–46 (2015) (listing such concepts and arguing that they are foundational “common law concepts” that serve as “the operational legal devices that the common law uses in doctrine to understand and compartmentalize aspects of a legal issue or dispute.”).

¹¹¹ *Id.* at 1243.

¹¹² Wesley Newcomb Hohfeld, *Some Fundamental Legal Conceptions as Applied in Judicial Reasoning*, 23 YALE L.J. 16, 58 (1913) (quoted in Balganes & Parchomovsky, *supra* note 110, at 1244 n.11).

¹¹³ Balganes & Parchomovsky, *supra* note 110, at 1244.

¹¹⁴ *Id.* at 1255 (“Scholars have previously noted the idea that legal concepts can have two meanings. Some legal theorists refer to it as the distinction between the ‘descriptive’ and ‘prescriptive’ meanings of legal terms, as the distinction between the ‘definitional’ content of legal concepts and their ‘justificatory theory,’ or as the difference between the legal concept as a mere ‘conceptual marker’ and the foundational theory in the service of which it is employed in a particular context.” (citations omitted)). See generally, Jules S. Coleman & Jody S. Kraus, *Rethinking the Theory of Legal Rights*, 95 YALE L.J. 1335 (1986); Timothy P. Terrell,

The normative flexibility of such legal concepts thus enables them to be informed by external interpretive influences, and thereby to accommodate shifts in morality and values over time, while nonetheless remaining legally identifiable and distinct.¹¹⁵ This capacity to be charged with dynamic moral meaning is important because it allows for a persistent connection between law and morality.¹¹⁶ As John Goldberg and Benjamin Zipursky have argued in the context of tort law, legal concepts translate deeply-rooted social norms into frameworks that structure the legal system's assignment of responsibility and liability.¹¹⁷ Thomas Merrill and Henry Smith have made a similar argument in the context of property law: that any sustainable property system must be "infused with moral significance"¹¹⁸ and that our property system embodies a particular moral perspective.¹¹⁹

Insurance law, like other areas of the law, has good reason to track the more general social norms that interact with it—including, in particular, notions of individual responsibility that track a distinction between misbehavior and misfortune. That we demand such a correspondence is evident in the way we talk about insurance generally.¹²⁰ Given that "[t]he very idea of insurance involves a group of individuals or entities in an indirect relationship, without any contract specifying the terms of that

"Property," "Due Process," and the Distinction Between Definition and Theory in Legal Analysis, 70 GEO. L.J. 861 (1981); Peter Westen, *"Freedom" and "Coercion"—Virtue Words and Vice Words*, 1985 DUKE L.J. 541 (1985).

For a particularly clear example of the interface between conceptual stability and dynamic content, see Balganesch & Parchomovsky, *supra* note 110, at 1276 (discussing "reasonable use" in nuisance law).

¹¹⁵ Balganesch & Parchomovsky, *supra* note 110 at 1244.

¹¹⁶ *See id.* at 1305.

¹¹⁷ *See* John C. P. Goldberg & Benjamin C. Zipursky, *Accidents of the Great Society*, 64 MD. L. REV. 364, 391 (2005).

¹¹⁸ Thomas W. Merrill & Henry E. Smith, *The Morality of Property*, 48 WM. & MARY L. REV. 1849, 1850 (2007).

¹¹⁹ *Id.*

¹²⁰ As the Supreme Court of California put it, "The insurers' obligations are . . . rooted in their status as purveyors of a vital service labeled quasi-public in nature. Suppliers of services affected with a public interest must take the public's interest seriously, where necessary placing it before their interest in maximizing gains and limiting disbursements." *Egan v. Mut. of Omaha Ins. Co.*, 620 P.2d 141, 146 (Cal. 1979).

relationship,”¹²¹ it is to be expected that conceptions of justice, particularly distributive justice, will permeate insurance law.¹²² Although the normative open-endedness of legal concepts allows the law to be infused with such public norms, the choice of which norms we infuse the law with is left up to us.

Section A of this Part describes the “jural” meaning of the non-responsibility requirement: its logically-stable but normatively-open-ended conceptual structure. It then describes the distinct normative meaning that infuses that structure in our particular legal tradition. It does so by analogizing the non-responsibility requirement to the concept of proximate causation in tort law, and to the way that the latter concept allows tort law to assign legal responsibility only for certain types of acts—namely, those that were foreseeable results of the tortfeasor’s breach. It argues that the non-responsibility requirement does similar work: it assigns legal responsibility to the insured only for certain types of losses—namely, those that were the results of the insured’s *own bad acts*. In doing so, insurance law relies on independent and inherently-normative conceptions of what it means for an insured’s act to be “bad” and what it means for the act to be attributable to the insured as his “own.” Section A then shows how the non-responsibility requirement’s conception of individual responsibility is reflected in, and reinforced by, the contours of the unique boundary of individual legal responsibility that insurance law draws in practice.

Section B of this Part studies the history of insurance for three particular types of loss—negligence, suicide, and arson—to show how the normative conceptions of wrongness and attributability have changed over time, thereby allowing insurance law to keep in-step with broader social changes.

¹²¹ Kenneth S. Abraham, *Four Conceptions of Insurance*, 161 U. PENN. L. REV. 653, 656 (2013).

¹²² See, e.g., *Allstate Ins. Co. v. Mugavero*, 589 N.E.2d 365, 369–70 (N.Y. 1992) (“We believe . . . that the ordinary person would be startled, to say the least, by the notion that Mugavero should receive insurance protection for sexually molesting these children, and thus, in effect, be permitted to transfer the responsibility for his deeds onto the shoulders of other homeowners in the form of higher premiums. . . . [T]he average person purchasing homeowner’s insurance would cringe at the very suggestion that the person was paying for such coverage. And certainly the person would not want to share that type of risk with other homeowner’s policyholders.” (internal citations and quotation marks omitted)).

A. THE CONCEPTUAL STRUCTURE AND NORMATIVE
CONTENT OF THE NON-RESPONSIBILITY REQUIREMENT

In tort law, the phrase “proximate cause” describes a judgment that a but-for cause of an event should be deemed close enough to it to be treated as legally responsible for it.¹²³ This judgment is based not just on facts (*i.e.*, not all but-for causes are also proximate causes) but on separate normative criteria. In the words of Justice Andrews, “[w]hat we . . . mean by the word ‘proximate’ is that, because of convenience, of public policy, of a rough sense of justice, the law arbitrarily declines to trace a series of events beyond a certain point. This is not logic. It is practical politics.”¹²⁴ Such core legal concepts are, as Justice Andrews notes, normatively open-ended. It is possible, for example, to argue that only efficiency-based considerations ought to determine proximate causation. One might thus argue that the proximate cause of a particular harm ought to be its most cheaply-avoidable but-for cause.¹²⁵ Of course, American tort law generally has not taken this position. It has, instead, focused on the question of *foreseeability*.¹²⁶ Did the tortfeasor’s breach cause the harm in a way that was foreseeable? If so, then the tortfeasor’s breach was a proximate cause.¹²⁷

¹²³ See generally James Angell McLaughlin, *Proximate Cause*, 39 HARV. L. REV. 149 (1925).

¹²⁴ *Palsgraf v. Long Island R.R. Co.*, 162 N.E. 99, 103 (N.Y. 1928) (Andrews, J., dissenting).

¹²⁵ Compare, for example, William Prosser’s proposal to replace existing negligence doctrine with a cost-benefit analysis that compares alternative liability regimes. See John C. P. Goldberg & Benjamin C. Zipursky, *Moral of Macpherson*, 146 U. PA. L. REV. 1733, 1756–62 (1998).

¹²⁶ See W. Jonathan Cardi, *Purging Foreseeability*, 58 VAND. L. REV. 739, 748–49 (2005); Goldberg & Zipursky, *supra* note 125, at 1742 n.38 (citing cases).

¹²⁷ Although foreseeability may also factor into negligence analysis in two places—e.g., duty and breach—I refer only to the role it plays in proximate causation analysis. See Cardi, *supra* note 126, at 743–66 (discussing the role of foreseeability in negligence analysis, in the context of breach, proximate cause, and duty). As Goldberg and Zipursky put it, in order for an act that causes an injury to count as a proximate cause of that injury, “the injury must be the realization of one of the risks that leads the law to deem the conduct careless in the first place.” JOHN C. P. GOLDBERG & BENJAMIN C. ZIPURSKY, *THE OXFORD INTRODUCTIONS TO U.S. LAW: TORTS* 107 (Dennis Patterson ed. 2010).

The non-responsibility requirement in insurance law draws a similar—and similarly “arbitrary”—boundary around a subset of an insured’s but-for effects. The non-responsibility requirement structures a judgment about whether an otherwise-covered loss was caused by acts that are attributable to the insured such that the law ought to hold the insured responsible for the loss by preventing insurance from covering it. This, I suggest, is the immanent structure of the non-responsibility requirement as a legal concept.

Just as it is possible to argue that considerations of pure efficiency ought to determine proximate causation, it is similarly possible to argue that instrumental values like the minimization of moral hazard, or maximization of victim compensation, should provide the normative content for the non-responsibility requirement. As the preceding analysis has suggested, however, our legal system has not chosen to draw the default boundary of responsibility in insurance law along such lines.¹²⁸ Study of the various sources of insurance law reveals that the non-responsibility requirement derives its normative content from two questions:

- (1) Did the insured exercise *substantial control* over the loss-causing act?
- (2) Was the loss-causing act itself *inherently wrong*?

These two questions perform an analogous function to the foreseeability analysis in the law of proximate causation. If both questions are answered in the affirmative, then the non-responsibility requirement demands that the insured ought not to benefit from coverage.

Of course, American insurance law could have turned out differently. It is not strictly necessary that the non-responsibility requirement must turn on the insured’s control or the inherent wrongness of the act. Nonetheless, this Section argues that a faithful interpretation of American insurance law reveals the above-described conceptual structure and normative content. Our legal tradition, in other words, hews to the maxim that an insured cannot be indemnified for the results of his own bad acts. In doing so, it defines an insured’s act to be his “own” if he exercised substantial

¹²⁸ See *supra* Section II.A–B. For exceptions to this default, see *supra* notes 38–43 and accompanying text.

control over it.¹²⁹ And it defines the act to be “bad” if it is inherently wrong, not merely something that is “illegal” or prohibited.¹³⁰ As demonstrated below, unpacking these two prongs of the analysis shows that they trace a boundary of individual legal responsibility that is different from the boundaries traced by tort or criminal law.

1. Substantial Control

It is only when the insured has exercised “substantial” control over the loss-causing act that the non-responsibility requirement suggests coverage should be disallowed.¹³¹

This element of the non-responsibility analysis arises most commonly in situations involving an insured whose acts are the direct cause of the insured loss.¹³² Insurance law generally holds that so long as a named insured was not at fault, it can be covered against losses caused by its agents,

¹²⁹ Cf. KENNETH S. ABRAHAM, *DISTRIBUTING RISK: INSURANCE, LEGAL THEORY, AND PUBLIC POLICY* 90 (1986) (“[T]he notion of control is a normative conclusion about the factors for which individuals can properly be asked to bear insurance responsibility. . . . In common parlance, people are not responsible for their gender, but they are responsible for and can control their smoking and eating habits. In between these extremes lie a variety of actions that are more difficult to characterize.”).

¹³⁰ Cf. McNeely, *supra* note 5, at 33 (“Thus it appears that before cases on liability insurance came before the courts, there was already a general recognition that an insurance contract was not necessarily against public policy because it covered . . . some criminal acts by the insured himself which were viewed as *mala prohibita*, rather than *mala in se*.”).

¹³¹ Professor Edwin Patterson identified this element as an essential feature of insurance, and through his efforts, it was incorporated into the 1939 New York Insurance Law’s definition of “insurance contract.” 16 HOLMES, *supra* note 38, at § 116.2[B] (2000). See N.Y. INS. L. § 1101(a)(2) (“[A] ‘fortuitous event’ is any occurrence or failure to occur which is, or is assumed by the hies to be, to a substantial extent beyond the control of either party.”).

¹³² See generally Willy E. Rice, *Destroyed Community Property, Damaged Persons, and Insurers’ Duty to Indemnify Innocent Spouses and Other Co-Insured Fiduciaries: An Attempt to Harmonize Conflicting Federal and State Courts’ Declaratory Judgments*, 2 EST. PLAN. & CMTY. PROP. L.J. 63 (2009); JERRY, *supra* note 59, at § 63C[b]; Gallagher, *supra* note 34, at 1276.

even if those agents caused harms intentionally,¹³³ and even if their actions incurred punitive damages.¹³⁴ For example, if a company has purchased insurance in its own name and then discovers that one of its employees has committed an intentional tort or intentionally destroyed company property, coverage will generally be allowed so long as the company's senior management did not approve of or participate in the act.¹³⁵ When faced with policy language that would appear to preclude coverage even for the

¹³³ See, e.g., *Perl v. St. Paul Fire & Marine Ins. Co.*, 345 N.W.2d 209, 216 (Minn. 1984) (refusing to enforce a professional liability policy to permit an individual attorney to be indemnified for the attorney's fees that he forfeited for breaching his fiduciary duty to his client but permitting recovery by the attorney's law firm); *Malanga v. Mfrs. Cas. Ins. Co.*, 146 A.2d 105 (N.J. 1958); *Baltzar v. Williams*, 254 So. 2d 470 (La. Ct. App. 1971); *Nuffer v. Ins. Co. of N. Am.*, 45 Cal. Rptr. 918 (Cal. Ct. App. 1965) (holding coverage for intentional burning of an insured's property by his agent is not contrary to public policy and citing other cases); *Morgan v. Greater N.Y. Taxpayers Mut. Ins. Ass'n*, 112 N.E.2d 273 (N.Y. 1953). See generally *Gallagher*, *supra* note 34, at 1277; *Fischer*, *supra* note 45, at 81–84.

¹³⁴ See RESTATEMENT OF THE L. OF LIAB. INS. § 45 cmt. e (AM. L. INST. 2019) (“Courts generally permit insurance coverage of liabilities that are assessed vicariously, even in situations in which the liability of the primary actor would be uninsurable in the jurisdiction, for example liability for punitive damages.”); 7 PLITT ET AL., *supra* note 36, at § 101:23; Michael A. Rosenhouse, Annotation, *Liability Insurance Coverage as Extending to Liability for Punitive or Exemplary Damages*, 16 A.L.R. 4th 11, § 4 (1982); French, *supra* note 18, at 79; Sharkey, *supra* note 47, at 428; *Gallagher*, *supra* note 34, at 1276–78. See also *Dayton Hudson Corp. v. Am. Mut. Liab. Ins. Co.*, 621 P.2d 1155, 1160 (Okla. 1980) (“In almost all jurisdictions which disallow insurance coverage for punitive damages, an exception is recognized for those torts in which liability is vicariously imposed on the employer for a wrong of his servant.”); *Nw. Nat'l Cas. Co. v. McNulty*, 307 F.2d 432, 440 (5th Cir. 1962) (“[I]f the employer did not participate in the wrong the policy of preventing the wrongdoer from escaping penalties for his wrong is inapplicable.”).

¹³⁵ See, e.g., *Ryan Homes, Inc. v. Home Indem. Co.*, 647 A.2d 939, 943 (Pa. Super. Ct. 1994) (denying coverage when the insured's general contractor's subcontractors did shoddy work, potentially saving the general contractor money, because “[t]o hold otherwise . . . would permit a contractor to receive an initial payment from the property owner, allow the project to proceed in a shoddy manner, and then to receive a subsequent payment from an insured company to correct its own mistakes or the mistakes of those it had hired.”); *D.I. Felsenthal Co. v. N. Assurance Co.*, 120 N.E. 268 (Ill. 1918) (holding a corporation is not barred from recovering if its agent acted intentionally to cause loss, but if the agent owns basically all the stock and controls the corporation, then the rule does not apply).

insured's agents' intentional harms, courts will often find a way to interpret the provision to allow coverage.¹³⁶ Insurance law generally takes the position that an insured principal is *not* legally responsible for its agent's acts *unless* it exercised substantial control over the act¹³⁷ or is otherwise morally responsible.¹³⁸ As a Louisiana Court put it, "No person can insure against his own intentional acts. Public policy forbids it. But public policy does not forbid one to insure against the intentional acts of another for which he may be held vicariously liable."¹³⁹

Insurance law thus draws a different boundary around an insured's legal responsibility for its agents' acts than does tort law, which typically

¹³⁶ See KEETON & WIDISS, *supra* note 24, § 5.4(d)(5), at 430 ("In most circumstances, courts hold both (1) that the express provisions commonly used in liability insurance policies do not preclude coverage for damages awarded for an intentional tort when the insured is held to be responsible on a theory of vicarious liability, and (2) that it would not be appropriate to imply a limitation that would restrict the coverage.").

¹³⁷ See *Nw. Nat'l Cas. Co. v. McNulty*, 307 F.2d 432, 440 (5th Cir. 1962) (allowing insurance where "the employer [does] not participate in the wrong"); *Dart Indus. v. Liberty Mut. Ins. Co.*, 484 F.2d 1295, 1298 (9th Cir. 1973); *Pawtucket Mut. Ins. Co. v. Lebrecht*, 190 A.2d 420, 423 (N.H. 1963) ("There is no such policy against insurance to indemnify an insured against the consequences of a violation of law by others without his direction or participation, or against his own negligence, or the negligence of others."); *Farris v. U.S. Fid. & Guar. Co.*, 542 P.2d 1031 (Or. 1975); *Avis Rent A Car Sys., Inc. v. Liberty Mut. Ins. Co.*, 526 A.2d 522 (Conn. 1987); *Capitol Indem. Corp. v. Evolution, Inc.*, 293 F. Supp. 2d 1067, 1073 (D.N.D. 2003) (holding that 68% majority shareholder of a corporation "was [the corporation]" for the sake of intentional act analysis, and denying coverage under the corporation's insurance policy for a fire that the majority shareholder intentionally caused); *Doloughy v. Blanchard Constr. Co.*, 352 A.2d 613 (N.J. Super. Ct. Law Div. 1976); *Com. Union Ins. Co. v. Reichard*, 273 F. Supp. 952 (S.D. Fla. 1967); *Hildebrand v. Holyoke Mut. Fire Ins. Co.*, 386 A.2d 329 (Me. 1978); *Arenson v. Nat'l Auto. & Cas. Ins. Co.*, 286 P.2d 816, 818 (Cal. 1955) (allowing coverage "where the [insured employer] is *not personally at fault*." (emphasis added)). See generally 10A PLITT ET AL., *supra* note 36, at § 149:51.

¹³⁸ See, e.g., *Dayton Hudson Corp.*, 621 P.2d at 1161 (Okla. 1980) ("We think the ultimate answer depends in each [case] on whether prior knowledge makes the master's negligence 'ordinary' or 'gross.'"). See also Gallagher *supra* note 34, at 1281 (discussing judicial analysis in contexts where principal appears to be morally responsible).

