

INVALIDATING THE FAMILY OR HOUSEHOLD EXCLUSION IN AUTO INSURANCE

In the Autumn 2000 issue, I wrote an article entitled “The ‘Household’ or ‘Family’ Exclusion in Auto Policies.” In it, I examined the state of the law in Montana with regard to those auto insurance provisions that exclude from coverage or benefit a class of victims solely because they are members of the named insured’s family or household. I noted that in *Transamerica Ins. Co. v. Royle*,¹ Montana invalidated the household exclusion insofar as it infringed the minimum limits of liability coverage required by the Mandatory Liability Protection Act, MCA §61-6-301. Because the Act required the liability policy to protect against bodily injury and property damage to “any person,” the “household exclusion” was invalid. I noted that the federal court in *Shook v. State Farm Mut. Ins.*,² had then found a household exclusion for liability coverage in excess of the minimum mandatory limits invalid for violating the reasonable expectations doctrine. I asserted that the Montana Supreme Court, in the companion cases of *Liebrand v. National Farmers Union Property and Casualty Co.* and *Cole v. Truck Ins. Exchange*,³ found the family exclusions in each of the insurer’s policies ambiguous. In doing so, the justices prospectively indicated serious reservations about the conscionability of family exclusions as applied to amounts over the minimum mandatory liability limits in the future, even if the exclusions were clearly written. Finally, I reported that the Montana Court, in *Stutzman v. Safeco Ins. Co.*,⁴ refused to invalidate the family exclusion as applied to UIM coverage, reasoning that UIM was not required or protected by statute in Montana.

Subsequently, lawyer feedback at the well-attended January MTLA Insurance Seminar in Bozeman, made clear that the family exclusion has become a major impediment to efforts of plaintiffs’ counsel to secure adequate compensation for victims to the point that it almost rivals the anti-stacking statute, MCA §33-23-203. Everyone seems to have clients who are being deprived of auto insurance benefits by the family exclusion. Often, it is the family member injured by the uninsured or underinsured motorist who can’t recover the family UM or UIM coverage, while a non-family member riding in the same car gets compensated. The more we traded stories about the family exclusion, the more I realized just how preposterous it is.

The Idaho Supreme Court, in *Farmers Ins. Group v. Reed*,⁵ illustrated its arbitrariness with a scenario in which a family is riding in a car negligently driven by the father and involved in an accident. The family exclusion defeats coverage for family members in the car no matter how seriously they are injured, while friends or relatives in the same car can recover. If a son, home from college for a visit, takes over the driving, family members are “cloaked with coverage.” However, if the mother or sister take over at a rest stop, the family again loses coverage. If a family friend “slips behind the wheel,” the coverage reappears. If a neighbor next door is driving behind with children from each family intermingled in the cars, and the cars are both involved in a collision, only those children or spouses who are not in a car with an immediate family member at the wheel will be compensated.

Consider then, the following apparent truths:

- 1 Insurance consumers buy auto insurance coverage such as Bodily Injury Liability, Medical Pay, Uninsured Motorist, and Underinsured Motorist primarily to protect themselves and their family members.
- 2 The passenger who will be injured in your car is most likely going to be a family member. (The average American family makes thirteen auto trips per day from home now.)
- 3 By inserting the family or household exclusion in Liability Coverage, Medical Pay Coverage, Uninsured Motorist Coverage, and Underinsured Motorist Coverage, the auto insurance industry is excluding from benefits the entire class of persons the auto insurance consumers most sought to protect.
- 4 Unlike exclusions for people who ride ATVs and motorcycles, this is not a risk-based exclusion, because it applies to a class of victims not drivers, and those victims present no more risk than any other auto victim insureds. It is simply an arbitrary exclusion of a large number of victims for the purpose of collecting premiums without paying losses.
- 5 The only thing family members could do to avoid the exclusion and the risk of being uninsured is to refuse to ride with family members and refuse to drive family members’ cars.

When the Montana Supreme Court abrogated the parental immunity doctrine in tort law in *Transamerica v. Royle*, it cited “the growing judicial distaste for a rule of law which in one sweep disqualified an entire class of

injured minors.”⁶ As the following cases show, there may be a growing judicial distaste for an insurance contract provision that disqualifies an entire class of injured family members from auto insurance benefits.⁷

Forms in which the family or household exclusion will appear.

In Bodily Injury Liability Coverage: After many states invalidated family exclusions in Bodily Injury Liability coverage for violating mandatory liability insurance laws, the insurers began using a modified provision excluding coverage for claims by family members in amounts over the statutory minimum prescribed by the Mandatory Liability Protection Act.⁸ For example, State Farm’s policy provides:⁹

There is no coverage: * * * 2. For any *Bodily Injury* to: ... (c) *any insured* or any member of *an insured’s* family residing in the *insured’s* household to the extent the limits of liability of this policy exceed the limits of liability required by law.

