

INVALIDATING AUTO INSURANCE PROVISIONS IN MONTANA

In last month's column, as part of a discussion of application of Montana law to out-of-state auto policies, I pointed out some of the consumer-friendly cases that exist in Montana. Two attorneys subsequently told me they were pleased to discover in that column, cases that invalidated insurance provisions with which they had been wrestling on behalf of their claimants. Consequently, I thought this month it might be beneficial to review cases in which the Montana Supreme Court has invalidated or limited provisions of the standard auto policies. By reason of space limitations, I cannot refer to all cases construing auto policies in Montana but will try to mention significant cases of invalidation of auto insurance clauses.

Generally, the court has invalidated auto insurance provisions on one of three grounds: First, if the provision causes an auto liability policy to violate Montana's Mandatory Liability Protection Act, MCA 61-6-301 to 61-6-304, either in coverage or amounts, it may be voided. Second, the court will declare a provision invalid if it violates the Uninsured Motorist statute, MCA 33-23-201. Third, a provision may be declared invalid if the court determines that it violates the insured customer's reasonable expectations about the policy promises.

Provisions declared invalid on ground of public policy as stated in the Mandatory Liability Protection Act.

The Mandatory Liability Protection Act requires owners of motor vehicles "registered and operated" in Montana to insure against loss from liability "caused by maintenance or use of a motor vehicle" (the vehicle must be insured in amounts set forth in the Motor Vehicle Safety Responsibility Act, MCA 61-6-103 to 151 which is referenced in the Mandatory Liability Protection Act). The requirement to insure liability arising out of "maintenance or use" is very broad. If the claimant who is not the cause of his or her own injury has been injured through "maintenance or use" of an automobile, and the insurer of the automobile contends that the injury is excepted from coverage by reason of some exclusion, limitation, offset, or condition of the policy, claimant's counsel should immediately assess the import of the provision to determine whether it violates public policy as expressed in the act. The question is, does the provision result in the policy containing less coverage or limits than required by the Mandatory Liability Protection Act? The Montana Supreme Court has repeatedly invalidated provisions that do. Consider these examples:

In *Transamerica Ins. Co. v. Royle*, 202 Mont. 173, 656 P.2d 820 (1983), the court declared invalid the "family" exclusion that blocked liability coverage from providing benefits to a member of the family living in the same household. The clause is invalid as applied to a policy obtained under the Mandatory Liability Insurance Act since the act requires coverage "against loss... suffered by any person" and contains no exception for family members residing under the same roof. However, in *Shook v. State Farm*, 872 F.Supp 768 (1994), Federal District Judge Hatfield held that a household exclusion that limits a family member's recovery to the minimum liability limits is not void as against public policy in Montana. (Note, however, that Judge Hatfield, in that decision, found State Farm's clause invalid because it defeated the "reasonable expectations" of the insured.) In *Stutzman v. Safeco Ins. Co.*, 284 Mont. 372, 945 P.2d 32 (1997), the Montana Supreme Court upheld a family exclusion in underinsured motorist coverage, citing the fact that UIM coverage is not statutorily mandated.

In *Allstate Ins. Co. v. Hankinson*, 244 Mont. 1, 795 P.2d 480 (1990), the "with the owner's permission" language that qualified the coverage if the insured drove non-owned autos was struck as being contrary to public policy because it excluded coverage mandated by the statute. Theoretically, even a thief's auto insurance should cover him while he is fleeing in a stolen ("non-owned") car.

Safeco's "employee" exclusion blocking auto liability coverage for "bodily injury to an employee of any insured person arising in the course of employment" was declared invalid for depriving employees of coverage even where they brought the claim against a third-party insured who was not their employer. An employee exclusion may validly block coverage on a claim against the employer that is covered by work comp. The broader exclusion violates the mandatory coverage requirement of MCA 61-6-301. *Fire Ins. Exchange v. Tibi, Kayser and Allstate*, 21 MFR 162 (Hatfield 1996).

The court held that an insurer could not exclude liability coverage for an auto dealer's customer who is driving a "loaner" in *Bill Atkin Volkswagen, Inc. v. McClafferty*, 213 Mont. 99, 689 P.2d 1237 (1984). Again, the statute applies to all vehicles "registered and operated" and makes no exception for an owner who is an auto dealer providing "loaner" vehicles.