¹³⁹ *McBride v. Lyles*, 303 So. 2d 795, 799 (La. Ct. App. 1974). See generally 16 HOLMES, *supra* note 38, § 116.3[D] (discussing cases).

imputes an agent's acts to its principal for the purpose of assigning liability.¹⁴⁰ Although an employer, for example, can defend itself against a *respondeat superior* claim by arguing that its employee acted beyond the scope of employment,¹⁴¹ the employer cannot assert lack of knowledge or approval of the employee's wrongful acts as a defense to vicarious liability.¹⁴² As Patterson put it, "the ordinary principle of the law of agency, that the agent's acts done and knowledge acquired, within the scope of his authority, are imputed to the principal, is inapplicable [in the insurance context] to willfully destructive acts done by the agent without the actual knowledge or connivance of his principal."¹⁴³ Of course, without this mismatch between the conceptions of "vicarious" responsibility contained within tort and insurance law, liability insurance for employers would be of far less value.

2. Inherent Wrongness

For an insured to be deemed responsible for an otherwise-covered loss, she must also have caused it by committing an act that is inherently wrong.

In most circumstances, this determination is made by focusing on the subjective intent of the insured.¹⁴⁴ If she subjectively intended to cause harm or loss, then the otherwise-covered results of her act are held to be uninsurable.¹⁴⁵ In other circumstances, courts appear to skip the intent

¹⁴⁰ See generally RESTATEMENT (SECOND) OF TORTS § 317 cmt. a (AM. L. INST. 1965); RESTATEMENT (SECOND) OF AGENCY § 215 (AM. L. INST. 1958).

¹⁴¹ See, e.g., *Taber v. Maine*, 67 F.3d 1029 (2d Cir. 1995) (Calabresi, J.); JOHN C. P. GOLDBERG ET AL., *TORT LAW: RESPONSIBILITIES AND REDRESS* 502–13 (2d ed. 2008).

¹⁴² See RESTATEMENT (SECOND) OF TORTS § 317 cmt. a (AM. L. INST. 1965);

¹⁴³ EDWIN W. PATTERSON, *ESSENTIALS OF INSURANCE LAW: AN OUTLINE OF LEGAL DOCTRINES IN THEIR RELATIONS TO INSURANCE PRACTICES* 259 (2d ed. 1957).

¹⁴⁴ See, e.g., *Nielsen v. St. Paul Cos.*, 583 P.2d 545, 547 (Or. 1978) ("[T]he insured's intentional, albeit unlawful, acts . . . must have been committed for the purpose of inflicting the injury and harm before either a policy provision excluding intentional harm applies or the public policy against insurability attaches."). See generally Farbstein & Stillman, *supra* note 45.

¹⁴⁵ See generally RESTATEMENT OF THE L. OF LIAB. INS. § 45 cmt. g (AM. L. INST. 2019). Standardized liability insurance policies also seem to make this

analysis in order to cut directly to the underlying question: Was the insured's bad act sufficiently "serious" to be uninsurable?¹⁴⁶ If so, then coverage will be disallowed regardless of what has been shown to be the insured's subjective intent.¹⁴⁷ Thus, where the underlying act is particularly heinous, subjective intent to harm is often said to be "inferred" as a matter of law.¹⁴⁸

distinction. *See* Farbstein & Stillman, *supra* note 45, at 1222–28 (on the history of liability insurance policies, the distinction between intending a harmful act, and intending the harm).

¹⁴⁶ *See, e.g.*, *Ill. Farmers Ins. Co. v. Keyser*, 956 N.E.2d 575, 578–79 (Ill. App. Ct. 2011) ("Whether a particular contract of insurance violates public policy depends on the nature of the risk against which insurance is sought. Applying these public policy principles, Illinois courts have approved personal injury coverage of certain intentional torts such as retaliatory discharge and defamation. On the other hand, they have excluded coverage of intentional torts that are also serious crimes [such as murder, sexual assault, or battery]. The distinction is apparent." (internal citations omitted)). *See also* *City of Muncie v. United Nat'l Ins. Co.*, 564 N.E.2d 979 (Ind. Ct. App. 1991) (holding that a Due Process clause violation is necessarily serious such that an intent to cause harm therefore may be inferred such that coverage is denied under a policy that contains an intentional/expected harm exclusion).

¹⁴⁷ Cases in which courts have allowed coverage for the insured's own "serious" harms generally involve types of insurance that legislatures have heavily regulated on the grounds that victim compensation goals ought to take precedent over general principles of insurance law. *See, e.g.*, *Aetna Life & Cas. Co. v. McCabe*, 556 F. Supp. 1342, 1353 (E.D. Pa. 1983) (applying Pennsylvania law) (holding that physician's intentional malpractice would be covered under insurance policy).

¹⁴⁸ *See, e.g.*, *Dodge v. Legion Ins. Co.*, 102 F. Supp. 2d 144, 153 (S.D.N.Y. 2000) (sexual abuse by psychiatrist of adult patient); *Allstate Ins. Co. v. Bailey*, 723 F. Supp. 665, 669 (M.D. Fla. 1989) (sexual molestation of child); *Allstate Ins. Co. v. Roelfs*, 698 F. Supp. 815, 820–21 (D. Alaska 1987) (sexual molestation of child); *Linebaugh v. Berdish*, 376 N.W.2d 400, 406 (Mich. Ct. App. 1985) (sexual molestation of child); *State Farm Fire & Cas. Co. v. Neises*, 598 N.W.2d 709, 711–12 (Minn. Ct. App. 1999) (grave robbing and corpse mutilation); *Farm Bureau Ins. Co. v. Witte*, 594 N.W.2d 574, 586 (Neb. 1999) (shaking baby, causing shaken baby syndrome); *Sanzi v. Shetty*, 864 A.2d 614, 620 (R.I. 2005) (sexual abuse of child by neurologist). *See generally* Fischer, *supra* note 76, at 132.

In situations where the insured is accused of sexual molestation of a child, for example, it may appear to be the case that the insured subjectively believed that he was actually benefitting, rather than harming, the victim. *See, e.g.*, *N.H. Ins. Grp. V. Strecker*, 798 P.2d 130, 130 (Mont. 1990) (insured testified that he did not intend to harm the victim). Yet in nearly every jurisdiction, intent to commit harm is imputed

The standard that insurance law uses to assign responsibility to insureds appears to track general social understandings of what is inherently wrong, rather than standards that other areas of the law—like tort or criminal law—use to assign legal liability to misbehaving actors. Modern insurance law, for example, allows a tortfeasor to be indemnified against the legal ramifications of harms he negligently causes others.¹⁴⁹ This reveals a mismatch between the ways tort law and insurance law assign responsibility for losses. The tort of negligence is “strict” in the sense that it requires perfect compliance with the objective standard of reasonable prudence.¹⁵⁰ If an insured departs from this standard, he may be held legally responsible by his victims in negligence, regardless of his good intentions.

Note that despite insurance law’s emphasis on intent, insurance for intentional torts is not always denied under the non-responsibility requirement.¹⁵¹ Although some intentional torts are uninsurable, there are many for which liability insurance coverage is frequently allowed. Such torts include defamation, trademark infringement, false imprisonment, employment discrimination, wrongful termination, malicious prosecution, and invasion of privacy.¹⁵² This mismatch is possible because the subjective intent standard is often stricter than that imposed for the sake of many

to the abuser in such cases, thereby precluding insurance coverage. *See generally* State Farm Fire & Cas. Co. v. Davis, 612 So. 2d 458, 463 (Ala. 1993) (“The rule applied by an overwhelming majority of courts is that, in cases involving sexual abuse of children, intent to injure is inferred as a matter of law regardless of claimed intent.” (internal quotations omitted)). *See generally* 17 HOLMES, *supra* note 38 § 119.6[A][1] (state by state survey).

¹⁴⁹ *See, e.g.*, Hartford Life Ins. Co. v. Title Guar. Co., 520 F.2d 1170 (D.C. Cir. 1975). This was not always the case, see *infra* Section II.B.1.

¹⁵⁰ *See* Kenneth S. Abraham, *Strict Liability in Negligence*, 61 DEPAUL L. REV. 271, 288–92 (2012) (examining strict liability in negligence).

¹⁵¹ *See* BAKER & LOGUE, *supra* note 21, at 416 (“[C]riminal, tort, and insurance law. . . . [a]ll use words like ‘intent’ and ‘intentional’ to draw doctrinal lines. . . . Recognizing the unique usage of the word ‘intent’ in each legal context is helpful in understanding both the intentional harm and criminal act exclusions.”).

¹⁵² *See generally* RESTATEMENT OF THE L. OF LIAB. INS. § 45 cmt. h (AM. L. INST. 2019) (listing cases); French, *supra* note 18, at 67–70 (listing cases); Gallagher, *supra* note 35, at 1273–74 (listing cases); 7 PLITT ET AL., *supra* note 36, at § 101:24 (listing cases).

intentional torts and because courts sometimes deem the relevant intentional tort to be insufficiently serious to warrant barring coverage.¹⁵³

Because insurance law appears to be concerned with the moral wrongness of the insured's act, one might expect there to be a correspondence between a determination that the insured's act was a crime and a determination that the non-responsibility requirement precludes insurance coverage for losses or liabilities arising out of the same act. But this is not the case either.¹⁵⁴ Instead, insurance law generally allows coverage for civil liability or property losses arising out of the insured's violation of criminal statutes so long as the crime was merely a *malum prohibitum*, rather than a *malum in se*.¹⁵⁵ Here too, this distinction is generally—although not

¹⁵³ See, e.g., *Fermino v. Fedco, Inc.*, 872 P.2d 559, 567 (Cal. 1994) (“The only mental state required to be shown to prove false imprisonment is the intent to confine, or to create a similar intrusion. Thus, the intent element of false imprisonment does not entail an intent or motive to cause harm; indeed false imprisonments often appear to arise from initially legitimate motives.” (internal citations omitted)); *City of Newark v. Hartford Accident & Indem. Co.*, 342 A.2d 513 (N.J. Super. Ct. App. Div. 1975) (determining that insurance policies providing indemnity to police officers against civil consequences of their own willful or intentional acts are not contrary to public policy so long as the police officers are acting within the scope of their employment).

¹⁵⁴ The standard for determining intent for the purpose of insurance coverage is distinct from rules governing intent for purposes of criminal responsibility. Evidence presented during a criminal proceeding can be used, however, to show intent in a subsequent civil action regarding insurance coverage. See, e.g., *Merritt v. State Farm Fire & Cas. Co.*, 463 S.E.2d 42 (Ga. Ct. App. 1995). A criminal conviction of an intent crime may be treated as *prima facie* evidence of intent for purposes of insurance coverage. See, e.g., *Shelter Mut. Ins. Co. v. Bailey*, 513 N.E.2d 490 (Ill. App. Ct. 1987). See generally Thomas D. Sawaya, *Use of Criminal Convictions in Subsequent Civil Proceedings: Statutory Collateral Estoppel Under Florida and Federal Law and the Intentional Act Exclusion Clause*, 40 U. FLA. L. REV. 479, 522 (1988); James L. Rigelhaupt, Jr., Annotation, *Criminal Conviction as Rendering Conduct for Which Insured Convicted Within Provision of Liability Insurance Policy Expressly Excluding Coverage for Damage or Injury Intended or Expected by Insured*, 35 A.L.R. 4th 1063 (1985); 7 PLITT ET AL., *supra* note 36, at § 101:25; 7A PLITT ET AL., *supra* note 36, at § 103:35.

¹⁵⁵ As the Supreme Court of Massachusetts put it, “If the maxim, that no man shall profit from his own wrong, be applied literally, then the slightest negligence . . . would bar recovery. Such a result would be recognized generally as impractical and unjust.” *Minasian v. Aetna Life Ins. Co.*, 3 N.E.2d 17, 18–19 (Mass. 1936).

always—made on the basis of whether the insured subjectively intended to cause loss or harm.¹⁵⁶ Thus, when an insured has been convicted of a crime, courts may review the relevant criminal statute to determine whether the conviction establishes the *type* of intent necessary to prevent insurance coverage.¹⁵⁷ Even when insurance policies contain explicit exclusions for liabilities arising out of intentional acts, courts have often read such clauses only to prevent coverage when the underlying crime is a “serious” one.¹⁵⁸

There is also no clear correspondence between acts that incur punitive damages and a determination that liability arising out of such acts is uninsurable. A majority of the states have held that liability for punitive

¹⁵⁶ See RESTATEMENT OF THE L. OF LIAB. INS. § 45 cmt. d (AM. L. INST. 2019); *Coop. Fire Ins. Co. v. Vondrak*, 346 N.Y.S.2d 965 (N.Y. Sup. Ct. 1973) (intentional violation of the law may be insured against where the ultimate damage to the injured person was unintentional).

¹⁵⁷ Such a finding is not always possible, especially when the underlying crime is either a “strict liability” or “general intent” crime. See, e.g., *Nationwide Mut. Ins. Co. v. Machniak*, 600 N.E.2d 266, 268 (Ohio Ct. App. 1991) (holding that intentional-injury exclusion did not apply to insured’s conviction for felonious assault because the crime was not statutorily defined as a specific-intent crime); *United States Fid. & Guar. Co. v. Perez*, 384 So. 2d 904 (Fla. Dist. Ct. App. 1980); *USX Corp. v. Adriatic Ins. Co.*, 99 F. Supp. 2d 593 (W.D. Pa. 2000), *aff’d*, 345 F.3d 190 (3d Cir. 2003).

¹⁵⁸ See, e.g., *Allstate Ins. Co. v. Raynor*, 21 P.3d 707, 712 (Wash. 2001) (holding that a criminal acts exclusion found in a homeowner’s liability insurance policy did not apply to all criminal conduct, but only to “serious” criminal conduct accompanied by “a wrongful disposition” to harm or injure others); *Van Riper v. Const. Gov’t League*, 96 P.2d 588 (Wash. 1939); *Sledge v. Cont’l Cas. Co.*, 639 So. 2d 805, 813 (La. Ct. App. 1994) (citing *Van Riper* for the rule that “violation of law’ exclusion in life insurance policy applied only to criminal acts of a serious nature.”). Courts sometimes do read criminal act exclusions literally, however, as not turning on the seriousness of the crime or the intent of the criminal. See, e.g., *Wilderman v. Powers*, 956 A.2d 613 (Conn. App. Ct. 2008) (denying coverage for liability for neighbor’s alleged psychological injuries when insured peeping tom photographed naked neighbor and was sued because his conduct was criminal in nature); *SECURA Supreme Ins. Co. v. M.S.M.*, 755 N.W.2d 320 (Minn. Ct. App. 2008) (holding that youth’s attack of neighbor was a “criminal act,” regardless of intent of youth to harm neighbor); *Gruninger v. Nationwide Mut. Ins. Co.*, 905 N.Y.S.2d 391 (N.Y. App. Div. 2010) (denying coverage when insured accidentally shot other hunter); *Progressive N. Ins. Co. v. McDonough*, 608 F.3d 388 (8th Cir. 2010) (interpreting plain language of criminal act exclusion as having no intent requirement such that insured’s intent was irrelevant at time of accident). See generally Knutsen, *supra* note 63, at 238 (discussing such cases).

damages is insurable.¹⁵⁹ States following this majority rule generally forbid insurance for punitive damages arising out of intentional conduct, however.¹⁶⁰ Here again, the relevant standard of “intent” is subjective intent by the insured to cause harm, rather than an intent to perform the act.¹⁶¹

As one might expect, given the general prevalence of the subjective-intent standard, most courts have accepted the view that if an insured suffered from a lack of mental capacity when causing the relevant harm or loss, his coverage ought not to be voided—either under policy language that explicitly carves-out “intentional” acts or under general principles of insurance law.¹⁶² “Broadly stated, if the actor does not have the mental capacity to do the act intentionally, the policy coverage remains operative.”¹⁶³ Such an allowance for mental incapacity makes sense insofar as the non-responsibility requirement in insurance law aims to make a determination akin to the types of moral-culpability determinations in criminal law, which similarly allows for an insanity defense.¹⁶⁴ Interestingly, as Robert Jerry has noted, “Most courts reject the view that the criminal standard for determining insanity is the appropriate test for determining lack

¹⁵⁹ RESTATEMENT OF THE L. OF LIAB. INS. § 45 cmt. i (AM. L. INST. 2019).

¹⁶⁰ Sharkey, *supra* note 47, at 432.

¹⁶¹ *See id.* at 452.

¹⁶² *See, e.g.,* Globe Am. Cas. Co. v. Lyons, 641 P.2d 251 (Ariz. Ct. App. 1981). *See generally* JERRY, *supra* note 59, at § 63B[a] (discussing insanity in the context of insurance for intentional harm); Farbstein & Stillman, *supra* note 45, at 1225–28; James. L. Rigelhaupt, Jr., Annotation, *Liability Insurance: Intoxication or Other Mental Incapacity Avoiding Application of Clause In Liability Policy Specifically Exempting Coverage of Injury or Damage Caused Intentionally by or at Direction of Insured*, 33 A.L.R. 4th 983 § 3[a] (1984); KEETON & WIDISS, *supra* note 24, at 481; VANCE, *supra* note 38, at 462 n.136 (3d ed. 1951) (discussing Karow v. Cont'l Ins. Co., 15 N.W. 27, 32 (Wis. 1883) where the court found that self-arson was covered if the insured is insane).

¹⁶³ *Ruvolo v. Am. Cas. Co.*, 189 A.2d 204, 208 (N.J. 1963).

¹⁶⁴ *See* Salton, *supra* note 63, at 1037–44 (reviewing criminal law treatment of insanity). Note that this allowance for mental incapacity again differentiates insurance law's conception of responsibility from that articulated by tort law, where no insanity defense is available to tortfeasors. *See* James Goudkamp, *Insanity as a Tort Defence*, 31 OXFORD J. LEG. STUD. 727 (2011); Patrick Kelley, *Infancy, Insanity, and Infirmary in the Law of Torts*, 48 AM. J. JURIS. 179 (2003); Farbstein & Stillman, *supra* note 45, at 1226; *Rajspic v. Nationwide Mut. Ins. Co.*, 662 P.2d 534 (Idaho 1983).

of mental capacity [for the sake of insurance coverage].”¹⁶⁵ Of course, there are situations where an insured is deemed to lack mental capacity under both the criminal and the insurance law standards.¹⁶⁶ The point, however, is that there is no clean correspondence between the insurance law and criminal law conceptions of insanity either.¹⁶⁷

B. THE NON-RESPONSIBILITY REQUIREMENT OVER TIME

Because the non-responsibility requirement is structured such that it derives its legal content from inherently normative social conceptions of control and wrongness, a full presentation of it also requires a demonstration of the connection between the requirement and evolving social norms. This Section does so by showing how historical changes in public morality have corresponded to changing determinations of whether coverage for certain types of acts ought to be disallowed.¹⁶⁸ As Emile Durkheim put it, “Moral reality, like all reality, can be studied from two different points of view. One can set out to explore and understand it and one can set out to evaluate it. The first of these problems, which is theoretical, must necessarily precede the second”¹⁶⁹ The relevant moral phenomena to be described in this

¹⁶⁵ JERRY, *supra* note 59, at § 63C[d]. *See also* Fischer, *supra* note 76, at 140–45; Farbstain & Stillman, *supra* note 45, at 1226–28. It is possible for an insane person’s acts to be intentional for the purpose of insurance law but unintentional for the purposes of criminal law: an insane insured may be unable to get insurance coverage for his intentional acts even though he was able to avoid criminal punishment through a successful insanity defense. *See, e.g.*, Johnson v. Ins. Co. of N. Am., 350 S.E.2d 616 (Va. 1986); Transamerica Ins. Corp. of Am. v. Boughton, 440 N.W.2d 922 (Mich. Ct. App. 1989). It is also possible, contrarily, for an insane person’s acts to be unintentional for the purpose of insurance law but intentional for the purposes of criminal law: an insane person’s acts may be deemed unintentional, and thus insurable, even when the insanity defense to related criminal charges fails.