Allstate’s policy excludes from the basic insuring agreement for Bodily Injury coverage:¹⁰
bodily injury to any person related to an insured person by blood, marriage or adoption and residing in that person’s household, to the extent that the limits of liability for this coverage exceeds the limits of liability required by the [name of state] Financial Responsibility law.

The exclusion may also occur in the form of a “named insured exclusion” which is similar to a family or household exclusion, because it defeats liability coverage for the “named insureds” who will invariably be family members such as the husband, wife, daughter or son named as insured drivers. State Farm’s “named insured exclusion” in the 9th Circuit case of *State Farm v. Falness*¹¹ provided: “There is no coverage... for any bodily injury to: . . . you.” The policy there defined “You” as “the named insured or named insureds shown on the declarations page.”

In Uninsured Motorist Coverage: In the UM coverage, family owned vehicles may be excluded from the definition of uninsured motor vehicle as follows:¹²

However, “uninsured motor vehicle” does not include any vehicle or equipment:

1. Owned by or furnished for the regular use of you or any “family member.”

In addition, in UM coverage the family exclusion will often appear in the form of the “family owned vehicle exclusion” which will provide:¹³

A. We do not provide Uninsured Motorist Coverage for “bodily injury” sustained:

1. By an “insured” while “occupying,” or when struck by, any motor vehicle owned by or furnished for the regular use of that “insured” which is not insured for this coverage under this policy. This includes a trailer of any type used with that vehicle.
2. By any “family member” while “occupying,” or when struck by, any motor vehicle you own which is insured for this coverage on a primary basis under any other policy.

In Underinsured Motorist Coverage: The policy will commonly define an underinsured motor vehicle and then, as in Liberty Mutual’s policy,¹⁴ exclude from the definition any automobile:

1. Owned by or furnished or available for the regular use of you or any family member unless the covered person was neither operating nor occupying such vehicle at the time of the accident.

* * *

5. To which the liability coverage of this policy applies.

The first clause, “1.” above, known as the “Family Car Exclusion,”¹⁵ is insidious for two reasons. First, attorneys may not recognize that it is in essence a family exclusion. Secondly, it has a certain logic to it insofar as attorneys examining it for validity may believe the insurer’s justification that it is simply trying to keep from having its insurance coverage extended to uninsured family vehicles for which the insurer receives no premium. The problem with that justification is that coverages such as Med Pay, UIM, and UM are individual and portable to the insured and not tied to the vehicle as will be discussed later.

For UIM, the carriers will also include family exclusions identical in form to those quoted above in A. 1. and 2. in the Uninsured Motorist coverage.¹⁶

In Medical Pay Coverage:

In Medical Pay coverage, an exclusion from the basic coverage will likely read:¹⁷

We do not provide Medical Payments Coverage for any “insured” for “bodily injury”:

* * *

5. Sustained while “occupying,” or when struck by, any vehicle (other than “your covered auto”) which is:
 - a. Owned by you; or
 - b. Furnished or available for your regular use.
6. Sustained while “occupying,” or when struck by, any vehicle (other than “your covered auto”) which is:
 - a. Owned by any “family member”; or
 - b. Furnished or available for the regular use of any “family member.”

As you can see, the family exclusion can appear in multiple guises in every coverage making a profound difference in the benefits available to family members as opposed to non-family members.

Social considerations that should affect public policy regarding family exclusions.

Who would argue that auto insurance consumers buy insurance, particularly the portable coverages of Medical Pay, Uninsured Motorist, and Underinsured Motorist, for any other reason than protection of themselves and their families. As the Missouri court said in *Husch v. Nationwide Mut. Fire Ins. Co.*,¹⁸ “When purchasing uninsured motorist coverage, policyholders are primarily concerned with protecting themselves, their spouses, and their minor children, i.e., the natural family unit. Minor children are unable to insure themselves and thus provide financial protection against disabling injuries.” The Kentucky Supreme Court in *Lewis v. West American Ins. Co.*,¹⁹ said:

Consumers purchase liability insurance coverage in excess of the mandatory amounts required by law out of a sense of personal, financial and social responsibility. By purchasing higher liability insurance limits, the insured provides a method to compensate those injured as a result of the insured’s negligence without endangering the financial security earned by years of hard work. Purchasers of automobile insurance expect their family members to receive comparable protection to that afforded to unknown third persons. Family exclusions defeat these goals and render liability insurance coverage illusory for those persons the insured most desires to protect, who are also the persons most likely to be passengers in the insured’s vehicle, the insured’s loved ones.

The weak justifications for the family exclusion after abrogation of intra-family tort immunity.