In *Iowa Mut. Ins. Co. v. Davis*, 231 Mont. 166, 752 P.2d 166 (1988), the court held that a "named driver" exclusion was invalid since MCA 61-6-301 prohibited the exclusion of named drivers from statutory minimum coverage under a motor vehicle liability policy. The insured and insurer could not agree to exclude a named family member as an insured driver. However, the 1989 legislature, reacting to *Davis* amended MCA 61-6-301 adding subsection (1)(b) to allow the parties to the insurance contract to exclude a named family member from insurance.

Provisions declared invalid on ground of public policy as stated in the Uninsured Motorist statute.

The second general ground for invalidation of auto insurance clauses in Montana is the Uninsured Motorist Statute, MCA 33-23-201. That statute requires that any motor vehicle liability policy offered in Montana must contain coverage in the amounts specified in the Motor Vehicle Safety Responsibility Act, protecting persons insured from damages arising out of the operation or use of uninsured motor vehicles. While the statute gives the named insured the right to reject the coverage, the Montana Supreme Court has treated UM coverage as a mandatory or “compulsory coverage” and has tested UM auto insurance provisions against the statute just as they have with the Mandatory Liability Protection Act. The test of validity of a provision excluding or limiting UM coverage in the face of MCA 33-23-201 is: Does the exclusion or limitation give less coverage for acts of the uninsured driver than the insured driver? Hence, if a provision results in UM coverage or limits less than those statutorily required, it may be invalidated. Consider the following cases:

The court ruled invalid a policy clause which requires, as a precondition to coverage, that there be physical contact between insured’s car and the uninsured motorist’s car, since such a requirement is in derogation of MCA 33-23-201 which contains no such precondition. *McGlynn v. Safeco Ins. Co.*, 216 Mont.379, 701 P.2d 735 (1985). *See also, Palmer by Diacon v. Farmers Ins. Exch.*, 233 Mont. 515, 761 P.2d 401 (1988).

The court held that an insurer cannot limit UM coverage to cases where the injured person is “occupying” the insured auto, since that violates the public policy behind MCA 33-23-201 of protecting all insureds against injury by uninsured motorists. *Jacobson v. Implement Dealers Mut. Ins. Co.*, 196 Mont. 542, 640 P.2d 908 (1982). Note however, that the court in *Chilberg v. Rose and Mid Century*, 273 Mont. 414, 903 P.2d 1377 (1995) held that the insured occupant could only recover one of three UM policy coverages because they were payable to an insured who “occupied” the insured auto, and the court said he could only occupy (and therefore be an insured in) one car at a time. (The court distinguished *Seyers* where the claimant fit the definition of “insured” under each policy without being an occupant.)

In *Sullivan v. Doe*, 159 Mont. 50, 495 P.2d 193 (1972), the court struck, as violating the legislative intent of the uninsured motorist statute (now MCA 33-23-201), the “workers’ compensation offset,” a policy provision that reduced the UM benefit where the injured insured received workers compensation benefits. The offset could have reduced the UM limit below the \$10,000 then required by the UM statute.

In *Guiberson v. Hartford Cas. Ins. Co.*, 217 Mont. 279, 704 P.2d 68 (1985), the court voided a clause whose import was to exclude UM coverage where the driver had no permission to use the vehicle. The court held the clause void as against public policy. (Tintinger, an escaped mental patient, stole a beer distributor’s truck and injured its driver, Guiberson, who was riding on it trying to get Tintinger to stop.)

The court held, in *Oleson v. Farmers Ins. Group*, 185 Mont. 164, 605 P.2d 166 (1980), that an auto tortfeasor’s policy that has limits of liability less than the amounts specified in the “financial responsibility statutes” of the state is not an “auto liability policy” that voids UM coverage. Hence, a vehicle with a \$20,000 BI limit would be an “uninsured motor vehicle.”

The court invalidated an offset provision by which Nationwide purported to reduce its UM/UIM coverage by any amount paid by or for any liable parties. *Grier v. Nationwide Mutual Insurance Company*, 248 Mont. 457, 812 P.2d 347 (1991). Grier’s Nationwide policy contained Uninsured Motorist coverage which included an underinsured motor vehicle in the definition of uninsured. Hence, underinsured coverage was part of the uninsured coverage section and there was no separate underinsured coverage. The court invalidated the offset, because its import was to reduce UM coverage below that required by the UM statute in Montana.