¹⁶⁶ *Boughton*, 440 N.W.2d at 925 (“We recognize that there will be cases where insanity manifests itself such that the insured cannot intend or expect to cause an injury; an actor may believe, for example, that he is peeling a banana rather than pointing a pistol.”); *Ruvolo*, 189 A.2d at 208–09.

¹⁶⁷ For a subtle treatment of the different ways that insurance law treats insanity, see Salton, *supra* note 63.

¹⁶⁸ This is what Balganesch and Parchomovsky call a process of “interpretive change.” Balganesch & Parchomovsky, *supra* note 110, at 1276.

¹⁶⁹ EMILE DURKHEIM, *SOCIOLOGY AND PHILOSOPHY* 35 (D. F. Pocock trans., 1953). *See also* Joshua Kleinfeld, *A Theory of Criminal Victimization*, 65 STAN. L.

Section correspond to the two elements of the non-responsibility requirement described in the preceding Section: what qualifies as an inherently wrong act, and what constitutes morally-relevant control over that act by the insured.

1. Insuring Negligence

Up until the 1830s, courts and treatise-writers did not distinguish between losses that were intentionally caused by the insured and those that resulted from the insured's lack of care. Courts thus held that losses caused by negligence of the insured were uninsurable.¹⁷⁰ Willard Philipps, in his *Treatise on the Law of Insurance* (1823) wrote:

[A]n agreement by one party to indemnify another against losses voluntarily incurred, seems to be so obviously opposed to the general interest of a community, that it could hardly be enforced by any legal tribunal. And there is the same objection, in a smaller degree, against sustaining a contract to indemnify a man against the consequences of his own negligence. By such an agreement one man would consent to put himself wholly in the power of another, and it could operate only to the injury of the parties, and of the community of which they were members.¹⁷¹

In 1828, Chancellor Kent stated in his *Commentaries on America Law* that it is “the better opinion” that “the insurer is not liable for . . . damage . . . [which] may be prevented by due care, and is within the control of human prudence and sagacity.”¹⁷²

REV. 1087, 1092 (2013) (making the same point in the criminal law context and quoting Durkheim); RICHARD A. POSNER, *THE PROBLEMATICS OF MORAL AND LEGAL THEORY* 5 (3d prt. 2002) (stating that one may “stud[y] morality as a phenomenon . . . rather than in preaching.”).

¹⁷⁰ See HORWITZ, *supra* note 39, at 202; Sharkey, *supra* note 47, at 420; 10A PLITT ET AL., *supra* note 36, at § 149:45.

¹⁷¹ 1 WILLARD PHILLIPS, *A TREATISE ON THE LAW OF INSURANCE* 158 (1823).

¹⁷² 3 JAMES KENT, *COMMENTARIES ON AMERICAN LAW* 334 (William M. Lacy ed., 1889).

As Kenneth Abraham has shown, the doctrinal vehicle through which this proposition was tested was the “barratry” defense¹⁷³—barratry being injury brought about through the design of the insured’s own shipmaster or crew.¹⁷⁴ As the Supreme Court of New York held in *Grim v. Phoenix*, which Kent discussed,¹⁷⁵ when an insurance policy explicitly covered barratry, the malevolent behavior of the shipmaster or crew would be covered on the grounds that even due care of the insured ship-owner could not have prevented such loss.¹⁷⁶ But if the loss resulted from negligence or other misconduct of the master or mariners that did not amount to barratry, then such loss was not covered, because the “act of the master must be referred to his principal, who appoints him; and, whenever a loss happens through the master’s fault, unless that fault amounts to barratry, the owner, and not the insurer, must bear it.”¹⁷⁷ Thus although insurers and courts, when delineating the coverage for barratry, made a distinction between the intentional and negligent conduct of the insured’s *agents*, they declined to make a similar distinction with regard to the insured’s own actions in selecting and managing his shipmaster and crew. From this perspective, the non-responsibility requirement precluded coverage for losses caused by negligence of agents both because the insured exercised sufficient control over them to be responsible for their actions, and also because responsibility

¹⁷³ Kenneth S. Abraham, *Liability Insurance and Accident Prevention: The Evolution of an Idea*, 64 MD. L. REV. 573, 576 (2005). See also HORWITZ, *supra* note 39, at 229–30 (“[The] defense of barratry was just another application of a more general principle that one could not insure against his own misfeasance.”).

¹⁷⁴ HORWITZ, *supra* note 39, at 335 n.198; *Grim v. Phoenix Ins. Co.*, 13 Johns. 451, 457 (N.Y. Sup. Ct. 1816) (“It is well settled that an act to be barratrous must be done with a fraudulent intent or *ex maleficio*. Barratry is a fraudulent breach of duty in respect to the owners.”).

¹⁷⁵ KENT, *supra* note 172, at 494.

¹⁷⁶ *Grim*, 13 Johns. at 457–58.

¹⁷⁷ *Id.* at 459. See also *Cleveland v. Union Ins. Co.*, 8 Mass (1 Tyng) 308, 321–22 (Mass. 1811) (“It is the duty of the owner [of the vessel] to see that he intrusts the property insured with a man of competent skill, prudence, and discretion. He is responsible for all losses or damage to the goods committed to his charge, which arise from his negligence, ignorance, or willful misconduct The principle of an implied warranty on the part of the assured, that every thing shall be done to prevent a loss, pervades the whole subject of marine insurance”). HORWITZ, *supra* note 39, at 202 (noting that before 1830, parties were not insured for losses arising out of their own negligence).

for losses caused by the insured's own "voluntary" acts (whether negligent or intentional) ought to lie with the insured and not on the insurer.¹⁷⁸

Over the ensuing decades, however, judicial and scholarly opinions changed such that marine insurers increasingly found that the defense of barratry failed when they sought to avoid coverage by showing that mere negligence had caused the loss.¹⁷⁹ Fire insurers' attempts to use the policyholder's own negligence as a defense similarly failed.¹⁸⁰ Historians have attributed this shift to different causes. Horwitz, for example, attributes the increased acceptance of insurance for losses caused by negligence to a rise of an actuarial consciousness during the mid-nineteenth century.¹⁸¹ "The courts, in short, were beginning to express what would become a more general change in nineteenth century legal consciousness: conceiving of greater numbers of business risks simply as 'costs of doing business,' largely outside the control of individual responsibility."¹⁸² The result was that losses caused by negligence gradually became paradigmatically insurable on the belief that humans are inherently and uncontrollably prone to carelessness. Although harms proximately caused by the insured's own negligence may give rise to legal claims against him, such negligence was not the sort of

¹⁷⁸ See *Grim*, 13 Johns. at 458–60. It was also a subject of controversy whether negligence was a covered cause of loss in the context of fire insurance on land. See KENT, *supra* note 172, at 496 ("[I]t is a vexed question, rendered the more perplexing by well balanced decisions, and in direct opposition to each other, whether a loss by fire proceeding from negligence, be covered by a policy insuring against fire.").

¹⁷⁹ See, e.g., *Patapsco Ins. Co. v. Coulter*, 28 U.S. 222, 236 (1830) (finding insurance coverage for barratry because negligence that was a remote cause will not be a defense to coverage, contrary to *Grim*); *Waters v. Merchs.' Louisville Ins. Co.*, 36 U.S. 213, 225 (1837) (holding that losses occasioned by insured perils (e.g., fire) are insured against even when caused by negligence). See generally Abraham, *supra* note 173, at 577; HORWITZ, *supra* note 39, at 202.

¹⁸⁰ See, e.g., *Columbia Ins. Co. v. Lawrence*, 35 U.S. 507, 517–18 (1836). See HORWITZ, *supra* note 39, at 230–31.

¹⁸¹ HORWITZ, *supra* note 39, at 226–37.

¹⁸² *Id.* at 230. See generally JONATHAN LEVY, *FREAKS OF FORTUNE: THE EMERGING WORLD OF CAPITALISM AND RISK IN AMERICA* (2012); JOHN FABIAN WITT, *THE ACCIDENTAL REPUBLIC: CRIPPLED WORKINGMEN, DESTITUTE WIDOWS, AND THE REMAKING OF AMERICAN LAW* (2004) (discussing the field of accident law and how it began to change in the nineteenth century to be more consistent with social theories).

inherently bad act that ought not to be insured.¹⁸³ This shift laid the legal groundwork for the rise of a new type of insurance: liability insurance.¹⁸⁴

The first form of liability insurance arose in the 1880s as “employers’ liability insurance,” designed to protect employers against liability to their employees during the period before workers’ compensation was enacted.¹⁸⁵ Soon thereafter, a “public liability” feature was added to such policies—extending coverage to third parties generally.¹⁸⁶ These policies eventually evolved into general commercial liability insurance.¹⁸⁷ The liability insurance that is sold today as part of residential insurance packages (“homeowners insurance”) provides the same kind of broad protection and uses much of the same policy language as commercial liability insurance.¹⁸⁸

When liability insurance first appeared, it was “considered of doubtful legality because it . . . requires the insurer *to interfere* in litigation to which he is not a party.”¹⁸⁹ This concern—that the insurer might shield the wrongdoer from being held directly responsible by his victims—was not present in the first-party insurance context. It did not take long for courts to come to the general conclusion, however, that insofar as civil liability takes the form of “a money compensation . . . though the life or limb of a person

¹⁸³ See, e.g., *Fed. Ins. Co. v. Tamiami Trail Tours Inc.*, 117 F.2d 794, 796 (5th Cir. 1941) (“An overwhelming percentage of all insurable losses sustained because of fire can be directly traced to some act or acts of negligence. Were it not for the errant human element, the hazards insured against would be greatly diminished. It is in full appreciation of these conditions that the property owner seeks insurance, and it is after painstaking analysis of them that the insurer fixes his premiums and issues the policies. It is in recognition of this practice that the law requires the insurer to assume the risk of the negligence of the insured and permits recovery by an insured whose negligence proximately caused the loss.”).

¹⁸⁴ See Abraham, *supra* note 173, at 580–82; McNeely, *supra* note 39; McNeely, *supra* note 5, at 27–29.

¹⁸⁵ See Abraham, *supra* note 173, at 580; McNeely, *supra* note 39, at 188.

¹⁸⁶ See Abraham, *supra* note 173, at 580.

¹⁸⁷ *Id.* See also McNeely, *supra* note 39, at 193.

¹⁸⁸ From the beginning, both homeowners and commercial liability insurance have been based on standard policy forms drafted by insurance trade associations. See Tom Baker, *Reconsidering Insurance for Punitive Damages*, 1998 WIS. L. REV. 101, 114 n.47 (1998). Commercial liability insurance policies, as well as homeowners’ policies, tend to include a promise to pay “those sums the insured becomes legally obligated to pay as damages because of bodily injury, personal injury, or property damage.” *Id.* at 115.

¹⁸⁹ PATTERSON, *supra* note 143, at 263 (emphasis added). See also McNeely, *supra* note 39 (discussing history of liability insurance).

may be, and most certainly is, of greater intrinsic value than goods and chattels,”¹⁹⁰ there is: “no valid reason for holding that the law . . . [has not] reached a stage of allowing an [insured] . . . to purchase from a third party an indemnity fund with which to make more certain his ability to respond in damages for personal injuries caused by his carelessness and neglect.”¹⁹¹ Although there was some early controversy over whether it was contrary to the public’s interest to allow insurance to cover liability for negligence generally, judicial and social consensus arrived fairly quickly at the determination that such coverage was permissible.¹⁹² The question whether it was wrong in the moral sense to permit insurance for losses due to negligence—*i.e.*, because it would allow the insured to avoid responsibility for his own wrongs—had already been answered in the negative in the property insurance context.¹⁹³

Thus, by the early twentieth century, insurance for negligence—whether in the first-party insurance context or the third-party insurance context—became fully permissible under the non-responsibility requirement. The insured was not deemed to be fully in control of “the errant human element”¹⁹⁴ that produced negligence nor was negligently caused loss regarded as the sort of inherently bad act that could not be diffused through

¹⁹⁰ *Bos. & A.R. Co. v. Mercantile Tr. & Deposit Co.*, 34 A. 778, 786 (Md. 1896).

¹⁹¹ *Id.* at 786–87.

¹⁹² *See, e.g.*, *Messersmith v. Am. Fid. Co.*, 133 N.E. 432 (N.Y. 1921) (finding auto liability coverage for an accident that was directly caused by improper and negligent conduct, in accordance with public policy); *Bos. & A.R. Co.*, 34 A. at 786 (“While the carrier will not be permitted by contract or otherwise to exempt himself from liability for losses caused by his own negligence or the negligence of his servants, there is no reason of public policy which prohibits him from contracting with a third person for insurance against these very same losses.”). *See generally* McNeely, *supra* note 5, at 33.

¹⁹³ By the early twentieth century, courts also began to cite empirical data to argue that the number of accidents due to negligence has not increased with the growth of liability insurance. McNeely, *supra* note 5, at 34 (citing *Merchs.’ Mut. Auto. Liab. Ins. Co. v. Smart*, 267 U.S. 126 (1925); *In re Op. of the Justs.*, 147 N.E. 681 (Mass. 1925)).

¹⁹⁴ *Fed. Ins. Co. v. Tamiami Trail Tours*, 117 F.2d 794, 796 (5th Cir. 1941).

insurance. Today, it remains “settled law” that a person may be insured against the results of his own negligence¹⁹⁵

2. Insuring Suicide

For most of the nineteenth century, a majority of courts in the United States followed the “English rule”¹⁹⁶ that it was contrary to the public interest for a beneficiary to recover under a life insurance policy where the insured, while sane, committed suicide.¹⁹⁷ This arose out of a tradition, carried over into Colonial American law, that suicide was a morally reprehensible act for which the insured ought not to be allowed to recover.¹⁹⁸ This attitude was reflected in the insurance law principle—imported from the marine and fire

¹⁹⁵ *Hartford Life Ins. Co. v. Title Guarantee Co.*, 520 F.2d 1170, 1175 (D.C. Cir. 1975). *Accord* *Nw. Nat’l Cas. Co. v. McNulty*, 307 F.2d 432, 442 (5th Cir. 1962); *St. Paul Mercury Ins. Co. v. Duke Univ.*, 670 F. Supp. 630, 637 (M.D.N.C. 1987), *aff’d in part, rev’d in part*, 849 F.2d 133 (4th Cir. 1988); *Cent. Dauphin Sch. Dist. v. Am. Cas. Co.*, 412 A.2d 892, 896 (Pa. Super. Ct. 1979), *rev’d*, 426 A.2d 94 (Pa. 1981); *Gordon H. Ball, Inc. v. Or. Erecting Co.*, 539 P.2d 1059, 1061 (Or. 1975).

¹⁹⁶ *JERRY*, *supra* note 59, at § 63B[a]. The English rule appears to originate in the criminalization of suicide. “Although suicide is no longer a criminal offense [in England] if the insured kills himself whilst not mentally disordered, the insurer can avoid liability on the ground that he cannot take advantage of his own intentional act.” *Id.* at 466 n.219 (quoting 25 HALSBURY’S LAWS OF ENGLAND § 530 at 302 (4th ed. reissue 1994)).

¹⁹⁷ *See, e.g.*, *Supreme Commandery of Knights of the Golden Rule v. Ainsworth*, 71 Ala. 436 (Ala. 1882); *Ritter v. Mut. Life Ins. Co.*, 169 U.S. 139, 154 (1898) (arguing on public policy grounds that the contrary rule would “tempt[] or encourage[] the assured to commit suicide in order to make provision for those dependent upon him, or to whom he was indebted.”). *See generally* PATTERSON, *supra* note 143, at 261 (noting that suicide by an insured, mentally sane or insane, is “not impliedly excepted from the insurer’s risks, by the weight of authority in the United States.”). When insurance was taken out in contemplation of committing suicide, the insurer could avoid the policy on the grounds of fraud even if the policy did not discuss suicide. 9A PLITT ET AL., *supra* note 36, at § 138:23; VANCE, *supra* note 38, at 518. *See, e.g.*, *Lange v. Royal Highlanders*, 110 N.W. 1110, 1112 (Neb. 1907).

¹⁹⁸ *See* Alex B. Long, *Abolishing the Suicide Rule*, 113 NW. U. L. REV. 767, 777–79 (2019).

insurance context—that an insured could not recover if his own bad act caused the otherwise-covered loss.¹⁹⁹

In 1898, the Supreme Court decided *Ritter v. Mutual Life Insurance Company of New York*,²⁰⁰ and it appeared to set a national standard that it was contrary to public interest for a life insurance policy to pay if the insured committed suicide while sane.²⁰¹ In *Ritter*, the insured was of sound mind and killed himself apparently with the intention of maturing his life insurance policies in order to repay his debts.²⁰² The Court held that his life insurer was relieved of liability, and that there was no error in the trial court's instruction to the jury that "[t]here can be no recovery by the estate of a dead man of the amount of policies of insurance upon his life, if he takes his life designedly, while of sound mind."²⁰³ In upholding this broad statement of law, the Supreme Court gave two reasons: (1) where, as in that case, there was no express exception of sane suicide, such an exception was to be implied; and (2) an express provision for payment in the case of suicide while sane would be contrary to public policy.²⁰⁴ The Court stated, "[a] contract, the tendency of which is to endanger the public interests or injuriously affect the public good, or which is subversive of sound morality, ought never to receive the sanction of court of justice, or be made the foundation of its judgment."²⁰⁵ In making its "sound morality" argument, the Court relied upon precedents set in jurisdictions where suicide was a crime.²⁰⁶ Even though suicide by that

¹⁹⁹ See *Ritter*, 169 U.S. at 160 ("[I]f a man insures his life for a year, and commits suicide within the year, his executors cannot recover on the policy, as the owner of a ship who insures her for a year cannot recover upon the policy if within the year he causes her to be sunk: a stipulation that, in either case, upon such an event the policy should give a right of action, would be void.") (quoting *Moore v. Woolsey*, (1854) 4 El & B. 243, 254).

²⁰⁰ *Ritter*, 169 U.S. at 139–60.

²⁰¹ Following *Erie R.R. Co. v. Tompkins*, 304 U.S. 64 (1938), the decisions of state courts became binding on federal courts.

²⁰² *Ritter*, 169 U.S. at 142.

²⁰³ *Id.* at 145.

²⁰⁴ *Id.* at 154.