It is ironic that one of the principle reasons the courts abrogated the intra-family immunity doctrines was the existence of insurance. The Montana Supreme Court in abrogating parental immunity in *Transamerica v. Royle*²⁰ said, “The principle reason relied on by the courts for allowing an action by a child against their parent in an automobile accident case is the prevalence of automobile liability insurance.” The court noted, “The existence of liability insurance prevents family discord and depletion of family assets in automobile negligence cases.” And, in *Miller v. Fallon County*,²¹ the court found, “Family harmony is even less of a concern because of insurance. A spouse is normally not seeking redress against the other spouse, but rather spouse’s insurance carrier.”

The court in *Miller v. Fallon County* rejected promotion of family harmony and discouraging fraud and collusion as the historical reasons for retaining intra-family tort immunity. Courts found it “unreasonable to eliminate causes of action of an entire class of persons simply because some undefined portion of the designated class may file fraudulent lawsuits.”²² However, as the guest statutes, interspousal immunity, and parental immunity tort doctrines were rejected, the insurers simply inserted the family exclusions into their policies to defeat the result.²³ In *Lewis v. West American Ins. Co.*, the Supreme Court of Kentucky, was asked to apply the modified family exclusion to deny liability coverage over the mandatory minimum \$25,000 to a nine-year-old girl who had been brain damaged. She was a passenger when a car driven by her mother collided with a tractor-trailer. The court invalidated the family exclusion outright, noting that, just as fraud and collusion had not justified the guest statutes

and family immunity tort statutes, they did not justify the family exclusion in auto liability policies. The reasoning in *Lewis* is so compelling that it deserves quoting at length:

As a result, an insurance policy containing such a clause prevents a specific class of innocent victims from receiving adequate financial protection. This exclusion is entirely based upon the person's status as a member of the named insured's family. Without documentation or factual basis, every member of this excluded class is labeled high risk and branded as being more likely to engage in collusion and fraud.

The *Lewis* court quoted the Washington Supreme Court reasoning in *Mutual of Enumclaw Ins. Co. v. Wiscomb*.²⁴

This exclusion becomes particularly disturbing when viewed in light of the fact that this class of victims is the one most frequently exposed to the potential negligence of the named insured. Typical family relations require family members to ride together on the way to work, church, school, social functions, or family outings. Consequently, there is no practical method by which the class of persons excluded from protection by this provision may conform their activities so as to avoid exposure to the risk of riding with someone who, as to them, is uninsured.

The Kentucky court cited three examples illustrating the inequities inherent in the family exclusion.²⁵ First, where a parent carpools to take neighborhood children to school, social, or recreational events, in the event of serious accident, the neighbor children can receive full compensation for bodily injury while the driver's children are limited to the mandatory minimum regardless of severity of their injury. Second, when two married couples drive together, the driver's spouse is limited to the minimum coverage, while the friends receive the full benefit. What's more, if one of the friends drives the car, their spouse has full coverage while the owner's spouse is still limited to the minimum. Third, in the commonplace situation where two families drive to an agreed destination with children from both families intermingled in the cars, the children riding with their neighbor are the only ones who receive full coverage. (Keep in mind, in these examples, that the car owner/driver's primary reason for buying insurance was for the protection of his or her own family.)

The court went on to say:²⁶

Many of the people denied insurance coverage are innocent children who have no say about the vehicle in which they are placed, who drives the vehicle, or the manner in which the vehicle is driven. Furthermore, because of their tender years, in many cases they are incapable of fraud or collusion. Despite these considerations, family exclusion clauses deny them the full protection provided by insurance policies.

The policies being contracts of adhesion, the consumers have no choice and may not avoid being exposed to the risk of riding with a family member who is, as to them, uninsured or underinsured while being fully insured as to neighbors and strangers.

Invalidating the family exclusion in the liability coverage.

Montana's *Transamerica v. Royle* case is representative of a host of appellate court decisions that voided the family exclusion insofar as it deprived family members of liability coverage in violation of state mandatory liability protection acts or financial responsibility acts. The Washington court, in *Tissel v. Liberty Mut. Ins. Co.*,²⁷ reasoned that Washington's Financial Responsibility Act stated "a public policy in favor of full compensation for accident victims." The Montana Supreme Court, in *Bennett v. State Farm*, recognized a similar public policy that "favors adequate compensation for accident victims,"²⁸ though the public policy is not based in a statute. In declaring family member exclusions invalid as against public policy, The Washington court in the *Tissell* case said:

The family or household exclusion clause strikes at the heart of this public policy. This clause prevents a specific class of innocent victims, those persons related to and living with the negligent driver, from receiving financial protection under an insurance policy containing such a clause. In essence, this clause excludes from protection an entire class of innocent victims for no good reason.²⁹

After *Royle* in Montana, the question was whether a family exclusion for amounts in excess of mandatory statutory minimum liability limits was valid. Unfortunately for insureds, the court, in *Iowa Mut. Ins. Co. v. Davis*,³⁰ while invalidating a named driver exclusion for violating the minimum limits for mandatory liability, said in the process:

Our ruling does not, however, prohibit an insurer from entering into agreements with their insureds to limit coverage to the statutory minimum amounts as set forth in §61-6-103, MCA. Other states have reached similar conclusions.

