



# Contract Interpretation and The Parol Evidence Rule

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by Todd Green

**L**ast month we looked at the so-called fraud “exception” to the parol evidence rule. This month we look at the rule, itself, and how it is applied to interpret a contract when the meaning of the contract is in dispute. The parol evidence rule, codified in §1856, subdivision (a), of the California Code of Civil Procedure, provides: “Terms set forth in a writing intended by the parties as a final expression of their agreement with respect to such terms as are included therein may not be contradicted by evidence of any prior agreement or of a contemporaneous oral agreement.” Cal.Civ.Proc.Code §1856, subd. (a).

Thus, the parol evidence rule “generally prohibits the introduction of any extrinsic evidence, whether oral or written, to vary, alter or add to the terms of an integrated written instrument.” *Pacific State Bank v. Greene*, 110 Cal.App.4th 375, 378-79 (2003).

But extrinsic evidence *is* admissible to construe a written instrument when its language is ambiguous. See *Winet v. Price*, 4 Cal.App.4th 1159, 1165 (1992); Cal.Civ.Proc.Code §1856, subd. (g) (parol evidence admissible “to explain an extrinsic ambiguity or otherwise interpret the terms of the agreement”). The threshold question then is whether the language of

the written instrument is ambiguous. The Supreme Court of California has explained that, under California law, the test of whether extrinsic evidence is admissible to construe an ambiguity is not whether the language appears to the court to be unambiguous on its face, but “whether the offered evidence is relevant to prove a meaning to which the language of the instrument is reasonably susceptible.” *Pacific Gas & E. Co. v. G.W. Thomas Drayage & Rigging Co.*, 69 Cal.2d 33, 37 (1968).

The reason why—even when the language of the contract appears clear and unambiguous on its face—our courts consider extrinsic evidence to determine whether the language is ambiguous has to do with the objective of contract interpretation: The basic goal of contract interpretation is to give effect to the parties’ mutual intent at the time of contracting, so far as that intent is ascertainable. Cal.Civ.Code §1636. And while the language in a contract may appear clear on its face, its “clear” meaning still may not be what the parties intended. Because the source of contractual rights and duties is the intention of the parties, in interpreting a contract a court must ascertain that intention “by determining *what the parties meant* by the words they used.” *Pacific Gas & E. Co.*, 69 Cal.2d at 38 (emphasis added). For this reason, the Supreme Court has held that contract interpretation “requires at least a preliminary consideration of all credible evidence offered to prove the intention of the parties.” *Id.* at 39-40.

Thus, as the Court of Appeal explained in *Winet v. Price*: “The decision whether to admit parol evidence involves a two-step process. First, the court provisionally receives (without actually admitting) all credible evidence concerning the parties’ intentions to determine ‘ambiguity,’ i.e., whether the language is ‘reasonably susceptible’ to the interpretation urged by a party. If in light of the extrinsic evidence the court decides the language is ‘reasonably susceptible’ to the interpretation urged, the extrinsic evidence is then admitted to aid in the second step—interpreting the contract.” *Winet v. Price*, 4 Cal.App.4th at 1165.

## Step One: When and How Does the Court Provisionally Receive the Parol Evidence?

There is no case law that describes exactly when or how a court is supposed to provisionally receive the extrinsic evidence of a contract’s meaning (or, for that matter, how the court is to determine whether the evidence qualifies as “credible” evidence). But two procedures come to mind. If the issue of contract interpretation may be dispositive of the entire case or a cause of action, then a motion for summary judgment or summary adjudication would be an appropriate vehicle. The court can then consider all evidence proffered as to the interpretations urged by the parties and determine whether, in light of the proffered evidence, the language of the contract is reasonably susceptible to more than one meaning. If it is, then summary judgment must be denied because the resolution of the ambiguity presents a question of fact. See *Wolf v. Superior Court*, 114 Cal.App.4th 1343, 1351 (2004). If the court determines that the contract is unambiguous, then the court can interpret the agreement as a matter of law and, potentially, dispose of the case.

If, regardless of how the contract is interpreted, triable issues of fact will remain so that summary judgment is not available, then a motion *in limine* may be the appropriate mechanism to tee up the contract interpretation issue. The party who contends that the contract is unambiguous could move to exclude extrinsic evidence of any meaning contrary to the one the moving party advocates. The court can then provisionally receive the parol evidence and determine whether, in light of this evidence, the contract is ambiguous. If the court determines that the contract is unambiguous, it can instruct the jury as to its meaning (if a party so requests).

## Step Two: If the Court Admits the Parol Evidence, Who Determines What the Contract Means?

If, after considering the extrinsic evidence, the court determines that the contract is ambiguous, then the resolution of

this ambiguity becomes a question of fact for the ultimate finder of fact. *See Abifadel v. Cigna Ins. Co.*, 8 Cal.App.4th 145, 159 (1992). In a jury trial, this means that the jury rather than the judge will be tasked with interpreting the contract. This is the rule in most states. One notable exception is Georgia. In Georgia, if the contract is ambiguous, the court “must apply the rules of contract construction to resolve the ambiguity . . .” The issue of the meaning of the contract only goes to the jury “if the ambiguity remains after use of the construction rules. . . .” *Eckerd Corp. v. Alterman Properties, Ltd.*, 589 S.E.2d 660, 664-65 (Ga.App. 2003). I suspect that there are not many judges in Georgia who find themselves unable to resolve a contractual ambiguity after considering the extrinsic evidence and applying the rules of contract construction.

## **Appellate Review of Contract Interpretation When Parol Evidence is Considered**

The standard for appellate review of questions of contract interpretation will depend on whether or not parol evidence was admitted to aid in the interpretation. The trial court’s ruling on the threshold question of ambiguity (*i.e.*, whether the proffered evidence is relevant to prove a meaning to which the language of the contract is reasonably susceptible) is a question of law and is subject to independent review. *See Winet*, 4 Cal.App.4th at 1165. The trial court’s resolution of an ambiguity is also a question of law if no parol evidence is admitted or if the parol evidence is not in conflict. But where the parol evidence is in conflict, the trial court’s resolution of that conflict is a question of fact and must be upheld if supported by substantial evidence. *See id.* at 1166; *see also Wolf v. Superior Court*, 114 Cal.App.4th 1343, 1351 (2004).

Of course, to obtain appellate review of a question of contract interpretation, you will need to know how the trier of fact interpreted the contract. In a jury trial for breach of contract, you will not know how the jury interpreted the contract if the jury renders a general verdict. In a general verdict, the jury simply renders a decision in favor of one party or the other without

articulating its factual findings. In a special verdict, the jury presents its conclusions of fact. *See Cal.Civ.Proc.Code §624*. Thus, to preserve the issue of contract interpretation for appeal, the party desiring to do so should request a special verdict form in which the jury states how it interpreted the disputed contractual provision. Similarly, in a bench trial, the party seeking to preserve the issue for appeal should request a statement of decision and should specify that the contract interpretation issue be addressed in the statement of decision. *See Cal.Civ.Proc.Code §632*.



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