²⁰⁵ *Id.*

²⁰⁶ *Id.* at 157–58 (discussing *Supreme Commandery of Knights of the Golden Rule v. Ainsworth*, 71 Ala. 436 (Ala. 1882) (crime) and *Fauntleroy's Case*, 4 Bligh (N.S.) 194, 211 (felony)). The Court also relied upon cases where the relevant death had been caused by a crime. *Ritter*, 169 U.S. at 156–58 (citing *N.Y. Mut. Ins. Co. v.*

time had been decriminalized in nearly all of the states, a general moral opprobrium towards suicide was still entrenched.²⁰⁷

Although *Ritter* stood for the proposition that it was contrary to public policy for a life insurer to cover death by suicide while sane, it carved out an exception for suicide while insane.²⁰⁸ The relevant definition of sanity was similar to that stated in the *M'Naghten* rule from the criminal law context: the insured must have been unable to understand the nature of his act or not know the act was wrong.²⁰⁹ The requisite forfeiture of insurance coverage in the event of suicide therefore was not necessary if the insured's mental state rendered him morally blameless for his suicide.²¹⁰ Moreover, even if the insurer attempted to exclude death by suicide in the policy form,

Armstrong, 117 U.S. 591, 600 (1886) (murder); Hatch v. Mut. Life Ins. Co., 120 Mass. 550 (Mass. 1876) (illegal abortion)).

²⁰⁷ Long, *supra* note 198, at 778–79. *See, e.g.*, Commonwealth v. Mink, 123 Mass. 422, 424 (Mass. 1877) (describing suicide as “sinful and immoral”); Aetna Life Ins. Co. v. Milward, 82 S.W. 364, 365 (Ky. 1904) (“The act of suicide is not only unnatural, but is highly immoral and criminal.”). *See also* Wash. v. Glucksberg, 521 U.S. 702, 774 (1997); Thomas J. Marzen et al., *Suicide: A Constitutional Right?*, 24 DUQ. L. REV. 1, 67–100, 148–242 (1985).

²⁰⁸ *Ritter*, 169 U.S. at 160 (“[I]f the suicide or self-destruction takes place when the assured is insane and not accountable for his acts, the rule arising from public policy does not apply, and his representatives are entitled to the policy money.”) (internal quotations omitted). Drawing upon the criminal law, some [state] courts explained that the act of taking one’s own life was not truly “suicide” if the decedent was insane. Long, *supra* note 198, at 779. *See also* Phadenhauer v. Germania Life Ins. Co., 54 Tenn. (7 Heisk.) 567, 577 (Tenn. 1872).

²⁰⁹ *See* Daniel Ward, *The M'Naghten Rule: A Re-evaluation*, 45 MARQ. L. REV. 506, 507 (1962). The *Ritter* court approved of the trial court’s following instruction:

If Mr. Runk understood what he was doing, and the consequences of his act or acts, to himself as well as to others—in other words, if he understood, as a man of sound mind would, the consequences to follow from his contemplated suicide, to himself, his character, his family and others, and was able to comprehend the wrongfulness of what he was about to do, as a sane man would—then he is to be regarded by you as sane. Otherwise he is not.

Ritter, 169 U.S. at 148.

²¹⁰ *See* Long, *supra* note 198, at 780. Other courts at the time allowed insanity of an insured suicide to be demonstrated if it could be shown that the suicide acted under an irresistible “impulse.” *See, e.g.*, Mut. Life Ins. Co. v. Terry, 82 U.S. 580, 582 (1872).

courts often upheld the argument that an insane person was unable to form the requisite intent to commit suicide—so the exclusion did not apply and coverage would be allowed.²¹¹ The non-responsibility requirement was thus applied in the life insurance context in a manner that relied upon general moral disapproval of suicide that was not reflected in the criminal statutes, but it nonetheless borrowed from criminal law conceptions of blameworthiness and sanity.

Soon after *Ritter*, state legislatures and supreme courts moved to repudiate the Supreme Court's declared common-law prohibition of life insurance for suicide committed while sane.²¹² The states shifted towards allowing coverage—whether the insured was sane or insane—so long as the individual did not defraud the insurer by failing to disclose an intent to commit suicide that was already present upon purchasing the policy.²¹³ Some states entirely prohibited the use of suicide as a defense by insurers unless fraud could be demonstrated²¹⁴ or allowed the defense only within a relatively short time-frame after the policy was purchased.²¹⁵ This appears to have been motivated by an increasing public perception that suicide was almost always the result of mental illness and not an act that was inherently

²¹¹ See Gary Schuman, *Suicide and the Life Insurance Contract: Was the Insured Sane or Insane? That Is the Question—Or Is It?*, 28 TORT & INS. L.J. 745, 756–57 (1993) (discussing *Terry*, 82 U.S. at 590–91).

²¹² E.g., *Patterson v. Nat. Premium Mut. Life Ins. Co.*, 75 N.W. 980, 983 (Wis. 1898); *Lange v. Royal Highlanders*, 110 N.W. 1110, 1112 (Neb. 1907).

²¹³ See W. R. Vance, *Suicide as a Defense in Life Insurance*, 30 YALE L.J. 401, 401–02 (1921) (noting that at the time of the article in 1921 only Alabama followed the *Ritter* decision).

²¹⁴ E.g., MO. REV. STAT. § 6945 (1909) (“In all suits upon policies of insurance on life hereafter issued by any company doing business in this state, to a citizen of this state, it shall be no defense that the insured committed suicide, unless it shall be shown to the satisfaction of the court or jury trying the cause, that the insured contemplated suicide at the time he made his application for the policy, and any stipulation in the policy to the contrary shall be void.”) (current version at MO. REV. STAT. §376.620 (West 2017); *Whitfield v. Aetna Life Ins. Co.*, 205 U.S. 489, 494 (1907) (applying the statute). See also Vance, *supra* note 213, at 402 (“So deep-seated is the revolt against the [*Ritter*] doctrine that no fewer than four state statutes have been passed prohibiting, either absolutely or with qualifications, the setting up of suicide as a defense in actions on insurance policies.”).

²¹⁵ See Schuman, *supra* note 211, at 754 n.55 (listing state statutes).

wrong.²¹⁶ “Such insanity is one of the diseases to which the insurer must have known that the insured was subject, and the unwitting act of self-destruction is as much the consequence of that disease as if some vital organ were thereby fatally affected.”²¹⁷

Eventually the Supreme Court took heed of this shift, reversing its position in *Ritter*,²¹⁸ and recognizing states’ power to limit an insurance company’s ability to use suicide as a defense²¹⁹ as well as their power to allow life insurance that affirmatively covers suicide whether sane or insane.²²⁰ The result was that life insurance companies were able to enforce a suicide exclusion of the following form: “If the insured dies by suicide, while sane or insane, within two years of the date of issue, our only liability will be for the amount of premiums paid.”²²¹ So long as such exclusions were clear, they were enforceable in the majority of jurisdictions,²²² and they

²¹⁶ See *Morton v. Supreme Council of Royal League*, 73 S.W. 259, 262 (Mo. Ct. App. 1903) (“[S]elf-destruction always indicates, if not insanity, at least an irresponsible state of mind, and may well be considered part of the risk assumed, if not specially excluded. For this reason the doctrine in question is not welcomed by all courts and seemingly not by those of this State, which hold that a company doing a life insurance business takes a risk on an insured person’s life subject to all his human passions and frailties.”). See also *Campbell v. Supreme Conclave Improved Ord. of Heptasophs*, 49 A. 550 (N.J. 1901) (finding coverage for suicide after felony arrest); *Lange v. Royal Highlanders*, 106 N.W. 224 (Neb. 1905), *aff’d*, 110 N.W. 1110 (Neb. 1907); *Marcus v. Heralds of Liberty*, 88 A. 678 (Pa. 1913); *Jackson v. Loyal Additional Benefit Ass’n*, 205 S.W. 318 (Tenn. 1917). See generally VANCE, *supra* note 38, at 561.

²¹⁷ VANCE, *supra* note 38, at 564.

²¹⁸ *Vance*, *supra* note 213, at 401 (noting the ruling of *Nw. Mut. Life Ins. Co. v. Johnson*, 254 U.S. 96 (1920)). William O. Cramer & Henry C. Rubin, *Public Policy in Relation to Suicide in Life Insurance*, 27 GEO. L.J. 361, 362–63 (1939).

²¹⁹ *Whitfield v. Aetna Life Ins. Co.*, 205 U.S. 489, 501 (1907). Justice Harlan, who wrote *Whitfield*, also wrote the majority opinion in *Ritter*.

²²⁰ *Nw. Mut. Life Ins. Co.*, 254 U.S. at 102.

²²¹ Schuman, *supra* note 211, at 759. The two-year period is the same as the incontestability period in most policies (*i.e.*, the period after which an insurer cannot contest coverage) which is also mandated by statute in many states. See VANCE, *supra* note 38, at 565.

²²² JERRY, *supra* note 59, at § 63B[a] (“Assuming the exclusion is clear, no court questions its enforceability.”). Schuman, *supra* note 211, at 759–60 (discussing how the minority view “sane or insane” language does not negate any issue of the insured’s state of mind).

remain prevalent today.²²³ Under a typical life insurance policy today, if the insured kills himself during the first two years, then the exclusion applies regardless of his mental state;²²⁴ if he commits suicide after the two-year period, then recovery is allowed.²²⁵

Comparing the contemporary rule with the *Ritter* rule reveals the degree to which the underlying structure of the non-responsibility requirement has persisted, even as public conceptions of the harms for which an individual must be held responsible have changed.²²⁶ Over the nineteenth and twentieth centuries, suicide itself gradually ceased to be regarded by the legislatures and courts as a *malum in se* for which the insured must be held responsible.²²⁷ Analytically and morally separate concerns about the wrongness of fraud, however, persisted.²²⁸ The shift to allowing insurers to deny coverage to suicides, “sane or insane,” committed during the first two years of coverage arose as an administratively simple way of expressing this

²²³ See JERRY, *supra* note 59, at § 63B[a] (“Only a few American courts have spoken approvingly of the ‘English rule’ that holds it against public policy for a beneficiary to recover under a policy where the insured, while sane, committed suicide. These cases are old and of dubious authority today.”). See also PATTERSON, *supra* note 143, at 261–62 (whether suicide ought to be treated as an implicit exception to life insurance policies is “not often of practical importance, since either express exceptions in the contract or statutes expressly denying such an exception are ordinarily decisive.”).

²²⁴ JERRY, *supra* note 59, at § 63B[a]. See Schuman, *supra* note 211, at 759–60.

²²⁵ See JERRY, *supra* note 59, at § 63B[a]; Schuman, *supra* note 211, at 755 n.59, 759–60. In order for a life insurance policy beneficiary (e.g., a child or spouse) to make out a *prima facie* case for recovery, she must show the existence of the contract, the payment of premiums, and the death of the insured. Schuman, *supra* note 211, at 750. The insurer then bears the burden of proving the applicability of a suicide exclusion, which involves overcoming a presumption that the insured did not commit suicide. *Id.* See also 9A PLITT ET AL., *supra* note 36, at § 138:66.

²²⁶ See generally *New Amsterdam Cas. Co. v. Jones*, 135 F.2d 191, 194 (6th Cir. 1943) (reviewing history of changing rules on the insurability of suicide).

²²⁷ See Long, *supra* note 198, at 772.

²²⁸ *Cramer & Rubin*, *supra* note 218, at 363. See, e.g., *Mut. Life Ins. Co. v. Durden*, 72 S.E. 295 (Ga. Ct. App. 1911); *Supreme Lodge Knights of Pythias v. Trebbe*, 74 Ill. App. 545 (Ill. App. Ct. 1897), *rev'd*, 53 N.E. 730 (Ill. 1899); *Seiler v. Econ. Life Ass'n of Clinton*, 74 N.W. 941 (Iowa 1898); *Supreme Conclave, Improved Ord. of Heptasophs of Balt. City v. Miles*, 48 A. 845 (Md. 1901); *Campbell v. Supreme Conclave Improved Ord. of Heptasophs*, 49 A. 550 (N.J. 1901); *Jackson v. Loyal Additional Benefit Ass'n*, 205 S.W. 318 (Tenn. 1917).

distinction, in the sense that it generally avoids a costly inquiry into the mental state of the deceased insured.²²⁹ Thus, if the insured kills himself soon after he purchased insurance, it will be presumed he purchased it fraudulently, planning on self-destruction. But if he kills himself thereafter, it can be presumed that he suffered from mental illness, a fatal disease that life insurance is supposed to cover. At bottom, the analysis has remained fundamentally the same over time: if the allegedly covered loss was the result of the insured's own inherently wrong act, then coverage should be forbidden. Otherwise, the presumption is that coverage should be allowed.

3. Insuring Innocent Co-Insureds

Applying the non-responsibility requirement becomes complicated when multiple insureds are covered under a single policy, and one of them causes a loss to both. One sadly-common fact-pattern involves co-insured spouses,²³⁰ where one spouse (usually an abusive or suicidal husband) intentionally burns down the marital home.²³¹ Can the innocent spouse recover under her fire insurance policy in such a situation? For more than a

²²⁹ See *Longenberger v. Prudential Ins. Co. of Am.*, 183 A. 422, 425 (Pa. Super. Ct. 1936) (“In fixing one year (or two years, as the case may be) as the period within which the insured’s suicide, whether sane or insane, should not create a cause of action on the policy, the insurers adopted the year or two thus chosen as the extreme limit of time that a person would probably take out life insurance with the intent of killing himself in order to benefit his family or his creditors at the expense of the insurance company; and by necessary implication they agreed thereby that suicide of the insured, sane or insane, after the expiration of this period of time was not contemplated by him at the time the insurance was taken out and would not be a fraud on the company; and that they would regard suicide after that length of time as one of the hazards covered by the policy.”).

²³⁰ See Willy E. Rice, *Destroyed Community Property, Damaged Persons, and Insurers’ Duty to Indemnify Innocent Spouses and Other Co-Insured Fiduciaries: An Attempt to Harmonize Conflicting Federal and State Courts’ Declaratory Judgments*, 2 EST. PLAN. & CMTY. PROP. L.J. 63, 82 (2009) (“Generally . . . ‘a fiduciary relationship exists between spouses’; and it does not terminate until the marriage dissolves.”).

²³¹ See *id.* at 71 (describing this as the “largest category of all innocent co-insured disputes” based on an empirical survey); BAKER & LOGUE, *supra* note 21, at 204 (citing Brief of Amici Curiae California Alliance Against Domestic Violence and Ad Hoc Committee of Law Professors Working on Domestic Violence in *Borman v. State Farm Fire & Cas. Co.*, 521 N.W.2d 266 (Mich. 1994) (No. 96266)).

hundred years,²³² courts and commentators have struggled with this question, and jurisdictions remain divided on it today.²³³ This sub-section traces the historical evolution of the law in this area. Whereas the previous two sub-sections revealed the degree to which the non-responsibility requirement has tracked changing social conceptions of what is *inherently wrong*, this sub-section shows that the non-responsibility requirement also tracks changing conceptions of individual *substantial control*.

From the late nineteenth century through the middle of the twentieth century, innocent spouses, involved in the above-described situation, seldom recovered from their insurer.²³⁴ When disputes over coverage arose, courts

²³² Cf. *Monaghan v. Agric. Fire Ins. Co.*, 18 N.W. 797 (Mich. 1884) (involving an arsonist mother and innocent co-insured children).

²³³ See, e.g., *Trinity Universal Ins. Co. v. Kirsling*, 73 P.3d 102, 105 (Idaho 2003) (listing majority and minority decisions vis-à-vis the rights of innocent co-insured spouses); *Atlas Assurance Co. v. Mystic*, 822 P.2d 897, 899–901 (Alaska 1991) (describing conflicts); *Hedtcke v. Sentry Ins. Co.*, 326 N.W.2d 727, 737–39 (Wis. 1982) (describing conflicts); *Murphy v. Tex. Farmers Ins. Co.*, 982 S.W.2d 79, 80–82 (Tex. Ct. App. 1998), *aff'd*, 996 S.W.2d 873 (Tex. 1999) (describing history of innocent co-insured decisions in Texas courts); *Cal. Cas. Ins. Co. v. Northland Ins. Co.*, 56 Cal. Rptr. 2d 434, 442 (Cal. Ct. App. 1996) (discussing conflicting innocent co-insured decisions); and *Thoele v. Aetna Cas. & Sur.*, 39 F.3d 724, 727 n.1 (7th Cir. 1994) (discussing conflicting innocent co-insured decisions).

For scholarship on this problem, see Rice, *supra* note 230; Rachel R. Watkins Schoenig, *Property Insurance and the Innocent Coinsured: Was It All Pay and No Gain for the Innocent Co-Insured?*, 43 *DRAKE L. REV.* 893 (1995); David L. Nersessian, *Penalty by Proxy: Holding the Innocent Policyholder Liable for Fraud by Coinsureds, Claims Professionals, and Other Agents*, 38 *TORT TRIAL & INS. PRAC. L.J.* 907 (2003); Benjamin M. Parrott, *For Better or For Worse - The Iowa Supreme Court's Decision to Compensate the Innocent Coinsured Spouse in Sager v. Farm Bureau Mutual Insurance Company*, 54 *DRAKE L. REV.* 561 (2006).

²³⁴ The traditional view was that “an innocent spouse may not recover under a fire insurance policy for damages resulting from the other spouse’s fraud by deliberate burning of their jointly owned property.” *St. Paul Fire & Marine Ins. Co. v. Molloy*, 433 A.2d 1135, 1140 (Md. 1981) (quoting *Steigler v. Ins. Co. of N. Am.*, 384 A.2d 398, 399 (Del. 1978)). *But see* *Mercantile Tr. Co. v. N.Y. Underwriters Ins. Co.*, 376 F.2d 502, 506 (7th Cir. 1967) (one of few early cases where recovery was allowed); *Hoyt v. N.H. Fire Ins. Co.*, 29 A.2d 121, 123 (N.H. 1942) (another early cases where recovery was allowed). See generally Parrott, *supra* note 233, at 564–65; Marvin L. Karp, *Arson and the Innocent Co-Insured - Drafting Insurance Policies to Protect against Arson and Fraud*, 22 *BRIEF* 9, 9 (1993); JERRY, *supra* note 59, at § 63A n.196.

relied upon the legal oneness of the couple—whether through their joint property interests or through their joint contractual obligations with the insurer²³⁵—to impute the wrongful act to both spouses, thereby voiding all insurance coverage.²³⁶ As the Supreme Court of Oklahoma put it, “[t]o allow recovery . . . where the arsonist has been proven to be a joint insured would allow funds to be acquired by the entity of which the arsonist is a member and is flatly against public policy.”²³⁷

Over time, however, the rules applied to such situations changed, with courts tending to conclude that the innocent spouse ought to recover.²³⁸ Thus, in 1968, the Supreme Court of Wisconsin considered a situation in which an innocent co-insured husband attempted to recover under his insurance policy when his wife burned down their home.²³⁹ The court allowed coverage, and stated:

²³⁵ See, e.g., *Rockingham Mut. Ins. Co. v. Hummel*, 250 S.E.2d 774, 776 (Va. 1979) (“Furthermore, the form of the insurance contract was joint; the ‘Named Insured’ was ‘Harold Lee and Mildred Hummel’. Thus under the policy and as the ‘insured’, each spouse had the joint obligation to use all reasonable means to save and preserve the property. Likewise each spouse had the joint duty to refrain from defrauding the insurer.”); *Klemens v. Badger Mut. Ins. Co.*, 99 N.W.2d 865, 866 (Wis. 1959) (finding that when a policy is written in the joint names of a husband and wife, there arises a joint obligation not to commit fraud, and thus when one insured breaches the obligation, “the breach caused by intentional destruction is chargeable to both insureds and precludes recovery by the innocent joint insured.”). See generally Parrott, *supra* note 233, at 566.