Accordingly, auto insurers inserted a modified family exclusion of the type set out above into their liability coverage. Some courts that have ruled the family exclusion invalid for violating statutory minimums have also found the exclusion valid for amounts over the statutory minimums. For example, in *Gabriel v. Shelter Mut. Ins. Co.*,³¹ a Missouri court noted that the Motor Vehicle Financial Responsibility Law in that state permitted coverage in excess of the minimums and provided that “such excess or additional coverage shall not be subject to the provisions of this chapter.” Montana’s Motor Vehicle Safety Responsibility Act, MCA §61-6-103(8), contains the identical quoted language. Because the Montana Mandatory Liability Act references the Financial Responsibility Act for the minimum dollar limits, and the Financial Responsibility Act contains the quoted language, it is hard to argue that the Acts invalidate the family exclusion for amounts over the minimums.³² Nevertheless, family exclusions for amounts of liability coverage over statutory minimums should not be considered valid.

In *American Family Mut. Ins. Co. v. Livengood*,³³ Nancy Henninger was driving the car of her boyfriend, Arthur Frehse, with whom she lived when she injured Livengoods who were riding a motorcycle. Her auto insurer, American, refused liability coverage under her own policy citing the “nonowned automobile exclusion,” while paying Livengoods the limits of her boyfriend’s separate liability policy with the company. Normally, where the non-owner driver and the auto are separately insured, both liability policies are applied as primary and excess coverages of the victim’s damages. However, in *Livengood*, the insurer used the exclusion to void Henninger’s own coverage completely. The court reasoned that it was permissible to preclude coverage while she drove other cars than her own as opposed to precluding coverage for injuries to certain persons as was the case in *Royle*. The natural implication is that exclusions precluding coverage of certain victims as opposed to driving of certain vehicles is invalid. Other courts have agreed with the principle that exclusions regarding conduct, i.e., driving non-owned vehicles, may relate to risk and be valid, while exclusions based on a certain class of victims don’t relate to risk and may be invalid.

Invalidating the family exclusion in Uninsured Motorist Coverage.

Montana’s Uninsured Motorist statute, MCA §33-23-201, provides that any auto liability policy in this state must provide coverage “for the protection of persons insured thereunder who are legally entitled to recover damages from owners or operators of uninsured motor vehicles” because of injury or death “caused by an accident arising out of the operation or use of such vehicle.” The court, in *Dagel v. Farmers Ins. Group*,³⁴ said the statute’s basic purpose is to provide protection for the UM policyholder against risk of inadequate compensation for injuries or death caused by negligence of a financially irresponsible motorist. In *Sullivan v. Doe*,³⁵ the court said the mandate of the UM statute is to place the injured policyholder in the same position he would have been in if the uninsured motorist had liability insurance. Moreover, the court in *Jacobson v. Implement Dealers Mut. Ins. Co.*,³⁶ held that the statute covers the insured regardless of whether he occupies the insured vehicle. As the North Carolina court in *Bray v. North Carolina Farm Bureau Mut. Ins. Co.*³⁷ explained, the member of such a class of family member insureds, is entitled to UM benefits under the statute, “whether she was struck by an uninsured motor vehicle while riding in an insured vehicle, or on a motorcycle, or just walking down the street.”³⁸ In *Bradley v. Mid-Century Ins. Co.*,³⁹ the Michigan court said of the UM insureds, “They are insured when injured in an owned vehicle named in the policy, in an owned vehicle not named in the policy, in an unowned vehicle, on a motorcycle, on a bicycle, whether afoot or on horseback or even on a pogo stick.” Under the auto policies, the family member is invariably included in the definition of “insured” and, hence, entitled to UM coverage even if on the pogo stick.

However, using the family-owned vehicle exclusion, the insurer attempts to make an exception excluding coverage when the family member is occupying a vehicle owned by a member of the same household which is not a “covered auto.” No such exception exists in the statute, just as the Mandatory Liability Protection Act contained no exception excluding liability coverage for family members. As the court said in *Bray*, the statute is “people-oriented,” and the exclusion is “vehicle-oriented” and “repugnant to the statute and ineffective to limit the UM coverage in this case.”⁴⁰ The exclusion is invalid for UM coverage because it reduces the scope of coverage required by the statutory mandate. The court in *Jacobson* said, “The policy behind the statute [the Montana UM statute] is to protect the policyholders from uninsured motorists in all instances.” *Jacobson* held such reductions to violate public policy. Furthermore, the court there found the premiums in UM coverage are not risk-related but “flat-rate” where coverage is available to everyone at the same rate. The UM coverage is personal and portable and does not depend on the nature of the space the insured occupies when injured by the uninsured motorist.