The “no consent to settlement” clause that prohibits the insured from settling with the tortfeasor without permission of the insured’s UM carrier was invalidated in *State Farm Mut. Automobile Ins. Co. v. Taylor*, 223 Mont. 215, 725 P.2d 821 (1986) because it prevented the insured from enforcing the contractual promise of UM coverage.

Dagel v. Farmers Ins. Group, 273 Mont. 402, 903 P.2d 1359 (1995) held that you don’t have to exhaust the occupied auto UM coverage to make a claim on the passenger’s own UM coverage (or the permissive user’s UM coverage) since the statutory contingency of “not insured by a bodily injury liability bond or policy” is met.

In the 1979 stacking case of *Chaffee v. United States Fidelity & Guaranty Co.*, 181 Mont. 1, 591 P.2d 1102, the court held that it was against public policy for a limit of liability clause to restrict recovery to one UM policy limit where there were three vehicles insured for three premiums under one policy since they should be treated the same as if they were insured under three policies. In reaction, the legislature in 1981 enacted MCA 33-23-203 which blocked stacking of coverages for multiple cars under a single policy but not for multiple cars under separate policies. (Effective May 2, 1997, that statute was amended with intent to block all stacking for policies taking effect after that date.)

Provisions declared invalid on ground of defeating insurance consumer’s reasonable expectations

Invalidation of coverage provisions for violating the Mandatory Liability Protection Act and the Uninsured Motorist Act only occurs for the mandatory or compulsory Bodily Injury Liability coverages and Uninsured Motorist coverage. Note that Medical Pay coverage and Underinsured motorist coverage have no statutory protection. However, if the UIM coverage is actually just a definition existing under the UM coverage, then the court will protect the UIM benefit as being compulsory UM

coverage. See, *Grier v. Nationwide*, above. The lack of statutory protection for Medical Pay coverage and Underinsured Motorist coverage brings us the third major reason for court invalidation of auto insurance provisions, the doctrine of the consumer's "reasonable expectations." If a consumer, considering a policy's language, format, and organization would have a reasonable expectation that the contract provided a benefit, then the court will honor that benefit.

Though the court voided the family exclusion in *Transamerica Ins. Co. v. Royle*, above, on grounds that it violated the Mandatory Liability Protection Act, the justices also held "that the household exclusion clause is invalid due to its failure to 'honor the reasonable expectations' of the purchaser of the policy." However, in *Stutzman v. Safeco Ins. Co.*, above, the court found Safeco's household exclusion in the UIM coverage was not ambiguous and didn't defeat reasonable expectations of the insured. On the other hand, in *Leibrand v. National Farmers Union*, 272 Mont. 1, 898 P.2d 1220 (1995), the court declared invalid family exclusion clauses limiting recovery to "limits of liability required by law" or to "the financial limits of the policy state" as being ambiguous.

In *Shook v. State Farm*, 872 F.Supp 768 (D. Mont. 1994), the federal court (Hatfield) found that State Farm's "family exclusion" clause limiting family member recovery to the minimum liability limit was ambiguous because of its policy placement and held that it defeated "reasonable expectations" of the insured so as to be unenforceable.

In *Farmers Alliance Mutual v. Holeman*, 278 Mont. 274, 924 P.2d 1315 (1996), the court invalidated the anti-stacking provisions of the Medical Pay and Underinsured Motorist Coverages (optional coverages) where separate premiums are charged for multiple vehicles under a single policy. The court held that MCA 33-23-203 does not prohibit stacking in those situations. (Senate Bills 266 and 44, 1997 Mont. Legislature, both amended MCA 33-23-203 with intent to prohibit stacking of any auto casualty coverage. The statute refers now to "each part of the policy" and applies regardless of "the number of policies issued by the same company covering the insured, or the number of separate premiums paid." SB 44 effective May 2, 1977, for policies taking effect after that date. This overrides the stacking in *Farmers Alliance Mutual v. Holeman*.)