²³⁶ See, e.g., *Steigler*, 384 A.2d at 399 (citing cases); *Koisor v. Cont’l Ins. Co.*, 13 N.E.2d 423, 425 (Mass. 1938).

²³⁷ *Short v. Okla. Farmers Union Ins. Co.*, 619 P.2d 588, 590 (Okla. 1980). Courts held that property ownership in joint tenancy, tenancy by the entirety, or community property served to void the policy as to both guilty and innocent coinsureds. See, e.g., *Bridges v. Com. Standard Ins. Co.*, 252 S.W.2d 511, 512–13 (Tex. Ct. App. 1952) (holding that an innocent co-insured spouse may not recover under a property insurance contract if the deviant co-insured spouse destroys jointly owned or community property).

²³⁸ See JERRY, *supra* note 59, at § 63A (“Beginning in the 1970s, a number of courts moved away from the rule barring recovery to a rule that permits recovery by an innocent coinsured of a loss intentionally caused by another coinsured.” (internal citations omitted)).

²³⁹ *Shearer v. Dunn Cnty. Farmers Mut. Ins. Co.*, 159 N.W.2d 89, 93 (Wis. 1968).

This court rejects the [insurer's] invitation to invent a doctrine that a spouse should be denied recovery on an insurance contract because of action of the other spouse when those actions cannot be imputed to the insured spouse. The marriage relationship should not be used as a basis for such a law. Married people are still individuals and responsible for their own acts. Vicarious liability is not an attribute of marriage.²⁴⁰

During the mid-twentieth-century, judges increasingly recognized that converting a joint property interest into a joint responsibility for arson “produces inequitable results.”²⁴¹ On this view, the possibility that an arsonist “may profit through the co-mingling of funds with the innocent insured or otherwise is a factual issue properly resolved by the fact finder.”²⁴² Courts also increasingly “tailor[ed] the recovery permitted [to] the innocent insured to guard against the possibility that the arsonist might receive financial benefit as a result of the arson.”²⁴³ So long as the arsonist was

²⁴⁰ *Id.* at 93.

²⁴¹ *See* Karp, *supra* note 234, at 11. *See, e.g.,* Hedtcke v. Sentry Ins. Co., 326 N.W.2d 727, 740 (Wis. 1982); *Steigler*, 384 A.2d at 401 (noting that “the ‘oneness’ theory . . . is, to say the least, somewhat ‘quaint’ in this day and age.”); *id.* at 402 (holding that allowing the innocent co-insured to recover “represent[s] both a more modern analysis of the problem and [] produce[s] a fairer result . . .” insofar as it avoids holding that the innocent insured is responsible for the independent actions of her deviant spouse). *Cf.* Howell v. Ohio Cas. Ins. Co., 327 A.2d 240, 242 (N.J. Super. Ct. App. Div. 1974) (“The significant factor is that the responsibility or liability for the fraud—here, the arson—is several and separate rather than joint, and the husband’s fraud cannot be attributed or imputed to the wife who is not implicated therein. Accordingly, the fraud of the co-insured husband does not void the policy as to plaintiff wife.”).

²⁴² *Hedtke*, 326 N.W.2d at 740.

²⁴³ *Id.* (denying the arsonist recovery while giving the innocent insured a pro-rata share). *See also* Am. Econ. Ins. Co. v. Liggett, 426 N.E.2d 136, 140 (Ind. Ct. App. 1981) (“The legal fiction of the entirety’s estate in real estate is designed for the protection of the spouses and the marriage. It was initially designed to prevent the individual creditors of either spouse from taking the marital home. The courts generally, and divorce courts in particular, find no difficulty in dividing an entirety’s estate. I find it a perversion of this legal fiction, designed to protect the spouses’ rights and marital property, to use it to destroy the property rights of an innocent spouse.”).

prevented from recovering, allowing the innocent co-insureds to receive coverage was increasingly deemed unproblematic.²⁴⁴

In order to reach this holding, state courts often determined that the language in the couple's insurance policy addressing intentional harm was ambiguous²⁴⁵—which opened the door to traditional methods of insurance policy interpretation that allow ambiguities to be construed against the insurer.²⁴⁶ In response, insurance companies redrafted their policy forms to unambiguously render co-insured spouses' obligation not to burn their home joint, rather than several.²⁴⁷ This led to a period during which many courts found such revised policy terms unambiguous and enforced them in favor of the insurance company—against the claims of the innocent co-insured.²⁴⁸

The spread of such new policy language inaugurated the third, and most recent, phase in the evolution of this area of law wherein both courts and legislatures began to add “a second step to the contractual analysis.”²⁴⁹

²⁴⁴ See, e.g., *Com. Union Ins. Co. v. State Farm Fire & Cas. Co.*, 546 F. Supp. 543, 547 (D. Colo. 1982). See generally JERRY, *supra* note 59, at § 63A; Karp, *supra* note 234, at 10.

²⁴⁵ Often, the relevant policy language excluded from coverage are the intentional or fraudulent acts of “the insured,” which courts have found to be ambiguous where only one of multiple co-insureds misbehaved. See, e.g., *Watson v. United Servs. Auto. Ass'n*, 566 N.W.2d 683, 690 (Minn. 1997) (citing similar cases).

²⁴⁶ See, e.g., *Steigler v. Ins. Co. of N. Am.*, 384 A.2d 398, 401 (Del. 1978) (using the reasonable expectations doctrine to decide in favor of the innocent insured); *Hoyt v. N.H. Fire Ins. Co.*, 29 A.2d 121, 123 (N.H. 1942) (“The ordinary person owning an undivided interest in property, not versed in the nice distinctions of insurance law, would naturally suppose that his individual interest in the property was covered by a policy which named him without qualification as one of the persons insured.”).

²⁴⁷ See Parrott, *supra* note 233, at 571 (“Insurers attempted to employ less ambiguous and more relevant language, including using the terms ‘an insured’ and ‘any insured’ in place of ‘the insured.’”); JERRY, *supra* note 59, at § 63A.

²⁴⁸ See, e.g., *Volquardson v. Hartford Ins. Co. of the Midwest*, 647 N.W.2d 599, 607 (Neb. 2002) (construing an intentional loss exclusion and explicitly stating “that there is no public policy specifically articulated by Nebraska statutes or case law which would preclude application of the intentional acts exclusion . . . to negate coverage against peril of fire to an innocent coinsured . . .”); *Vance v. Pekin Ins. Co.*, 457 N.W.2d 589, 590 (Iowa 1990) (holding that “[a]n innocent coinsured spouse may recover depending on whether the coinsureds’ interests under the policy are joint or severable.”). See generally Parrott, *supra* note 233, at 573 (discussing how the *Vance* court found no concerns about the legitimacy of the exclusion despite there being public policy concerns); JERRY, *supra* note 59, at § 63A n.205.

²⁴⁹ *Watson*, 566 N.W.2d at 689.

Courts ask whether public interest requires that policy language unambiguously denying coverage to an innocent co-insured ought nonetheless to be judicially reformed to allow for coverage. An increasing number of courts have answered this question in the affirmative. Thus, in *Osbon v. National Union Fire Insurance Co.*, the Supreme Court of Louisiana held that a widow could recover under a fire insurance policy that named both her and her husband as co-insureds, even though it unambiguously denied her coverage because her husband intentionally destroyed their home.²⁵⁰ The policy language at issue differed from the Louisiana standard fire insurance policy language, however, and therefore conflicted with a state law that required all fire insurance policies made in the state to conform to the standard.²⁵¹ The Court interpreted the legislatively-mandated standard fire insurance form only to preclude recovery for an insured “who . . . is responsible for causing the loss . . . ,” and reformed the widow’s policy accordingly thereby granting her coverage.²⁵² It argued:

This interpretation is in line with the legislative intent Specifically, we do not believe that the legislature intended to impute the incendiary actions of an insured to the innocent co-insured who has no control over the unauthorized conduct. Nor do we think that the legislature intended to penalize an innocent insured, here, a victim of arson, with the perpetrator of a wrongful act. That is, having lost the property, the innocent insured would be victimized once again by the denial of the proceeds under the insurance policy. We do not believe that the legislature intended for the statute to have such a harsh and inequitable result.²⁵³

Since *Osbon*, other state high courts have adopted the method deciding such cases by analyzing the insurance policy language against the backdrop of a

²⁵⁰ *Osbon v. Nat’l Union Fire Ins. Co.*, 632 So.2d 1158, 1161 (La. 1994).

²⁵¹ *Id.* at 1160–61.

²⁵² *Id.* at 1160.

²⁵³ *Id.*

legislatively-mandated standard policy form—typically in order to find coverage for innocent co-insureds.²⁵⁴

Over the last several decades, state legislatures have also enacted laws that explicitly allow a spouse to recover under an insurance policy where the intentional act of her partner is part of a pattern of domestic abuse, despite unambiguous policy exclusions to the contrary.²⁵⁵ These statutes have been interpreted to promote “the public good by ‘not punishing the innocent victim for the wrongs of another’”²⁵⁶ Such statutes are often interpreted to require that any compensation enjoyed by an innocent spouse does not flow to the bad actor—a requirement that courts have been able to satisfy, in practice.²⁵⁷ Washington and Missouri statutes, for example, allow

²⁵⁴ See, e.g., *Trinity Universal Ins. Co. v. Kirsling*, 73 P.3d 102, 107 (Idaho 2003) (holding that the policy in question “provides less coverage than the standard policy in violation of [the state code].”); *Watson v. United Servs. Auto. Ass’n*, 566 N.W.2d 683, 691 (Minn. 1997) (holding that an “‘intentional loss’ provision, insofar as it excludes coverage for innocent co-insured spouses, is at odds with the rights and benefits of the Minnesota standard fire insurance policy.”); *Volquardson v. Hartford Ins. Co. of the Midwest*, 647 N.W.2d 599, 610 (Neb. 2002) (finding the *Watson*’s ruling determined “that insofar as the policy in question excluded coverage for an innocent coinsured, it conflicted with the standard policy and must be reformed.”); *Lane v. Sec. Mut. Ins. Co.*, 747 N.E.2d 1270, 1271 (N.Y. 2001) (holding that an intentional loss exclusion “impermissibly restricts the coverage mandated by statute and afforded the innocent insured.”). See also *Traders & Gen. Ins. Co. v. Freeman*, 81 F. Supp. 2d 1070, 1074–78 (D. Or. 2000) (applying a similar statutory construction and allowing the innocent coinsured to recover). See generally Parrott, *supra* note 233, at 578; Susan Randall, *Freedom of Contract in Insurance*, 14 CONN. INS. L.J. 107, 145–46 n.297 (2007) (citing cases).

²⁵⁵ See, e.g., NEB. REV. STAT. ANN. § 44–7406(6) (West 1998); N.D. CENT. CODE ANN. § 26.1-32-04 (West 1995); WASH. REV. CODE ANN. § 48.18.550 (West 2020); MO. ANN. STAT. § 375.1312(5) (West 2013) (“If an innocent coinsured files a police report and completes a sworn affidavit for the insurer that indicates both the cause of the loss and a pledge to cooperate in any criminal prosecution of the person committing the act causing the loss, then no insurer shall deny payment to an innocent coinsured on a property loss claim due to any policy provision that excludes coverage for intentional acts. . . . insurers shall not be required to make any subsequent payment to any other insured for the part of any loss for which the innocent coinsured has received payment. An insurer making payment to an insured shall have all rights of subrogation to recover against the perpetrator of the loss.”); 215 ILL. COMP. STAT. 5/155.22b (West 2004).

²⁵⁶ *Watts v. Farmers Ins. Exch.*, 120 Cal. Rptr. 2d 694, 702 (Cal. Ct. App. 2002).

²⁵⁷ See Parrott, *supra* note 233, at 587–89 (listing cases performing a “case-by-case” analysis).

an innocent spouse to recover so long as she files a police report and cooperates with any law enforcement investigation relating to the act of domestic abuse.²⁵⁸ Although not all states have moved in this direction, “[t]he clear trend has been in favor of allowing innocent co-insured coverage.”²⁵⁹

Thus, as social understanding of the marital relationship evolved over the course of the twentieth century, courts and legislatures increasingly determined that the non-responsibility requirement ought not to preclude an innocent spouse from recovering when her husband—acting on his own and often aiming to hurt her—intentionally destroys their home. Whereas earlier decisions treated the married couple as a unit and imputed joint responsibility for intentional loss to them both as a matter of law, later decisions disaggregated the two actors and denied coverage only to spouses who exercised substantial control over the destructive act.

IV. NORMATIVE ANALYSIS

The preceding Part II presented a theory of the non-responsibility requirement as a free-standing legal concept that assigns responsibility to the insured for certain types of acts on the basis of inherently moral ideas. It then suggested that the theory fits the law that we have today, and the law that preceded it, precisely because it has tracked underlying social conceptions of morality. The above analysis aimed to show that the non-responsibility requirement is part of our moral and legal culture—as evidenced by our practice.

The preceding Part II did not, however, offer a justification for the normative content of the non-responsibility requirement. Is it morally defensible to make insurance coverage depend on individual responsibility—and, in particular, on a conception of individual responsibility that turns on social understandings of which acts are “inherently wrong” and the insured’s “own”? This Part offers such a

²⁵⁸ WASH. REV. CODE ANN. § 48.18.550; MO. ANN. STAT. § 375.1312(5).

²⁵⁹ *Shepperson v. Metro. Prop. & Cas. Ins. Co.*, 312 F. Supp. 3d 183, 197 (D. Mass. 2018) (applying Massachusetts law to find coverage for the innocent co-insured, on the argument that the standard fire policy dictated by statute overrode the policy language). *See also* *Century-Nat'l Ins. Co. v. Garcia*, 246 P.3d 621, 627 (Cal. 2011) (finding in favor of innocent co-insured on grounds that statutorily mandated policy language overrode more restrictive language in insurer's form).

justification, in three steps. First, it argues that it is justifiable, as a matter of political theory, to use a conception of individual responsibility to place limits on insurance coverage. Second, it argues that the institutions and practices that we currently use to implement the non-responsibility requirement are well-suited to the task. Third, it argues that the two alternative instrumentalist theories—*i.e.*, those that focus on efficiency and victim compensation—are not as well-suited to the institutional framework of our current insurance law system.

A. POLITICAL THEORY

The theoretical argument in favor of the non-responsibility requirement is straightforward. It rests on the basic intuition that there is a meaningful distinction between luck and choice, and that the two forces jointly determine how well we fare in the world: someone's position can improve or decline based on her good or poor choices, and also based on her good or bad luck. Choice differs from luck in the sense that a person is responsible for the results of her choices, but she is not responsible for those things that we recognize as the result of luck.²⁶⁰ Because luck impacts persons differently, liberal-egalitarian theorists have long argued that redistribution is justified if it is done in a way that is "responsibility-tracking."²⁶¹ The general proposition is that "nonsubordination requires

²⁶⁰ Note that the conception of "luck" used here is similar to Dworkin's concept of "brute luck" rather than "option luck." Ronald Dworkin, *What is Equality? Part 2: Equality of Resources*, 10 PHIL. & PUB. AFFS. 283, 293 (1981) ("Brute luck is a matter of how risks fall out that are not in that sense deliberate gambles."). See Daniel Markovits, *How Much Redistribution Should There Be?*, 112 YALE L.J. 2291, 2294–95 (2003) (describing these intuitions).

²⁶¹ Markovits, *supra* note 260, at 2295. See, e.g., RONALD DWORKIN, *SOVEREIGN VIRTUE: THE THEORY AND PRACTICE OF EQUALITY* 287 (2000) ("[I]ndividuals should be relieved of consequential responsibility for those unfortunate features of their situation that are brute bad luck, but not from those that should be seen as flowing from their own bad choices."); G. A. Cohen, *On the Currency of Egalitarian Justice*, 99 ETHICS 906, 916 (1989) (arguing egalitarianism's "purpose is to eliminate involuntary disadvantage, by which I (stipulatively) mean disadvantage for which the sufferer cannot be held responsible, since it does not appropriately reflect choices that he has made or is making or would make."); Richard J. Arneson, *Luck Egalitarianism and Prioritarianism*, 110 ETHICS 339, 339 (2000) ("[T]he aim of justice as equality is to eliminate so far as is possible

redistribution to follow moral responsibility, specifically by eliminating luck's differential effects on persons' fortunes while leaving persons fully to bear the consequences of their (morally responsible) choices."²⁶² Respecting individual freedom to make choices thus requires a hands-off approach to some differences—*i.e.*, leaving people to bear the negative consequences of their bad choices and allowing them to enjoy the positive consequences of their good choices.²⁶³

Insurance can be interpreted straightforwardly as a redistributive practice that is justifiable from within such a liberal-egalitarian frame: it reallocates resources in a way that counteracts luck's differential effects while respecting insureds' capacity to make choices for which they are morally responsible.²⁶⁴ The rules and principles of insurance law therefore can be justified by showing that they support this liberal-egalitarian interpretation of insurance practice. The non-responsibility requirement, I argue, is justifiable in precisely this way: from a liberal-egalitarian standpoint, it is proper to force an insured to bear the cost of losses that are the result of his own (bad) choices.²⁶⁵ The normative framework of the non-responsibility requirement—which assigns responsibility to the insured on

the Impact on people's lives of bad luck that falls on them through no fault or choice of their own."); Kasper Lippert-Rasmussen, *Egalitarianism, Option Luck, and Responsibility*, 111 ETHICS 548, 548 (2001) ("As construed by the majority of its current supporters, egalitarianism accommodates choice and responsibility."); John E. Roemer, *A Pragmatic Theory of Responsibility for the Egalitarian Planner*, 22 PHIL. & PUB. AFFS. 146 (1993). See generally Markovits, *supra* note 260, at 2295–97 nn.17–24 (describing this general view among egalitarian political theorists).

²⁶² Markovits, *supra* note 260, at 2294 (describing the responsibility-tracking egalitarian view).

²⁶³ *Id.* at 2297–98 ("[T]aking from a person who has chosen well in order to compensate another person for the bad consequences of her bad choices involves subordinating the first person to the second. It involves requiring the first person to bear a burden for which he is not responsible—something the second person, who is after all the source of this burden, is not required to do.").

²⁶⁴ That insurance is easily interpreted as such a scheme of redistribution is demonstrated by the fact that prominent political theorists like Ronald Dworkin use hypothetical insurance markets as the model for thinking about what amount and kind of egalitarian redistribution is warranted. See Dworkin, *supra* note 260, at 292–304.

²⁶⁵ *Cf.* *Nicholson v. Am. Fire & Cas. Ins. Co.*, 177 So. 2d 52, 54 (Fla. Dist. Ct. App. 1965) ("We believe that a person has no right to expect the law to allow him to place responsibility for his reckless and wanton actions on someone else.").

the basis of the inherent wrongness of his act and on the basis of whether he exercised control over the act—makes sense as a way of distinguishing between losses that we think of as being the results of the insured’s bad luck, versus the results of his bad choices.