Nor should the family exclusion be valid for UM coverage in excess of the statutory minimum. In the Missouri case of *Gulf Ins. Co. v. American Family Mut. Ins. Co.*,⁴¹ Holly Knox, a child, was injured by an uninsured motorist while she rode in a car belonging to her 18-year-old sister. She was an “insured” for UM purposes, being a “relative” of her father who was the named insured. However, the UM coverage excluded bodily injury to a person “While occupying, or when struck by, a motor vehicle that is not insured under this Part, if it is owned by you or any resident of your household.” American refused to pay any of its \$100,000 UM benefits. The court found the exclusion to be contrary to the reasonable expectation of the insureds and voided it for all amounts. (See the section below on invalidating the family exclusion for defeating the reasonable expectations of the insured.)

Invalidating the family exclusion in the Underinsured Motorist Coverage.

The “Family Car Exclusion” which excludes any family owned vehicle from being considered an underinsured motor vehicle has been held valid when applied to prevent the claimant from recovering under both the Bodily Injury Liability Coverage and the Underinsured Motorist Coverage under a single auto policy.⁴² In such situations, the courts reason that permitting such recovery allows the insured to convert cheap UIM coverage into more expensive BI Liability Coverage.⁴³ However, the Minnesota Supreme Court,⁴⁴ established the *Sarvela* rule that “a policy which excludes underinsured motorist benefits when the insured is injured while occupying a vehicle owned by the insured or family member is *presumed to be invalid*.” A limited exception to the rule is the situation where the plaintiff attempts to convert UIM to BI coverage under a single policy.⁴⁵ However, where the plaintiff family member seeks to recover under the BI coverage of one family policy and the UIM coverage of another, the “Family Car Exclusion” has been ruled invalid as a violation of public policy. This has occurred in Minnesota, in *DeVille v. State Farm*, and in Pennsylvania, in *Marroquin v. Mutual Ben. Ins. Co.*⁴⁶ Hence, a family member can recover UIM coverage from a second family policy after getting liability coverage from the first. Because the *Deville* and *Marroquin* cases arose in states that address UIM coverage by statute, insurers could argue they do not apply in Montana where UIM coverage is not the subject of legislation. However, the Montana Supreme Court rejected that argument in *Bennett v. State Farm Mut. Auto. Ins. Co.*⁴⁷ where, in a “stacking” dispute, it said:

We disagree. The purpose of underinsured motorist coverage is to provide a source of indemnification for accident victims when the tortfeasor does not provide adequate indemnification. *State Farm Mutual Automobile Ins. Co. v. Estate of Braun*, (1990), 243 Mont. 125, 793 P.2d 253. The public policy expressed in *Braun*, and in the earlier cases cited above, favors adequate compensation for accident victims. The absence of a statutory requirement is irrelevant, for the public policy considerations that invalidate contractual “anti-stacking” provisions in an uninsured motorist endorsement also support invalidating those provision in an underinsured motorist endorsement.

Simply stated, Montana has a judicially recognized public policy that favors adequate compensation for accident victims. The insurers use of the family exclusion in UIM coverage must not run afoul of that public policy.

In *Tissell v. Liberty Mutual Ins. Co.*,⁴⁸ the Washington Supreme Court completely invalidated the family exclusion for UIM coverage and allowed the passenger claimant to recover under both the liability and UM coverage of a single policy covering her family auto. In that case, the deceased was a passenger in a car when her husband drove it off the road and into the river. She fell into a coma and died five years later. Liberty Mutual denied

the UIM coverage citing the family exclusion and also the “liability coverage exclusion” which excluded from the definition of an underinsured auto any auto covered by the liability coverage of the same policy.

With regard to the family exclusion of UIM benefits, the court said, “We hold that the family member exclusion violates the public policy in favor of full compensation for accident victims, has not been authorized by the Legislature, and is void as a result.” The court analyzed the risk involved and said, “an exclusion may be justified where an insurer’s risk is affected by the nature of the persons or conduct excluded – such as when an unauthorized driver takes the wheel.” But, if the provision excludes a class of victims, it has no bearing on the risk the insurer is taking, and the justification does not apply. The court found the family exclusion to involve a class of innocent victims whose conduct does not affect the nature of the insurer’s risk and said, *An exclusion which denies coverage when certain victims are injured is violative of public policy.* [italics the court’s] The court acknowledged that the insurer has less risk if it refuses to insure family members, but asserted that insuring victims who are family members does not subject the insurer to an indeterminate risk. The insurer can calculate the premium necessary to comply with the policy of full compensation for victims.