In *Bennett v. State Farm*, 261 Mont. 386, 826 P.2d 1146 (1993), the court invalidated State Farm's anti-stacking "other insurance" provisions for UIM coverages for automobiles declared under the same policy with separate premiums. The court said the fact that UIM is not statutorily required was irrelevant because the same public policy considerations existed under the reasonable expectations doctrine. The court said: "Montana citizens should have a reasonable expectation that when they purchase separate policies for underinsured motorist coverage, they will receive adequate compensation for losses caused by an underinsured motorist, up to the aggregate limits of the policies they have purchased." (This was on certification from the Ninth Circuit which was reviewing Judge Hatfield's decision at 758 F.Supp.1388 [1991] in which he came to the same conclusion.) Again, for policies effective after April 2, 1997, stacking is now blocked by the amended MCA 33-23-203.

The court, in *Ruckdaschel v. State Farm*, 285 Mont. 395, 948 P.2d 700 (1997), invalidated contractual anti-stacking provisions that applied to medical coverage on the ground that the public policy against anti-stacking provisions was the same for optional as it was for mandatory coverages.

In *Augustine, Augustine and Gray v. Simonson and Farmers Ins. Exchange*, 283 Mont. 259, 940 P.2d 116 (1997), the court said: "The provision requiring that the tortfeasor's liability insurance be entirely exhausted as a prerequisite to securing indemnification from the Underinsured Motorist coverage is contrary to Montana public policy and unenforceable to the extent that it violates public policy." (Public policy to encourage settlement and avoid unnecessary litigation.) The decision cited *Sorenson, above*, for the proposition that UIM coverage may not be voided on technicalities. *Augustine* lays out the procedure for calculating Underinsured Motorist Coverage where there is potential recovery from a third party tortfeasor.

Provisions Declared Invalid on Other Public Policy Grounds

In *Sorenson v. Farmers Insurance Exchange*, 279 Mont. 291, 927 P.2d 1002 (1996), the court adopted a "no prejudice" rule that, absent some showing of material prejudice to the underinsurance carrier, a claim for Underinsured Motorist coverage may not be precluded on the technicality that the insured released the tortfeasor and destroyed the insurer's right of subrogation. Farmers contended that the release destroyed their right of subrogation. The court noted absence of prejudice from destruction of the subrogation right where the tortfeasor is judgment proof. Hence, the insured may recover on an Underinsured Motorist claim after releasing the tortfeasor without the insurer's permission, if the tortfeasor is judgment proof.

The court declared the subrogation clause as applied to automobile Medical Pay coverage invalid as an assignment of a personal injury chose in action in *Allstate Ins. Co. v. Reitler*, 192 Mont. 351, 628 P.2d 667 (1981). See also, *Youngblood v. American States Insurance Co.*, 262 Mont. 391, 866 P.2d 203 (1993) for the same holding. The *Reitler* holding was limited to auto Medical Pay. Subrogation to recover UM coverage has been approved. *Farmers Ins. Exch. v. Christenson*, 211 Mont. 250, 683 P.2d 1319 (1984).

The court limited application of the subrogation clause to those situations in which the insured has recovered the insured's entire loss plus costs including attorney fees, before the insurer can subrogate. *Skaug v. Mountain States Tel. & Tel. Co.*, 172 Mont. 521, 565 P.2d 628 (1977) and *DeTienne Associates v. Farmers Union Mut. Ins. Co.*, 266 Mont. 184, 879 P.2d 704

(1994). The theory is that if a party must bear the loss, it should be the insurer, since that is the risk the insured paid the insurer to assume.

The court invalidated the subrogation clause as applied to the insurer's own insured and any additional insured under the policy in *Truck Ins. Exch. V. Transport Indem. Co.*, 180 Mont. 419, 591 P.2d 188 (1979).

In *Bill Atkin Volkswagen, Inc. v. McClafferty*, 213 Mont. 99, 689 P.2d 1237 (1984), the court declared excess clauses to be mutually repugnant where both policies claimed to be excess and held each liable for a pro rata share of the loss apportioned in ratio of the limit of each to the total limit of available coverage. (The fact that the coverage is required by the Financial Responsibility Act or the Mandatory Liability Act does not mean it must be primary as long as there is adequate coverage.)

Conclusion

The list of auto insurance policy provisions invalidated by the Montana Supreme Court is extensive and confirms the court's commitment to test insurance provisions to ensure that they comport with public policy. Consumer counsel needs to know the public policy bases underlying the insurance code and to understand when a provision's effect violates those public policies. In that manner, counsel can protect Montana claimants and insureds from the unfairness of unlawful exclusions, limitations, offsets, or conditions.