Of course, although a liberal-egalitarian framework can motivate an argument that the non-responsibility requirement is normatively necessary, it does not suggest that following the requirement is sufficient to justify the operations of any particular insurance practice or institution. The non-responsibility requirement determines when insurance protection for otherwise-covered losses should *not* be available; it says nothing about how much insurance protection *should be* available—a question about which political theorists also have something to say. A number of answers to this latter question—“How much insurance should there be?”—have been proposed, with varying degrees of radicalism.²⁶⁶ It is possible, however, to interpret the modern liberal welfare state, with its characteristic mix of market-based and government-run methods of allocating and reallocating resources, as one practical answer to this question. On this view, government supports the operation of markets (including insurance markets), whenever markets prove to be a better method of effecting responsibility-based redistribution than vertical control.²⁶⁷ Where markets (including insurance markets) fail to produce transfers that “ought” to occur, government intervenes to promote such transfers. In insurance markets specifically, such intervention usually takes the form of requirements (“mandates”) to purchase insurance or requirements that insurers not discriminate on the basis of certain characteristics.²⁶⁸ Where necessary, governments may also step in to create “public” forms of insurance that entirely bypass private insurance companies and the contractual form of the insurance policy. This pragmatic

²⁶⁶ See, e.g., Markovits, *supra* note 260; Roemer, *supra* note 261; Kenneth J. Arrow, *Uncertainty and the Welfare Economics of Medical Care*, 53 AM. ECON. REV. 941 (1963).

²⁶⁷ See R. H. Coase, *The Nature of the Firm*, 4 ECONOMICA 386 (1937). There may also be non-instrumental reasons why government may support the operation of markets. See DANIEL MARKOVITS, CONTRACT LAWS AND LEGAL METHODS 1197–1203 (2012).

²⁶⁸ Two key elements of the Affordable Care Act—the insurance mandate and the prohibition against discrimination on the basis of preexisting conditions—can be understood in this way. See Patient Protection and Affordable Care Act, Pub. L. No. 111-148, 124 Stat. 119 (2010), *as amended by* Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, 124 Stat. 1029 (2010) (amending §5000A of the Internal Revenue Code of 1986).

compromise between what Guido Calabresi calls “commodification” and “commandification”²⁶⁹ is our usual method of social ordering; it is not particular to insurance or to insurance law. The relevant point, for the purpose of this inquiry, is that it too is plausibly justifiable from within a liberal-egalitarian frame.

Obviously, there are other normative standpoints from which one could critique, or justify, the institutions of insurance practice and the rules and principles of insurance law. Taking such perspectives might make the non-responsibility requirement, in particular, appear to be either justifiable or not. Utilitarianism, for example, might recommend violating the non-responsibility requirement under certain circumstances.²⁷⁰ Similarly, a subtler application of liberal-egalitarian political theory than the simplified sketch provided above might reveal that the non-responsibility requirement, as-applied in insurance cases, is not always straightforwardly justifiable.²⁷¹ This Article’s goal is not to provide a complete political-theoretical defense of the non-responsibility requirement from a liberal-egalitarian point of view. Nor does it aim to argue that this particular political-theoretical interpretation of insurance law is the best one. Rather, this Article aims to show merely that what is generally recognized as the dominant strain of political theory today (*i.e.*, liberal egalitarianism in the Rawlsian tradition, which is explicitly designed to reach “reflective equilibrium” with our considered moral judgments²⁷²) appears both to reflect a generally shared set of moral intuitions²⁷³ and to provide a method of justifying the non-responsibility requirement.

²⁶⁹ GUIDO CALABRESI, *THE FUTURE OF LAW AND ECONOMICS: ESSAYS IN REFORM AND RECOLLECTION* 24–40 (2016).

²⁷⁰ *See* JOHN RAWLS, *A THEORY OF JUSTICE* 26–27 (1971) (discussing utilitarianism and its contrast with egalitarianism).

²⁷¹ For example, it may well be argued that the choices that individuals face are themselves the result of luck, and therefore, it does not make moral sense to hold them responsible for the results of their choices. *See, e.g.*, Victor Tadros, *Distributing Responsibility*, 48 *PHIL. & PUB. AFFS.* 223, 226–28 (2020).

²⁷² *See* Richard Arneson, *Egalitarianism*, *STAN. ENCYCLOPEDIA OF PHIL.* (Apr. 24, 2013), <https://plato.stanford.edu/archives/sum2013/entries/egalitarianism/>; Norman Daniels, *Reflective Equilibrium*, *STAN. ENCYCLOPEDIA OF PHIL.* (Oct. 14, 2016), <https://plato.stanford.edu/entries/reflective-equilibrium/>.

²⁷³ *Cf.* ABRAHAM, *supra* note 129, at 10 (“When values are shared . . . then they have as much objectivity as we have a right to ask for or ever need. Agreement on

B. INSTITUTIONAL DESIGN

In order for this normative theory of insurance law's non-responsibility requirement to be a good theory, it must also be able to justify the institutional practices of insurance law that implement the requirement. This Section argues that the theory of the non-responsibility requirement laid out above can provide normative support for the particular institutional framework that we use to apply it.

1. Courts as Deciders

When disputes arise as to the proper application of the non-responsibility requirement—understood as a legal concept that turns on normative conceptions of inherent harm and individual control—it makes sense that *courts* decide such cases. Courts are well-positioned to determine whether a particular loss is, based on the two-pronged analysis of the non-responsibility requirement, appropriately characterized as the result of “bad luck,” and therefore, insurable or as the result of the insured’s “choice,” and therefore, uninsurable. Information about such moral phenomena²⁷⁴ is available to courts. It is, of course, proper that legislatures be allowed to correct courts’ distinctions between luck and choice, when necessary.²⁷⁵ But as a general matter, this is a type of determination that courts are relatively well-suited to make.

2. The Priority of Policy Language

In practice, the non-responsibility requirement almost never becomes a dispositive issue unless a court first determines that the terms of the insurance policy could be interpreted to cover losses for which the insured may be held morally responsible.²⁷⁶ Does this practice of giving decisional priority to the policy terms, rather than to the non-responsibility

what is important creates objectivity in the realm of values. In discussing the purposes of insurance law, therefore, the issue is not whether the values served by this body of law are objectively grounded, but whether they are able to command agreement.”).

²⁷⁴ See *supra* Section II.A.2.

²⁷⁵ Indeed, legislatures appear to have done so in the case of suicide and certain types of innocent co-insureds. See discussions *infra* Section III.B.1–2.

²⁷⁶ See *supra* notes 38–39 and accompanying text. But see *infra* notes 253–259 and accompanying text.

requirement as an abstract principle, fit with the normative theory of the requirement laid out in the preceding Section?

Yes. As explained above, a private market for insurance coverage can be presumed to underwrite risks according to terms of coverage that are mutually agreeable to insurers and insureds. Assuming such terms capture an understanding that was shared by both parties,²⁷⁷ they can be presumed to be socially beneficial so long as they do not contravene general principles of public policy—including the non-responsibility requirement.²⁷⁸ Of course, an insurance agreement may be tailored to indemnify the insured against fewer losses than could permissibly be covered without violating the non-responsibility requirement.²⁷⁹ Insurance law's starting point, therefore, is the same as contract law's starting point: the terms of the agreement determine the relative rights and obligations of the parties.²⁸⁰ Once the meaning of the terms is determined, a second level of analysis asks whether background principles—including the non-responsibility requirement—suggest that the terms ought to be rendered unenforceable.²⁸¹ It therefore makes sense that the non-responsibility requirement would only become a dispositive issue when policy language would seem to extend coverage to a loss that was the result of the insured's bad choice rather than his bad luck.

3. Enforcement of the Requirement by Insurers

The non-responsibility requirement is typically enforced by the insurer seeking to deny coverage for a particular claim, rather than by a sort of “attorney general” representing the public's interest in the proper

²⁷⁷ This is not always a safe assumption. What courts often do, in practice, is determine the scope of ambiguity, which can be large, and pick the point within it that is insured-friendly, and/or meets the reasonable expectations of the insured. See Ronald J. Gilson et al., *Text and Context: Contract Interpretation as Contract Design*, 100 CORNELL L. REV. 23, 81–86 (2014) (discussing the recent trajectory of the doctrines of *contra proferentem* and “reasonable expectations”).

²⁷⁸ For example, it may be argued that such exchanges are beneficial because they are efficient in the sense of being Pareto-improving, or because they enact a particular type of formal relationship.

²⁷⁹ For a colorful example on the types of restrictions that may be placed on insurance coverage, see WILLIAM F. MEYER, *LIFE AND HEALTH INSURANCE LAW*, A SUMMARY 221–22 (1976) (quoting an 1854 life insurance policy).

²⁸⁰ RESTATEMENT OF THE L. OF LIAB. INS. § 44 (AM. L. INST. 2019).

²⁸¹ *Id.* at § 45.

functioning of redistributive institutions. Does this fit within the normative theory described above?

Yes. Insurers are likely to be particularly effective enforcers of the non-responsibility requirement. Insurance companies have a profit-based motive to be constantly testing the limits of what types of coverage courts will agree is impermissible under the non-responsibility requirement in order to avoid paying claims.²⁸² Insurers also have relatively good access to the information needed to perform this role because claims adjusters can gather facts about the circumstances of the loss to determine whether it was the result of the insured's choice or luck. Of course, it is possible that insurers' business models might be such that they lack a financial interest in vigorously enforcing the non-responsibility requirement, and, therefore, fail to do so.²⁸³ Given the economics of the insurance business, however, such situations have proven to be both rare and correctible through regulation and legislation.²⁸⁴

This point reveals that the non-responsibility requirement is not plausibly understood as a principle of "private law" in the sense that that term is used by New Private Law theorists today.²⁸⁵ Its normative force (as argued above) arises not out of a correlative relationship between private persons (*e.g.*, tortfeasor and victim, buyer and seller)²⁸⁶ but rather out of general commitments to conceptions of freedom, equality, and distributive justice. The non-responsibility requirement, therefore, is not formally

²⁸² See *supra* notes 55–57 and accompanying text.

²⁸³ See TOM BAKER & SEAN J. GRIFFITH, ENSURING CORPORATE MISCONDUCT: HOW LIABILITY INSURANCE UNDERMINES SHAREHOLDER LITIGATION 188 (2010) (suggesting that directors and officers liability insurers "understand that, in the long run, their D&O insurance market will dry up if they press too hard on the fraud exclusion." Thus, they fail to challenge coverage for fraud-based claims even when the defense might be available.); Meyers & Hersch, *supra* note 91, at 976–77 (arguing that employment practices liability insurance coverage appears to extend to liability for wrongful acts either perpetrated or covered up by upper management, as evidenced by the recent Harvey Weinstein settlement).

²⁸⁴ See Meyers & Hersch, *supra* note 91, at 978–83 (discussing regulatory and legislative changes meant to address moral hazard).

²⁸⁵ See, *e.g.*, ERNEST J. WEINRIB, THE IDEA OF PRIVATE LAW ch. 1 (1995) (defining private law); JULES L. COLEMAN, THE PRACTICE OF PRINCIPLE: IN DEFENCE OF A PRAGMATIST APPROACH TO LEGAL THEORY ch. 1–5 (2001).

²⁸⁶ See WEINRIB, *supra* note 285, at ch. 1 (describing the correlative relationship between doer and sufferer in private law).

dependent on a “sufferer” bringing a civil suit against a “doer;”²⁸⁷ there is no theoretical reason why the insurer (or any other party, for that matter) must be the one to enforce the non-responsibility requirement against the insured.²⁸⁸ There are, however, practical reasons why we rely on insurers to fulfill the enforcement role under most circumstances.

C. ALTERNATIVE THEORIES

As discussed in Part I, there are at least two other normative theories that are frequently used to determine whether a loss that the insured caused ought to be insurable. On the one hand, economic analysis suggests that losses ought not to be insurable if allowing coverage will create moral hazard. On the other hand, concern with victim compensation suggests that losses ought to be deemed insurable even if they were the result of the insured’s intentional act whenever doing so would increase the victim’s likelihood of recovery.²⁸⁹ In this Section, I suggest that although these

²⁸⁷ *Id.*

²⁸⁸ This is important, because in any insurance agreement at least one of the parties—the insurance company—is a corporation. Kantian arguments that reason from the normative status of natural persons in a private-law relationship therefore are not available in the insurance context. Obligations that derive from a commitment to treat private parties as “ends in themselves” fall flat in situations involving corporations, which are properly regarded as means rather than ends. See Daniel Markovits, *Contract and Collaboration*, 113 YALE L.J. 1417, 1464–71 (2004) (arguing that a collaborative theory of contract cannot be applied to contracts between corporations); Nathan B. Oman, *Corporations and Autonomy Theories of Contract: A Critique of the New Lex Mercatoria*, 83 DENV. UNIV. L. REV. 101, 113–114 (2005) (arguing against the practice of assuming contracting parties are natural persons and not corporations).

In theory, there might be circumstances in which it would be better to create a sort of “attorney general” in charge of enforcing the insured’s non-responsibility requirement. Indeed, similar moves were taken beginning in the eighteenth century when it was determined that insurance companies were failing to prevent policyholders from using insurance as a form of gambling—for example, by taking out a policy on a life or property in which they had no interest. Since then, “wager policies” have been strictly controlled by government-appointed regulators. See GEOFFREY CLARK, *BETTING ON LIVES: THE CULTURE OF LIFE INSURANCE IN ENGLAND, 1695–1775* (1999) (describing legislative and enforcement efforts taken to prevent insurance from serving as a form of gambling).

²⁸⁹ See *infra* Section II.B–C.

frameworks might be able to justify decisions about which losses ought to be insurable, they are not well-suited to the institutional practice that we currently have for deciding coverage disputes involving the insured's misbehavior.

1. Moral Hazard Concerns

As discussed above, disputes over the insurability of a given loss are generally resolved by courts. But courts are poorly situated to determine whether granting or denying coverage in a given case will promote wider economic goals, such as decreasing the overall amount of losses, spreading risks more cheaply, or decreasing the administrative costs of the system for dealing with accident costs.²⁹⁰ Judges are not in a good position to gather the sort of information necessary to make decisions on these bases. The argument that judges, when deciding cases about the insurability of intentionally caused losses, ought to consider moral hazard, therefore, is weak from an institutional-competency perspective.²⁹¹

Insurers, by contrast, have better access to the type of information necessary to determine, for example, whether granting a particular type of coverage will create moral hazard—*i.e.*, increase the overall amount of loss.²⁹² They are also generally able to structure their relationships with insureds to further their own interest in promoting such goals.²⁹³ It therefore

²⁹⁰ This draws on Guido Calabresi's distinction between primary, secondary, and tertiary costs. CALABRESI, *supra* note 9, at 26–28. *Cf.* JULES L. COLEMAN, RISKS AND WRONGS 204 (1992) (discussing Calabresi's economic goals distinction). On the third point (decreasing administrative costs), standardized policy forms may support this purpose. *See* Abraham, *supra* note 24, at 779 (“Insurance law has had little need to generate cost-reducing default rules, because the insurance industry has already done so through the development of standard-form policy provisions.”).

²⁹¹ *See* Ernest J. Weinrib, *The Insurance Justification and Private Law*, 14 J. LEG. STUD. 681, 682 (1985) (discussing a ruling from the High Court of Australia that found no justification for courts to make use of policy determinants in most circumstances).

²⁹² *See* Meyers & Hersch, *supra* note 91, at 973 (“When insurers seek to reduce moral hazard for purposes of their bottom line, society benefits as well.”).

²⁹³ *See* Baker, *supra* note 188, at 126 (“[I]nsurance companies have a strong financial incentive to construct the insurance relationship in a manner that answers the theoretical objections to insurance for punitive damages [and moral hazard concerns].”). Insurers can, for example, impose deductibles, coinsurance, limits, and

makes sense to presume that these economic goals will be fairly well-served so long as insurance markets function smoothly. Put differently, it is reasonable to presume that market forces will contain moral hazard and related economic costs fairly well.²⁹⁴ The proper role for judges vis-à-vis such economic goals is, therefore, to ensure that the rules of insurance policy interpretation support the functioning of insurance markets.

This line of thinking suggests that although the need to avoid moral hazard and to minimize other related costs of administering insurance may be an essential part of a good theory of insurance *economics*, it is probably not part of a good theory of insurance *law*. This distinction is important because it is often possible to give two overlapping justifications for a decision about whether an insured ought to receive coverage for a loss he caused.²⁹⁵ A denial of coverage to someone who incinerates his own barn might be justified as necessary to the healthy operation of the insurance business. On this argument, allowing coverage would lead to a torrent of other intentional losses, thereby threatening the solvency of insurers. The same denial might also be justified by referring to insurance law's underlying commitment—rooted in a moral distinction between choice and luck—to holding individuals responsible for their own bad acts. Both justifications “concur in the judgement,” as it were, that coverage should be denied to the arsonist.

To the extent that insurance companies insert language into their policy forms that clearly denies coverage to such individuals, it will often be the case that judges do not even reach the question of whether the non-responsibility requirement, on its own, requires a denial of coverage. But

experience-rated premiums in order to control moral hazard. *See* Meyers & Hersch, *supra* note 91, at 973. *Cf.* *N. Bank v. Cincinnati Ins. Cos.*, 125 F.3d 983, 988 (6th Cir. 1997) (“[C]ommon sense suggests that the prospect of escalating insurance costs and the trauma of litigation . . . would normally neutralize any stimulative tendency the insurance [of intentional torts] might have.”) (internal quotations omitted).

²⁹⁴ Of course, there may well be situations where insurance markets fail to promote such broader economic goals. Under such circumstances, legislatures are better-situated than courts—both epistemically, and normatively—to make the type of interventions necessary to steer the ship back on course.

²⁹⁵ *See* ABRAHAM, *supra* note 129, at 208 (discussing “multiple justification” of insurance law, including economic, distributional, and equitable purposes). *Cf.* Alan Schwartz & Daniel Markovits, *Function and Form in Contract Law*, in *THE OXFORD HANDBOOK OF THE NEW PRIVATE LAW* 243 (Andrew S. Gold et al. eds., 2020).

insofar as courts *are* required to determine whether the insured's self-caused losses ought to be covered under a policy that lacks a clear carve-out, it makes sense as a matter of institutional competency for them to apply modalities of analysis that suit their abilities and that are properly characterized as frameworks of insurance law. Legislatures, of course, might choose to intervene when it is determined that insurers are failing to, for whatever reason, adequately control moral hazard or promote other related economic goals. This is the type of public-policy-based decision to which legislatures are both epistemically and normatively well-suited.²⁹⁶ But barring such an intervention, it makes little sense for judges to be deciding intentional harm cases on the basis of moral hazard concerns rather than on the basis of the non-responsibility requirement.

This analysis also raises a deeper point about why, to the extent that judges *do* engage in moral-hazard-based reasoning, their decisions generally do not run contrary to the non-responsibility requirement's overtly normative framework for determining the scope of the insured's responsibility for his own harms.