Hence, in **Tissell**, the family exclusion in UIM coverage was simply held invalid without regard to whether it excludes amounts in excess of the minimum mandatory limits. Again, the public policy of full compensation for accident victims was based on the Washington UIM statute. However, Montana judicially recognizes the same public policy as stated in **Bennett**, and the family exclusion in UIM should be declared invalid because its arbitrary exclusion of an innocent class of insureds from benefits violates the public policy of full compensation for accident victims expressed in **Bennett**.

Recovering under both the Liability Coverage and the UIM Coverage.

With regard to the “liability coverage exclusion,” the court in **Tissell** also held that Mrs. Tissell could recover under both the liability coverage and the UIM coverage of the Liberty Mutual policy. The policy UIM coverage contained a “liability coverage exclusion” removing from the definition of an underinsured motor vehicle, any vehicle insured under the liability coverage of the policy. This meant that a neighbor passenger in the wrecked vehicle could recover under her UIM coverage, but Mrs. Tissell could not recover under hers. The court noted that the exclusion thwarted the public policy in favor of full compensation, because the victim there was the purchaser of the policy. She had no alternative source of UIM coverage, and it was unreasonable to expect her to buy a separate policy of UIM just to avoid the exclusion. Again, where the Montana claimant is a named insured, and hence a person who purchased the same policy, the line of argument used in **Tissell** when combined with the public policy of **Bennett** should prompt a court to invalidate the “liability coverage exclusion” where it results in depriving the insured victim of the benefit of the UIM coverage.

I should note here that states like New Mexico and Washington have statutes that make UIM coverage mandatory. Hence, the New Mexico Appellate Court, in **Martinez v. Allstate Ins. Co.**,⁴⁹ held that, under the New Mexico UIM statutory provision, UIM coverage had to be offered for the protection of all insureds, so that a “family member” living in the same household fell in that class of protected insureds. Consequently, the court held that the insurance policy contract could not impose an exclusion (“family” or “family owned vehicle”) where the statute did not. Query: Shouldn’t the MTLA seek to amend the UM statute, MCA §33-23-201, by simply adding UIM into it? Carriers would just have to offer UIM coverage; consumers could refuse it; and UIM coverage would be protected.

Testing the family exclusion against the reasonable expectations of the insured.

In **Transamerica v. Royle**, the court, after ruling the household exclusion invalid for violation of the Mandatory Liability Protection Act, added that it also was invalid due to “its failure to ‘honor the reasonable expectations’ of the purchaser of the policy.” The court in **Royle** quoted Professor Keeton’s famous underpinning for the reasonable expectations doctrine.⁵⁰

The objectively reasonable expectations of applicants and intended beneficiaries regarding the terms of insurance contracts will be honored even though painstaking study of the policy provisions would have negated those expectations.”

As the Federal Court in Montana said in *Shook*, “The objectively reasonable expectations of the purchaser are ‘honored [in Montana] notwithstanding the fact that a “painstaking study” of the policy would [negate] those expectations.”⁵¹ In *Shook*, the court found the State Farm household exclusion to the Bodily Injury Liability coverage to be ambiguous because a reasonable insured might read the exclusion, “There is no coverage . . . 2. For Any Bodily Injury to: . . . c. any insured or any member of the insured’s family residing in the insured’s household . . .” to mean that the policy provides no indemnification or defense to an insured or the family member who is sued. The insurer argued it could only mean the insured could not make a claim for injury under the coverage. Having found the provision ambiguous, the court subjected it to the reasonable expectations test. It noted that the exclusion was separated “both in space and relation” from the broad basic insuring agreement which promised that State Farm would “Pay damages for which an insured becomes legally liable to pay because of: a. bodily injury to others” and found it violated the insured’s reasonable expectations.

The Kentucky Supreme Court in *Lewis v. West American Ins. Co.* found that, where family exclusion provisions defeat the coverage, the coverage “bought, paid for and reasonably expected” by the insured “is illusory.”⁵²

The over inclusiveness of the family exclusion clause is socially destructive and corrosive to our citizenry’s confidence in our system of justice. The family exclusion operates to bar all valid claims of injured family members in order to preclude the possibility of collusion. We cannot lock our Commonwealth’s courthouse doors to the many who are injured and maimed because of a suspicion that a few members of this class might advance an exaggerated claim.⁵³

The court in *Lewis* held the family exclusion to violate the public policy of “fair compensation for injuries received by innocent victims of another’s negligence.” The language in *Lewis* by which the court reasoned and held the family exclusion invalid does not appear to be limited to exclusions to Bodily Injury Liability Coverage, but would equally apply to family exclusions to UM and UIM coverage.

Counsel’s task is to persuade the court that the family exclusion defeats the reasonable expectations of the insured. In some jurisdictions, that means initially persuading the court that the clause or its placement result in ambiguity.⁵⁴ If the exclusion is not ambiguous, such courts do not inquire into the reasonable expectations of the insured, and the family exclusion has been upheld for amounts over statutory minimums.⁵⁵

In *State Farm v. Falness*,⁵⁶ the 9th Circuit completely invalidated the “named insured exclusion” (a form of family exclusion) as applied to the liability coverage on the ground that it violated the reasonable expectations of the insureds. Though the court could not ascertain from the insured husband and wife their reasonable expectations, since they were both killed in the accident, it based the violation on the fact that the exclusion appeared on page six of the 18-page policy. The court followed the Arizona Appellate Court opinion in *State Farm v. Dimmer*⁵⁷ which had followed a “format and clarity” analysis and said:

...the exclusion in this case is unenforceable against the Dimmers because of its technical wording and inconspicuous location within the policy boilerplate, and because it guts the coverage ostensibly granted by the declarations page.

Dimmer, too found the household exclusion completely invalid for violating the reasonable expectations of the insured. It said the test was not the understanding of “a person trained in the law or the insurance business,” but what “the reasonably intelligent consumer who might check on his or her rights would understand.”

In the Arizona case of *Averett v. Farmers Ins. Co.*,⁵⁸ the court overturned a summary judgment for the insurer that relied on a family exclusion to the liability coverage and remanded the case for trial. The Averett children were seriously injured passengers in an accident in which their mother, who was driving, was killed. Their father had ordered from the agent, “full coverage” for his entire family, and the agent sold him \$250,000 per person limits of BI coverage subject to a family exclusion that reduced the children’s recovery to minimum mandatory \$15,000 apiece. The Arizona court set out four situations in which it would not enforce such exclusions even if unambiguous, if they violated the customer’s reasonable expectations.⁵⁹ Those were (1) where the unambiguous policy term cannot be understood by the reasonably intelligent consumer; (2) where there is inadequate notice of a term that is unusual, unexpected or that emasculates apparent coverage; (3) where conduct of the insurer would

“create an objective impression of coverage in the mind of a reasonable insured”; (4) where activity of the insurer has induced the reasonable belief in coverage, though “expressly and unambiguously denied by the policy.”

Testing the family exclusion against Montana public policy, which prohibits provisions that defeat coverage for which the insurer has received valuable consideration.

In *Bennett*,⁶⁰ the Montana Supreme Court said:
The public policy embodied in these decisions is that an insurer may not place in an insurance policy a provision that defeats coverage for which the insurer has received valuable consideration.

Clearly, the auto insurers are placing in the auto policies in Montana household or family exclusions that defeat BI, Med Pay, UM, and UIM coverages. Insurers will argue that their premiums reflect the reduced risk that the family or household exclusions provide them and will assert that they have not received valuable consideration for coverage of family members.⁶¹ Given the fact that extensive use of the family exclusions has made some coverages illusory and others minimum limits, it is worth asserting violation of this public policy and doing the discovery necessary to determine whether they are indeed receiving valuable consideration for coverages they have defeated.

Conclusion

The pervasive insertion of family, household, or family car exclusions into BI, UM, and UIM coverages in automobile policies defeats the primary purpose for which most insureds purchase auto insurance. Insureds buying high limits out of responsibility for and protection of their families often find the coverage paid for is illusory or limited to statutory minimums. The defense that the exclusions are express and unambiguous flies in the face of the fact that even lawyers have not appreciated the extent to which they defeat coverage against the reasonable expectations of the insureds. The fact that family exclusions appear in these contracts of adhesion and that there is no practical way the insured families can change their conduct to avoid the exclusions adds to their inherent unfairness. In effect, the family exclusions are a throwback, relegating whole classes of insureds to the time before courts abrogated guest passenger statutes, spousal immunity and parental immunity. In many cases, the insured's freedom from antiquated and harsh tort law has simply been suppressed by the family exclusions.

It is time in Montana to mount an offensive against the family exclusions in all forms. Where the exclusions violate mandatory insurance statutes, they need to be declared invalid. Where they do not, there are sound judicially recognized public policy reasons for invalidating them. Courts around the United States have been wrestling with the family exclusions, because they ultimately deprive innocent injured family victims of adequate compensation for which they planned, paid, and reasonably expected. Consequently, there is much case law available to the lawyer who wants to tailor arguments in the effort to invalidate these arbitrary and illogical exclusions. The ALR 4th annotation on validity of family exclusions has over 120 pages of cases in its text and supplement. Sadly, many of the decisions find the exclusions valid. Nevertheless, plaintiff's counsel, mining the cases will find rich veins of eloquent, compelling, and highly logical legal opinions by courts that have invalidated the family exclusions in light of statutes or judicially declared public policy.