"Moral hazard" is generally regarded as an evil because of an insured's increased tendency to engage in risky behavior that unfairly imposes costs on others—either by forcing innocent insureds in the same risk pool to pay higher premiums or by imposing negative externalities on third parties generally.²⁹⁷ Thus, for example, when auto insurance leads an insured

²⁹⁶ See CLARK, *supra* note 288, at 22 (arguing that the passage of the Gambling Act of 1774, which prohibited wagering policies in England, "represented the first thoroughgoing attempt to sunder activities that had previously been carried out side by side within a common domain and to consign them to different legal and moral spheres."); Baker, *supra* note 78, at 257–59 (discussing separation of gambling from insurance).

²⁹⁷ See, e.g., Priest, *supra* note 17, at 1026 ("The exclusion of coverage of losses intended by the insured thus benefits two classes of individuals. The first class is the broader set of insureds not intentionally engaging in acts causing harms. These insureds gain because the costs of intentional harm-causing activities will not be averaged into the premiums they pay. . . . The second set of beneficiaries is those that might suffer loss if insurance for intentional acts were available. That is, the number of intentional harm-causing actions and the extent of harm intentionally caused would be higher if insurance coverage were available than if coverage were excluded.").

to drive less carefully,²⁹⁸ this has the effect of raising premiums for other insureds and also increasing the danger to all others who share the road. Put differently, moral hazard is bad because it allows an insured to make choices that affect others in a way that subordinates their interests to the individual's. This formulation reveals that the normative force of the moral hazard argument is dependent upon an antecedent conception of responsibility-tracking distributive justice. Although multiple such conceptions are available, the most acceptable framework for judges to apply is the one our legal system has developed for exactly this context—*i.e.*, the notion of individual responsibility captured in insurance law's non-responsibility requirement.²⁹⁹ This explains why it is not common for judges to apply a steely-eyed economic analysis of "moral hazard"—as distinct from an overtly moralizing analysis—to explain, or to justify, decisions about what cannot be insured unless those decisions are independently acceptable according to the normative framework of the non-responsibility requirement.³⁰⁰

2. Victim Compensation

Questions about the insurability of particular losses are generally resolved through civil disputes between insurers and insureds. Third parties that are impacted by such disputes lack a formal role in the proceedings.³⁰¹

²⁹⁸ See, e.g., *Herschensohn v. Weisman*, 119 A. 705, 705 (N.H. 1923) (plaintiff and defendant were driving in the latter's car, and when plaintiff protested about defendant's reckless driving, defendant answered, "Don't worry, I carry insurance"; then came crash) (discussed in *McNeely*, *supra* note 5, at 33).

²⁹⁹ The fact that the availability of insurance coverage for negligence is not understood to be problematic from a moral hazard perspective proves this point. We hold a negligent tortfeasor responsible for harms in tort law, but we do not object to him using insurance to defray his responsibility for civil liability that might arise out of such a suit. See *infra* Section III.B.1 (discussing history of insurability of negligence).

³⁰⁰ Cf. *supra* notes 113–15 and accompanying text (discussing moral hazard concerns that are present in certain forms of nonetheless permissible coverage, such as insurance for negligence and suicide).

³⁰¹ See 7A PLITT ET AL., *supra* note 36, at § 104:2 ("As a general rule, and in the absence of a contractual provision or a statute or ordinance to the contrary, at common law, the absence of privity of contract between the claimant and the insurer

Third parties also generally have no say about whether those who might injure them purchase insurance coverage, or about the terms of the coverage that potential injurers do purchase.³⁰² These facts make it difficult to argue that our current institutional practice is structurally well-suited to consider the interests or deserts of such third parties—including victims of a tortfeasor-insured. The law of tort, by comparison, *does* provide an institutional mechanism whereby persons who have been wronged by an insured may seek redress directly against him or her. Tort suits are structured in a manner that is more appropriate to considering the interests of victims, who are the ones that initiate the legal process and that present evidence about the scope of the injuries they have suffered.³⁰³

Moreover, the legislative process provides an institutional mechanism whereby the interests of potential third parties can influence whether insurance is purchased (or provided by the government), as well as the scope of its coverage. Workers' compensation laws, mandatory automobile liability insurance laws, medical malpractice insurance,³⁰⁴ and the Patient Protection and Affordable Care Act's "individual mandate" are examples of this process working.³⁰⁵ When democratic representative bodies have decided to intervene in the marketplace in order to promote the goal of

bars a direct action by the claimant against the latter under both automobile liability insurance and under other forms of liability insurance, at least where the direct action is on the basis of the insured's negligence." (internal citations omitted)).

A minority of states have enacted "direct action" statutes, which provide victims with the right to sue the insurer of their tortfeasor directly. Two states, Louisiana and Wisconsin (as well as the territories of Puerto Rico and Guam), have enacted statutes that provide for a direct cause of action by an injured party against an insurer. *See* LA. STAT. ANN. § 22:1269 (2011); WIS. STAT. ANN. §§ 803.04(2), 632.24 (West 2021); P.R. LAWS ANN. tit. 26, §§ 2001, 2003 (2007); 22 GUAM CODE ANN. § 18305 (2017). These are not to be confused with "direct action" statutes in other states that permit a suit directly against a tortfeasor's insurer only after judgment has been secured against the insured. ALA. CODE § 27-23-2 (1975); IND. CODE ANN. § 27-1-13-7 (West 2016); N.Y. INS. LAW § 3420 (McKinney 2020).

³⁰² *See* Knutsen, *supra* note 63, at 230–31; BAKER & LOGUE, *supra* note 21, at 407 ("Whether we think that victims are the 'real' beneficiaries of liability insurance or not, they do not get to choose the liability insurance policies that their tortfeasors purchase.").

³⁰³ *See* JOHN C. P. GOLDBERG & BENJAMIN C. ZIPURSKY, *RECOGNIZING WRONGS* 26 (2020); Ernest J. Weinrib, *Corrective Justice in a Nutshell*, 52 U. TORONTO L.J. 349 (2002) (discussing how tort law effects corrective justice).

³⁰⁴ *See* cases cited in *supra* note 56.

³⁰⁵ *Id.*

victim compensation, it makes sense for courts to allow such clearly-expressed public policies to override more general principles of insurance law—including the non-responsibility requirement. In such cases, courts may legitimately override insurance law's non-responsibility requirement by averting explicitly to the state's interest, as expressed through legislation, in protecting a particular class of victims.³⁰⁶

This institutional division of labor suggests a reason for why victim-compensation-based arguments are often hamstrung in insurance coverage disputes. Attempts to treat victim compensation as private insurance's goal are exposed to the objection that such "insurance" will force innocent premium-payers to pay for other bad actors' poor choices.³⁰⁷ This objection

³⁰⁶ See, e.g., *Aetna Life & Cas. Co. v. McCabe*, 556 F. Supp. 1342, 1353 (E.D. Pa. 1983) (finding that intentional harm was covered by a medical malpractice liability policy because of Pennsylvania's "strong interest in compensating Pennsylvania victims of malpractice for injuries suffered at the hands of Pennsylvania physicians . . ."); *Nationwide Mut. Ins. Co. v. Roberts*, 134 S.E.2d 654, 659 (N.C. 1964) ("The primary purpose of compulsory motor vehicle liability insurance is to compensate innocent victims who have been injured by financially irresponsible motorists. Its purpose is not, like that of ordinary insurance, to save harmless the tortfeasor himself. Therefore, there is no reason why the victim's right to recover from the insurance carrier should depend upon whether the conduct of its insured was intentional or negligent. . . . The victim's rights against the insurer are not derived through the insured as in the case of voluntary insurance."); *Wheeler v. O'Connell*, 9 N.E.2d 544, 546–47 (Mass. 1937) (finding that intentional harm was covered by an auto liability policy because of a Massachusetts statute).

When states have declined to make malpractice insurance coverage mandatory, this has weighed against allowing victim compensation concerns to override the non-responsibility requirement. See, e.g., *Am. Home Assurance Co. v. Stone*, 61 F.3d 1321, 1328 (7th Cir. 1995).

³⁰⁷ See Swedloff, *supra* note 75, at 770 (discussing such objections); Baker, *supra* note 59, at 75 (discussing such objections); *Allstate Ins. Co. v. Mugavero*, 589 N.E.2d 365, 369 (N.Y. 1992) ("We believe . . . that the ordinary person would be startled, to say the least, by the notion that Mugavero should receive insurance protection for sexually molesting these children, and thus, in effect, be permitted to transfer the responsibility for his deeds onto the shoulders of other homeowners in the form of higher premiums.") (internal citations omitted). The possibility of allowing insurers to bring a subrogated claim against the tortfeasor-insured, and thereby to recoup the costs of coverage, does not solve this problem. If tortfeasor-insureds had deep-enough pockets to make the insurer whole, then they would also

has rhetorical force because the conception of responsibility-tracking distributive justice that has been developed in the insurance context is well-established and has normative appeal.³⁰⁸ Our society appears to have decided that there are certain types of losses that are the result of the insured's own bad acts; allowing the cost of these losses to be spread using insurance would be an unjust form of redistribution. The presence of the tort law regime—which reflects a logic of corrective justice rather than distributive justice³⁰⁹—makes it easier to argue that compensating victims in such situations simply is not the business of insurance law.³¹⁰ This suggests that unless and until we abandon the liberal-egalitarian logic that underpins the non-responsibility requirement, and adopt a more solidaristic political philosophy that collapses all corrective justice regimes into distributive justice regimes, the logic of victim-compensation will continuously fail to have real normative force in the arena of private insurance law. Such shifts are definitely possible, as illustrated by New Zealand's comprehensive no-fault accident compensation scheme³¹¹ and by the “individual mandate” in the Patient Protection and Affordable Care Act.³¹² But they are, at least in the American legal and

have deep-enough pockets to pay damages to their victims. It is only because such tortfeasor-insureds are frequently so poor as to be “judgement-proof” that arguments are made for recasting liability insurance as primarily a vehicle for victim compensation. See Gilles, *supra* note 33.

³⁰⁸ See discussion *infra* Section IV.A–B.

³⁰⁹ On the distinction between corrective and distributive justice, see Weinrib, *supra* note 303.

³¹⁰ See Baker, *supra* note 59, at 75 (on the conception of insurance as “defendant protection” rather than victim compensation); Weinrib, *supra* note 291, at 682 (“The task of the courts remains that of loss fixing rather than loss spreading and if this is to be altered it is, in my view, a matter for direct legislative action rather than for the courts.” (quoting *Caltrex Oil (Austl.) Pty. Ltd. v The Dredge “Willemstad”* (1976) 136 CLR. 529, 581 (Austl.)).

³¹¹ See Simon Connell, *Community Insurance Versus Compulsory Insurance: Competing Paradigms of No-Fault Accident Compensation in New Zealand*, 39 LEGAL STUD. 499, 499–500 (2019) (discussing New Zealand's comprehensive no-fault accident compensation scheme where “victims of personal injury by accident receive ‘entitlements’ under the scheme and cannot recover compensation from wrongdoers through the civil law. New Zealand still has a law of torts, but tort cases are rarely concerned with personal injuries.”).

³¹² See Patient Protection and Affordable Care Act, Pub. L. No. 111-148, 124 Stat. 119 (2010), as amended by Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, 124 Stat. 1029 (amending §5000A of the Internal

political tradition, localized exceptions to a general rule. Moreover, the steady gravitational pull back from solidarism towards individualism is, today more than ever in the United States, difficult to ignore.³¹³ So long as that pull has force, victim-compensation arguments will generally fall flat in the insurance-law arena.³¹⁴

V. IMPLICATIONS FOR INSURANCE LAW

A successful theory of the non-responsibility requirement must also provide a useful framework for analyzing insurance law problems that appear to fall within its ambit. Kenneth Abraham has argued that such a project is unlikely to succeed.³¹⁵ Although he agrees that background principles of insurance law generally prevent indemnification of the insured's own intentional losses, he argues that such principles are not helpful when attempting to determine the scope of coverage in particular cases.³¹⁶ Theorizing the “essence of what insurance is designed to protect against, is a poor and misleading substitute for doing the hard work of interpreting policy language”³¹⁷ which, he argues, is the “actual source of

Revenue Code of 1986) (requiring all citizens to purchase health insurance or pay a fee).

Note that the penalty for failure to purchase “minimum coverage” under the Affordable Care Act was called a “shared responsibility payment,” revealing its solidaristic logic. *See No Health Insurance? See If You'll Owe A Fee*, HEALTHCARE.GOV, <https://www.healthcare.gov/fees/fee-for-not-being-covered/> (last visited Oct. 22, 2021) (“A payment (‘penalty,’ ‘fine,’ ‘individual mandate’) you made when you filed federal taxes if you didn’t have health insurance that counted as qualifying health coverage for plan years 2018 and earlier. The fee for not having health insurance no longer applies. This means you no longer pay a tax penalty for not having health coverage.”).

³¹³ *See, e.g.*, Timothy Jost, *The Tax Bill and the Individual Mandate: What Happened, and What Does It Mean?* HEALTH AFFS. (Dec. 20, 2017), <https://www.healthaffairs.org/doi/10.1377/hblog20171220.323429/full/> (describing the repeal of the individual mandate).

³¹⁴ *See* Swedloff, *supra* note 75, at 768 (“Even to the extent that crime victims elicit compassion or have a lobby, the redistributive nature of [a] compulsory insurance regime will likely meet fierce opposition, and moral arguments about indemnifying bad actors will likely color the debate.”).

³¹⁵ *See* Abraham, *supra* note 24.

³¹⁶ *Id.* at 791–92.

³¹⁷ *Id.* at 797.

these limitations on coverage”³¹⁸ Deciding cases on the basis of theories of insurance law, rather than on the basis of specific policy exclusions, can also have material downsides, Abraham suggests:

To the extent that policy language already satisfactorily reflects . . . [background principles], making reference to [such principles] . . . as if [they] were not entirely subsumed within applicable policy language could only risk implying incorrectly to decision makers that they had two decisions to make, one applying policy language and the other applying the separate and additional requirements of a legal rule In its least harmful form, such an approach would lead to needless duplication of effort. In a more harmful form, the approach could generate incorrect decisions.³¹⁹

This Article has argued that although it is proper for courts, as a first step, to focus on policy language in coverage disputes involving the insured’s own bad acts, such an analysis is not always sufficient. If the requisite policy language is absent or ambiguous, and if the insurer raises a defense that sounds in the non-responsibility requirement, judges do indeed have a second decision to make. Although there are good reasons why judges ought not to *begin* their analysis with the consideration of background principles, it is suggested here that the possibility of such a second-level analysis does not undermine the practice of insurance law generally.³²⁰

This Part proposes several other practical implications of the preceding theorization of the non-responsibility requirement. Sections A and B point to two places that the *RLLI* departed from the non-responsibility requirement. Section C shows how a deeper understanding of the requirement can be tactically useful to those who might want to reform the insurance law we have today.

³¹⁸ *Id.* at 791.

³¹⁹ *Id.* at 781–82.

³²⁰ Some courts have explicitly adopted this two-step process in the insurance context. *See, e.g.*, *Perl v. St. Paul Fire & Marine Ins. Co.*, 345 N.W.2d 209, 211 (Minn. 1984) (“There are, as we see it, two main issues: (1) Does the insurance policy, by its terms, cover forfeited attorney fees? (2) If so, is such a policy provision unenforceable as a matter of public policy?”).

A. INSURANCE OF LIABILITIES INVOLVING “AGGRAVATED FAULT”

The *RLLI* includes a section addressing insurance of liabilities involving “aggravated fault,”³²¹ which refers to insurance policies that provide coverage for civil liability for “criminal acts, expected or intentionally caused harm, fraud, or other conduct involving aggravated fault.”³²² Early drafts of the *RLLI* stated that “[i]t is not against public policy for a liability insurer to pay damages to a third-party claimant for the civil liability of the insured for intentionally caused harm, punitive damages, fraud, criminal acts, or other conduct involving aggravated fault.”³²³ After receiving comments on the draft,³²⁴ the *RLLI*'s reporters revised the section to add that “[e]xcept as barred by legislation or judicially declared public policy, a term in a liability insurance policy providing coverage for civil liability arising out of aggravated fault is enforceable.”³²⁵

This Article suggests that the general common law of insurance—embodied in the non-responsibility requirement—is that the insured ought not to be able to use insurance to avoid responsibility for his own bad acts, and that this is reflected not only in judicial opinions, but also in legislation, regulations and the policy forms themselves. A more correct restatement of this area of the law, therefore, would be the inverse of the *RLLI*'s formulation: except as *allowed* by legislation or judicially declared public policy, a term in a liability insurance policy providing coverage for civil liability arising out of aggravated fault is *unenforceable*.

³²¹ RESTATEMENT OF THE L. OF LIAB. INS. § 45 (AM. L. INST. 2019).

³²² *Id.* at § 45(2).

³²³ RESTATEMENT OF THE L. OF LIAB. INS. § 34(2) (AM. L. INST., Council Draft No. 2, 2015).

³²⁴ *See, e.g.*, Letter from Kim V. Marrkand to Reporters regarding §§ 34–35 (Jan. 20, 2016), at 2–3 (cited in Victor E. Schwartz & Christopher E. Appel, *Restating or Reshaping the Law?: A Critical Analysis of the Restatement of the Law, Liability Insurance*, 22 U. PENN. J. BUS. L. 718, 741 n.120 (2020)) (quoting Marrkand's letter, which stated that the proposed rule “runs squarely against established law in numerous jurisdictions” and “does away with the public policy determination of state legislatures and courts that have concluded that insurance coverage for punitive damages is against public policy”) (internal quotations omitted).

³²⁵ RESTATEMENT OF THE L. OF LIAB. INS. § 45(2) (AM. L. INST. 2019).

As described above, this encompasses the contexts where legislatures have determined that victim compensation concerns are paramount. Where such interventions have not been made, however, general principles of insurance law suggest that the insured ought not to receive coverage for his own bad acts. This suggests, further, that the majority-rule interpretation of the carve-out for “expected or intended” language is the correct one, insofar as it denies coverage to an insured who was morally responsible for an otherwise-covered loss.³²⁶ States that have departed from this standard as their general rule of interpretation can be understood to have departed from general principles of insurance law—which are, as argued above, normatively justifiable and well-suited to our current institutional setup.

Earlier drafts of the *RLLI* also suggested that the pay-and-then-subrogate approach³²⁷ would be consistent with current insurance law doctrine.³²⁸ The theory of the non-responsibility requirement articulated in this Article suggests otherwise. To replace the general prohibition against allowing the insured to receive coverage for his own bad acts with a pay-and-then-subrogate approach is certainly normatively defensible. It does not, however, conform to the immanent normative logic of the non-responsibility requirement, the doctrine of insurance law, or to the division that our legal system has made between tort and insurance law. Of course, should victim-compensation concerns be deemed paramount in certain situations, it would be proper for a legislature to impose the pay-and-then-subrogate approach. But until that time, it makes more sense to view the cases that have gone down that path as exceptional.

B. BURDENS OF PROOF

In addition to the sustained judicial disagreement over the meaning of the expected/intended language in liability insurance policies,³²⁹ courts are also divided over which party has the burden of proving whether bodily

³²⁶ See *supra* note 67 (describing the *RLLI*'s standpoint on the expected and intended language).

³²⁷ See *supra* notes 91–98 and accompanying text (discussing the pay-and-then-subrogate approach).