1. 656 P.2d 820 (Mont. 1983).

2. 872 F.Supp. 768 (D. Mont. 1994).

3. 898 P.2d 1220 (Mont. 1995).

4. 945 P.2d 32 (Mont. 1997).

5. 712 P.2d 550 (Idaho 1985).

6. citing *Gibson v. Gibson*, 479 P.2d 648 (Cal. 1971).

7. See, Deborah Maschal, *The Demise of the Family Member Exclusion Clause in Automobile Insurance Policies*, 25 Tex. Tech. L. Rev. 1103 (1994) for an article friendly to the idea.

8. MCA §61-6-301, incorporating 61-6-103.

9. *Shook v. State Farm Mut. Ins. Co.*, 872 F.Supp. 768 (1994).

10. *Martinez v. Allstate Ins. Co.*, 124 N.M. 36, 946 P.2d 240 (N.M.Ct.App. 1997).

11. 39 F.3d 966 (9th Cir. 1994).

12. I.S.O., Inc., PAP form PP 00 01 06 94.

13. *Id.*

14. From *Tissell v. Liberty Mutual Ins. Co.*, 115 Wash.2d 107, 795 P.2d 126 (1990).

15. *Marroquin v. Mutual Ben. Ins. Co.*, 591 A.2d 290 (Pa.Super. Ct. 1991).

16. I.S.O., Inc, PAP form PP 03 11 06 94.

17. I.S.O., Inc., PAP form PP 00 01 06 94, Part B.
18. 772 S.W.2d 692 at 694 (Mo.Ct.App.1989).
19. 927 S.W.2d 829 (Ky. 1996).
20. **Royle** at 823.
21. 721 P.2d 342 (Mont. 1986).
22. **Brown v. Merlo**, 506 P.2d 212 (Cal.1973); **Lewis v. West American Ins. Co.**, 927 S.W.2d 829 (Ky. 1996).
23. **Lewis**, at 832.
24. 643 P.2d 441 (Wash.1982).
25. **Lewis**, at 833.
26. *Id.*
27. 795 P.2d 126 (Wash. 1990).
28. 862 P.2d 1146 (Mont. 1993).
29. 795 P.2d, at 128.
30. 752 P.2d 166 (Mont.1988).
31. 897 S.W.2d 119 (Mo.Ct. App.1995).
32. See, also, **Liberty Mutual v. Sanford**, 879 S.W.2d 9 (Tex. 1994).
33. 970 P.2d 1054 (1998).
34. 903 P.2d 1359 (Mont. 1995).
35. 495 P.2d 193 (Mont. 1972).
36. 640 P.2d 908 (Mont. 1982).
37. 462 S.E.2d 650 (N.C. 1995).
38. Citing, **Bass v. N.C. Farm Bureau Mut. Ins. Co.**, 418 S.E.2d 221 (N.C. 1992).
39. 294 N.W.2d 141 (Mich. 1980).
40. 462 S.E.2d, at 653.
41. 768 F.Supp. 272 (E.D. MO. 1991).
42. **Wolgemuth v. Harleysville Mut. Ins. Co.**, 535 A.2d 1145 (Pa.Super. Ct. 1988).
43. *Id.*
44. **American Motorist Ins. Co. v. Sarvela**, 327 N.W.2d 77 (Minn. 1982).
45. *Id.*
- 46., 367 N.W.2d 574 (Minn. 1985); 591 A.2d 290 (Pa.Super. Ct. 1991).
47. 862 P.2d 1146 (Mont. 1993).
48. 795 P.2d 126 (Wash. 1990).
49. 946 P.2d 240 (N.M.Ct.App.1997).
50. **Royle**, at 824.
51. **Shook**, at 774 citing **Wellcome v. Home Ins. Co.**, 849 P.2d at 193.
52. 927 S.W.2d, at 834.
53. *Id.*
54. See, **Smalls v. State Farm**, 678 A.2d 32 (D.C. 1996).
55. *Id.*
56. 39 F.3d 966 (9th Cir. 1994).
57. 773 P.2d 1012 (Ariz. App. 1988).
58. 869 P.2d 505 (Ariz. 1994).
59. *Id.*, at 507.
60. 862 P.2d at 1148 (Mont. 1993).
61. See, Kevin Black, *Lewis v. West American Insurance Co.: Public Policy or Insurance Policy?*, 24 N.Ky.L.Rev. 333 (1997) for an opposing point of view on family exclusions.