³²⁸ RESTATEMENT OF THE L. OF LIAB. INS. § 47 cmt. j (AM. L. INST., Preliminary Draft No. 3, 2016) (“Subrogation against the insured provides an alternative to a public-policy-based prohibition of insurance for certain liabilities.”).

³²⁹ See discussion *infra* Section II.B.

injury or property damage was expected or intended from the standpoint of the insured.³³⁰ The dispute arises out of differing understandings of the effect of the language—specifically, whether it defines the scope of the initial grant of coverage or whether it carves out an exception from that initial grant.³³¹

Some argue, on the one hand, that the language is meant to describe the initial grant of coverage and that “[i]t is hornbook law” that the insured bears the burden of proving that its claim falls within the policy’s insuring agreement.³³² Because such expected/intended language often is included in the definition of an “occurrence” in the insuring agreement, rather than (or in addition to) the language under the heading, “Exclusions,” it may be understood as a description of the initial scope of coverage rather than a carve-out from it.³³³

On the other hand, some authorities hold that the expected/intended language is an “exclusion” from the already-defined scope of coverage, regardless of where it is stated in the insurance policy itself.³³⁴ The burden

³³⁰ See 3 DAVID LEITNER ET AL., LAW AND PRACTICE OF INSURANCE COVERAGE LITIGATION § 35:20 (2005) (“Inconsistency in opinions which address the burden of proof issue appears to arise from a situation which, in the eyes of some, presents a fundamental conflict.”); Fischer, *supra* note 76, at 105–10 (discussing the differing rulings of courts).

³³¹ See Fischer, *supra* note 76, at 107–08 (discussing the debates on whether the intentional act language is an “exception” or an “exclusion”).

³³² See, e.g., *New Castle Cnty. v. Hartford Accident & Indem. Co.*, 933 F.2d 1162, 1181 (3d Cir. 1991) (“It is hornbook law that the insured must demonstrate that the claimed loss is comprehended by the policy’s general coverage provisions.”); *id.* at 1191 (“Thus, to establish coverage, the [insured] must show that . . . it ‘neither expected nor intended’ environmental damage to result from its operation”); *Chem. Leaman Tank Lines, Inc. v. Aetna Cas. & Sur. Co.*, 817 F. Supp. 1136, 1148 (D.N.J. 1993), *aff’d in part and remanded*, 89 F.3d 976 (3d Cir. 1996); *Royal Globe Ins. Co. v. Whitaker*, 226 Cal. Rptr. 435, 437 (Cal. Ct. App. 1986) (“[H]ere, the insurer only promises to indemnify or defend actions involving bodily injury caused by an accident resulting in bodily injury neither expected nor intended by the insured. It was therefore the appellants’ burden to show they came within this definition.”). See generally LEITNER ET AL., *supra* note 330, at § 35:20 (discussing this debate).

³³³ See Fischer, *supra* note 76, at 108.

³³⁴ See, e.g., *Stonewall Ins. Co. v. Asbestos Claims Mgmt. Corp.*, 73 F.3d 1178, 1205 (2d Cir. 1995) (“[U]nder New York law, the exclusionary effect of policy

typically rests on the insurer to prove that claims are barred by a valid exclusion to coverage, and exclusions are typically construed by courts narrowly with all ambiguities resolved in favor of the insured.³³⁵ The *RLLI* takes this position—*i.e.*, that the expected/intended language is an exclusion regardless of its location in the policy form, and that the “insurer bears the burden of proving that a claim falls within the scope of an exclusion in the policy.”³³⁶

If the non-responsibility requirement is a basic feature of insurance law that describes the types of coverage that are available, then it makes more sense to conceive of it as a description of the initial grant of coverage, rather than as a carve out from that grant. This is true, moreover, regardless of where relevant policy terms reside in the insurance agreement.³³⁷ This position reflects the proposition that insurance policy language that explicitly carves out coverage for the insured’s own bad acts mostly serves to codify the underlying and implicit common law rule that defines what insurance is, and also reflects the reasonable expectations of both the insurer and the insured: neither insurer nor insured can reasonably expect insurance to cover the insured’s own bad acts.³³⁸

If this is correct, then it is more proper to place the initial burden upon the insured, rather than the insurer, to show that the policy language

language, not its placement, controls allocation of the burden of proof.”), *op. modified on other grounds*, 85 F.3d 49 (2d Cir. 1996). See generally RESTATEMENT OF THE L. OF LIAB. INS. § 32 cmt. a (AM. L. INST. 2019) (“[E]xclusions can appear in almost any part of an insurance policy: the insuring agreement, the definitions section, endorsements, and even in the conditions section.”).

³³⁵ See, e.g., *Gore Design Completions, Ltd. v. Hartford Fire Ins. Co.*, 538 F.3d 365, 370 (5th Cir. 2008) (applying Texas law) (“Exclusions are narrowly construed, and all reasonable inferences must be drawn in the insured’s favor.”). See generally French, *supra* note 18, at 75.

³³⁶ RESTATEMENT OF THE L. OF LIAB. INS. § 32 cmt. e (AM. L. INST. 2019).

³³⁷ Cf. PATTERSON, *supra* note 143, at 257–67 (describing “impliedly excepted causes”).

³³⁸ Cf. Bruce Chapman, *Allocating the Risk of Subjectivity: Intention, Consent, and Insurance*, 57 U. TORONTO L.J. 315, 315 (2007) (“[I]nsurance for [intentional] wrongs is not consistent with the reasonable expectations of the two contracting parties, the insurer and the insured.”).

that closely tracks the non-responsibility requirement does not preclude coverage.³³⁹

C. FUTURE LEGAL CHANGE

Given the non-responsibility requirement's status as a long-established and stable principle of the common law that governs insurance, as well as its justifiability from both a political-theoretical and an institutional-competency perspective, normative proposals to reform insurance law would be wise to work within its conceptual architecture.³⁴⁰ Attempts to remove or replace insurance law's conception of individual responsibility outright are likely to face significant obstacles, given its strong legal and normative foundations.

This recognition can be tactically useful for potential reformers. For those who would prefer liability insurance companies to be forced to cover the harms inflicted by insured murderers, rapists, or child molesters, for example, it may make strategic sense to recast the insured's acts in the courtroom as the result of mental health deficiencies—rather than as especially heinous crimes.³⁴¹ Such a radical re-orientation might seem difficult to imagine, but the history of the evolution of suicide coverage provides a helpful model for such a strategy. Harmful acts that are understood to be the result of mental incapacity, or “irresistible impulses,” are less likely to be deemed uninsurable under the non-responsibility

³³⁹ It may still be appropriate to allow this initial burden to be carried easily, thereby still giving the insurer the burden of producing evidence that overcomes a higher standard, in order to show that the non-responsibility requirement bars coverage. *Cf.* *Brown v. Snohomish Cnty. Physicians Corp.*, 845 P.2d 334, 340 (Wash. 1993) (en banc) (once insured has made a *prima facie* case that there is coverage, burden shifts to insurer to prove that an exclusionary provision applies); Schuman, *supra* note 211, at 750 (“Generally, in life insurance contract cases, the beneficiary makes out a *prima facie* case for recovery merely by showing the existence of the contract, the payment of premiums, and the death of the insured. The insurer then bears the burden of pleading and proving the applicability of the suicide exclusion.” (internal citations omitted)).

³⁴⁰ *Cf.* Balganesch & Parchomovsky, *supra* note 110, at 1304–09 (making a similar point).

³⁴¹ *Cf.* Dahlia Lithwick, *Is Pedophilia a Crime or an Illness?*, SLATE (Mar. 3, 2019, 7:30 PM), <https://slate.com/news-and-politics/2019/03/leaving-neverland-michael-jackson-pedophilia-punishment.html>.

requirement.³⁴² The same inner logic of the non-responsibility requirement may also explain why proposals to create mandatory insurance regimes for domestic intentional torts—which are generally not covered under homeowners insurance policies—have failed.³⁴³ Insofar as such proposals have been unable to recast domestic violence as something for which the insured tortfeasor is *not* morally responsible, they have faced predictable resistance to “the thought of helping bad actors with liability insurance.”³⁴⁴

Those who are interested in controlling moral hazard may also find it tactically useful to understand the inner logic of the non-responsibility requirement. Recently, the Weinstein Company received a payout under its employment practices liability insurance policy for its liability in a class action settlement for Harvey Weinstein’s pervasive sexual harassment.³⁴⁵ Although Mr. Weinstein’s behavior was apparently “widely known” within the company,³⁴⁶ the insurer did not attempt to use the non-responsibility requirement as a defense to coverage—even though such a defense might well have been successful.³⁴⁷ Erin Meyers and Joni Hersch have argued that the availability of such coverage “is troubling from the standpoint of ex post moral hazard.”³⁴⁸ Allowing insurance coverage for “this type of behavior incentivizes a business’s decision makers to attempt to cover up instances of

³⁴² See *supra* notes 200–05 and accompanying text.

³⁴³ See Wriggins, *supra* note 93, at 165 (making such a proposal); Swedloff, *supra* note 75, at 768–71 (discussing the likelihood of enactment of Wriggins’s proposal).

³⁴⁴ Swedloff, *supra* note 75, at 770–71. See also *id.* at 771 n.168 (“Indeed, I am struck by the general aversion to this proposal (this is by no means an empirical claim), even among colleagues and peers who are especially sympathetic toward the plight of crime victims.”).

³⁴⁵ See Alisha Haridasani Gupta, *Weinstein’s Accusers Near a \$25 Million Settlement. He Pays the Victims Zero.*, N.Y. TIMES (Dec. 13, 2019), <https://www.nytimes.com/2019/12/13/us/weinstein-sexual-misconduct-settlement.html>; Meyers & Hersch, *supra* note 91, at 974.

³⁴⁶ Ronan Farrow, *From Aggressive Overtures to Sexual Assault: Harvey Weinstein’s Accusers Tell Their Stories*, NEW YORKER (Oct. 10, 2017), <https://www.newyorker.com/news/news-desk/from-aggressive-overtures-to-sexual-assault-harvey-weinsteins-accusers-tell-their-stories>.

³⁴⁷ Meyers & Hersch, *supra* note 91, at 974.

³⁴⁸ *Id.* at 947. See also Joan T. A. Gabel et al., *The Peculiar Moral Hazard of Employment Practices Liability Insurance: Realignment of the Incentive to Transfer Risk with the Incentive to Prevent Discrimination*, 20 NOTRE DAME J.L. ETHICS & PUB. POL’Y 639, 641 (2006) (“[W]hen the injured third party is an employee, EPLI creates a peculiar and particularly troubling moral hazard”).

discrimination, harassment, retaliation, and wrongful termination, rather than addressing them head on.”³⁴⁹ Meyers and Hersh propose that these moral hazard concerns could be addressed by imposing federal regulations on insurers in the form of mandatory minimum coinsurance for employer-facilitated wrongs, as well as regulations allowing insurers a right of subrogation against their insured in such cases.³⁵⁰

The analysis in Part III of this Article suggests that these regulatory proposals are not likely to be successful. The institutional design of our current insurance regime suggests that moral hazard concerns are adequately and appropriately addressed by the insurer, on its own.³⁵¹ There is, moreover, little to prevent insurers from refusing to recover from the insured through subrogation, even if they are given the right to do so.³⁵² Meyers and Hersh suggest an alternative tack that may be more successful: the imposition of uninsurable fines by the EEOC against employers who facilitate wrongful employment acts.³⁵³ Such a remedy relies on the logic of punishment for inherently bad acts,³⁵⁴ and so cannot be undercut by the argument that moral hazard is not the concern of insurance law as such.

VI. CONCLUSION

Commentators often argue that “[i]t is a mistake to focus on the indemnification of the ‘bad actor’ to the exclusion of the compensation to the innocent victim.”³⁵⁵ Such arguments are generally rooted in a sociological analysis of the tort and insurance system, understood as a whole, which reveals that “[l]iability insurance protects not just the well being of

³⁴⁹ Meyers & Hersch, *supra* note 91, at 947. *See id.* at 975 (“[I]f an insurer does not hold a business any more or less accountable based on upper management’s actions, they will be incentivized to cover up any misbehavior.”).

³⁵⁰ *Id.* at 977–81 (“Because many employment suits are brought under federal law, such as Title VII, the ADA, or the ADEA, Congress could feasibly amend these statutes to place restrictions on the EPLI market.”).

³⁵¹ *See* discussion *supra* Section IV.C.1.

³⁵² *See* Meyers & Hersch, *supra* note 91, at 981 (conceding this point).

³⁵³ *Id.* at 984.

³⁵⁴ Currently, any damages resulting from EEOC lawsuits against employers are insurable. Under this proposal, Congress would need to characterize the punishment as a regulatory fine, which is generally excludable under insurance contracts. *See id.*

³⁵⁵ Swedloff, *supra* note 75, at 766. *See also* Knutsen, *supra* note 63, at 230; Wriggins, *supra* note 93, at 151.

the insured, but also the well being of the victim.”³⁵⁶ As demonstrated above, even in first-party insurance contexts—such as property insurance or life insurance—there are frequently innocent third parties who would benefit from the insured receiving coverage for their own misbehavior.³⁵⁷

It is also often argued that moral hazard concerns recommend that coverage for intentional harm should be allowed when it is not likely to incentivize misbehavior,³⁵⁸ and disallowed when it is likely to increase the net amount of losses.³⁵⁹ Allowing incentive effects to determine the scope of permissible coverage will, in the long run, allow insurers to “provide the broadest level of insurance” to the largest possible population.³⁶⁰

This Article suggests that although there are merits to these perspectives, they are not the *law’s* perspective. The majority rules of private insurance law doctrine present it as a method of protecting insureds, rather than as a way of protecting third parties, or as a method of maximizing the efficient spreading of losses.³⁶¹ This distinctly legal understanding of insurance has ideological force, because it can be justified straightforwardly using mainstream political-theoretical frameworks, as well as arguments based on relative institutional competencies and rule of law. Thus, although the sociological and economic perspectives can motivate calls for legal and institutional reform, they struggle to provide an accurate description of the law we have today.

Gaining an understanding of this matters, for two reasons.

First, “insurance” is often used by scholars, lawyers, and judges as a stand-in term for a legal arrangement that pursues purely instrumental goals, such as loss-spreading, maximization of welfare, minimization of loss, or

³⁵⁶ Swedloff, *supra* note 75, at 766. *See also* Baker, *supra* note 59, at 75 (“[L]iability insurance protects victims.”); French, *supra* note 18, at 100 (“[P]ublic policies such as compensating victims and enforcing contracts outweigh the notion that it would be unseemly to allow insurance recoveries for such conduct.”).

³⁵⁷ *See* discussion *infra* Section II.B.

³⁵⁸ *See, e.g.*, Scheuermann, *supra* note 89, at 343 (“In brief, if the insured-actor intentionally causes the insurance-activating event to occur, he violates the fortuity requirement, but he does not necessarily realize moral hazard. He realizes moral hazard only if he violates the fortuity requirement with the intent to exploit his insurance coverage.”).

³⁵⁹ *See, e.g.*, Priest, *supra* note 17, at 1026.

³⁶⁰ *Id.*

³⁶¹ *Cf.* Knutsen, *supra* note 63, at 211 (describing a conception of liability insurance as “wealth protection”).

progressive redistribution.³⁶² From this perspective, “insurance” is juxtaposed to a more traditional view of private law that “treats the two litigants as connected through an immediate personal interaction as doer and sufferer of the same harm.”³⁶³ Justice Traynor’s famous opinion in *Escola v. Coca-Cola Bottling Co. of Fresno*, a products liability case, has this character: “[t]he cost of an injury and the loss of time or health may be an overwhelming misfortune to the person injured, and a needless one, for the risk of injury can be insured by the manufacturer and distributed among the public as a cost of doing business.”³⁶⁴ Such a conception of insurance as merely a mechanism of risk-spreading is often leveraged to reform areas of the private law (most often, tort law) along instrumentalist lines.³⁶⁵

This Article suggests that, at least from the law’s perspective, “insurance” is not what proponents of these arguments think it is. Rather, insurance law, like tort law and criminal law, contains its own logic for assigning responsibility. Our existing legal practices and institutions of insurance reflect certain concepts and normative commitments which are *immanent* in them. This is why everyday lawyers may feel some resistance, in their gut, to the proposition that legal liability for an injury caused by the insured’s own misbehavior ought to be assigned among insurer, insured, and victim not according to a conception of individual responsibility but rather, for example, according to what is the most efficient way to spread the loss.³⁶⁶ In situations where the non-responsibility requirement suggests that the

³⁶² See Weinrib, *supra* note 291, at 684 (discussing instrumentalist use of “insurance”).

³⁶³ *Id.* at 683. See also, *id.* (“Now the invoking of insurance undermines this conception of [private] law by draining the parties’ relationship of its immediacy. Attention is no longer confined to the interaction of doer and sufferer.”).

³⁶⁴ *Escola v. Coca Cola Bottling Co.*, 150 P.2d 436, 441 (Cal. 1944) (Traynor, J., concurring).

³⁶⁵ Private law theorists in the “formalist” tradition argue against this move. See, e.g., COLEMAN, *supra* note 290, at 208 (“We need to be careful not to confuse the fact that liability decisions have insurance implications with the very different claim that insurance implications should dictate liability decisions.”); Weinrib, *supra* note 291, at 687 (“The rise of insurance as a factor in tort litigation is a harbinger of the attenuation of the hold of private law as a ruling component of the American legal experience.”).

³⁶⁶ See COLEMAN, *supra* note 290, at 207 (“[S]preading costs in general is alien to institutions that impose liability in ways that reflect judgment of individual responsibility.”).

insured *ought not to be allowed to offset responsibility for his own bad acts*, an instrumentalized conception of insurance will conflict with the immanent logic of the law. This suggests that attempts to recast other areas of the law as types of “insurance” often misunderstand what insurance actually is, at least from a legal perspective.

Second, it is important to understand insurance law’s immanent logic because our government often leverages insurance concepts to justify broader social policies to the general public. Programs like unemployment insurance, Social Security, Medicare, and Medicaid, are all represented as types of “insurance”—even though they often work quite differently from private insurance.

As shown above, insurance law concepts both rely upon, and inform, public conceptions of what insurance *is*. This means that attempts to characterize public health programs, or progressive redistribution, as types of “insurance” may backfire when they run up against insurance concepts like the non-responsibility requirement. Such concepts can motivate arguments, for example, for reducing government benefits to those who “are too lazy to get a job,” or whose illness is due to their own poor health choices, on the grounds that “insurance” properly-understood simply does not indemnify people against the effects of their own bad (in)actions. So long as we represent government programs as types of insurance, the immanent logic of insurance law will have an outsize influence on public policy debates.

This Article suggests that it is both possible and useful to study insurance law’s immanent structure and logic, because such internal architecture exists and is discoverable in the doctrine. Further work can be done—insurance law does not turn on the non-responsibility requirement alone. But insofar as gaining a better understanding of the non-responsibility requirement can help us to rationalize and justify the law that we have, and also to understand how to talk about “insurance” generally, it suggests that further study of the other internal structures of insurance law is an enterprise worth pursuing. This is true both for those who would aim to preserve insurance as it operates today, and those who would seek to reform it.