

Policy Interpretation

Criminal Act Exclusion in Auto Liability Policy Is Not Contrary to Public Policy and Is Therefore Enforceable.

No Reasonable Expectation of Coverage Resulted from Ambiguity in Auto Rental Pamphlet Describing Restrictions on Coverage

Bailey v. Lincoln General Insurance Company, __ P.3d __, 2011 WL 2150759 (Colo. May 16, 2011)

Case at a Glance

The application of an excess automobile liability policy's criminal acts exclusion to intentionally criminal conduct, as opposed to criminally negligent conduct, does not violate Colorado public policy.

"There are two main ways in which the doctrine of reasonable expectations has manifested itself in Colorado, ensuring that insurers have 'fully and fairly' conveyed coverage limitations to insureds. The first is where an ordinary, objectively reasonable person would, based on the language of the policy, fail to understand that he or she is not entitled to the coverage at issue." The language of a car rental agreement setting forth prohibited uses of the rented vehicle and explaining that such uses will void coverage would not lead an ordinary, objective insured to expect coverage for his criminal acts under a supplemental policy that provides coverage in excess of the statutorily mandated minimum. "The second manifestation of the doctrine is where, because of circumstances attributable to an insurer, an ordinary, objectively reasonable person would be deceived into believing that he or she is entitled to coverage, while the insurer would maintain otherwise." This principle does not create coverage for excluded criminal acts under the supplemental policy even though the rental clerk told the renter that he would be covered if he "gets into a wreck," failed to explain the coverage or its exclusions to the renter, and failed to provide the renter a copy of the policy or a brochure describing the policy.

Summary of Decision

Relevant Facts. This case began with a serious vehicular accident in which Julie Bailey sustained serious injuries, and her child was killed, when their collided with a car rented and driven by Raymond Juhl. Juhl was stoned on methamphetamines at the time. When the police tried to stop him, he initiated a high-speed chase; it lasted 12 minutes; it went on for 20 miles; Juhl ran several stop signs; drove at illegal speeds up to 100 mph; repeatedly swerved into the oncoming lane; forced other vehicles off the road; and avoided police planted stop sticks. At last, while in the oncoming lane, he crashed into the on-coming Bailey car.

Juhl pled guilty to five felonies related to his use of the car, including second degree murder, first degree assault, vehicular homicide, vehicular assault, and unlawful possession with intent to distribute a controlled substance. He was sentenced to 43 years in prison.

So far as the rental arrangements are concerned, two weeks before the accident, Juhl rented the car in a transaction which lasted no more than 6 minutes, during which Juhl purchased \$1 million "Supplementary Liability Insurance" (SLI)—a form of excess insurance for a covered amount over \$25,000—from Lincoln General Insurance (LGI). The car rental company, Dollar Rent-A-Car, provided Juhl's primary insurance as part of the car rental agreement. The Dollar primary policy provided only statutorily mandated minimum liability coverage of \$25,000 per person/\$50,000 per accident. The Dollar primary policy was not at issue before the Colorado Supreme Court, except to the extent that it was relevant to the meaning of the SLI policy.

The rental clerk sold the SLI policy. He had no formal training in selling insurance. He told Juhl "if [Juhl] got into a wreck, the car was covered." The clerk never reviewed the policy with Juhl, and did not tell him about any coverage exclusions or prohibitions. Indeed, the clerk never gave Juhl a copy of the SLI policy. The only source of information Juhl had on the SLI policy was the rental agreement, which the clerk provided Juhl at the end of the transaction. The rental agreement was organized into sections addressing major rental car topics. One section spelled out, in capitalized block letters, how a renter can violate the terms of the agreement by engaging in

a prohibited use of the vehicle, along with the attendant consequences for such a violation. The prohibitory language forbade, among other things, racing or similar contests, using the car for any illegal purpose, using the car in any felony, the driver being under the influence of drugs, the driver intentionally causing damage, or the driver engaging in any willful, reckless, or wanton conduct, while using the car. The prohibitory language expressly warned Juhl in bold, all capital letters that any prohibited use of the vehicle would void the optional SLI coverage. The same warning was made in a separate part of the rental agreement describing Juhl's third-party liability responsibility. That section also informed Juhl that a brochure describing the SLI coverage and its exclusions was available to the rental counters. Juhl neither asked for nor received the brochure. He also never read the rental agreement.

Legal History. Before going to prison, Juhl assigned his claim against LGI to the Baileys—mother and estate of deceased son. The underlying case then proceeded. There was an uncontested hearing at which the judge awarded the Baileys \$2 million in damages against Juhl. The car rental company paid \$25,000 immediately.

In the ensuing coverage litigation between LGI and the Baileys, the trial court granted summary judgment in favor of LGI based on Juhl's violation of the rental agreement's prohibition against using the car in the commission of a crime. The Colorado Court of Appeals affirmed, holding that the SLI coverage's criminal-acts exclusion was not ambiguous, did not violate public policy, and was not unconscionable. *Lincoln Gen.*, 224 P3d at 339–42. The court also determined that the criminal-acts exclusion was not unenforceable under the doctrine of reasonable expectations, which did not apply because that doctrine, according to the court, is only "an interpretive tool used to resolve ambiguity." 224 P3d at 339. The Colorado Supreme Court granted certiorari, and affirmed the court of appeal, albeit on somewhat different grounds.

Applicable Law of Public Policy. The first issue the supreme court treated was public policy and insurance policies. The court concluded that the criminal acts exclusion at issue did not violate public policy. The court weighed Colorado's public policy of protecting innocent tort victims against the state's public policy of promoting freedom of contract, and

ruled that an insurer's contractual right to exclude coverage for criminal acts should prevail. Here is how the court got there.

The court applied a *de novo* standard when determining public policy and its requirements. Insurance provisions which violate public policy can be declared unenforceable. Any such declaration depends upon the facts of each individual case. However, public policy challenges to contract language should be treated with caution. Unless insurance policy provisions "dilute, condition, or limit statutorily mandated coverage," they usually will survive a challenge on public policy grounds. Although courts will occasionally strike down a criminal acts exclusion that encompasses not just intentional criminal conduct, but criminally negligent conduct as well, no such negligent conduct was at issue here. Juhl's conduct "arose far above . . . mere criminal negligence." Prohibiting an exclusion of coverage for Juhl's felonious criminal conduct would violate the central concept of insurance by allowing a single insured to consciously control risk. Indeed, the public policy against giving insured's license to engage in intentional misconduct has led several jurisdictions to treat insurance for criminal acts as a violation of public policy.

Doctrine of Reasonable Expectations. The Colorado high court described two ways the doctrine of reasonable expectation protects insurance consumers. First, policies are subject to invalidation or alteration when their wording if it is likely to be misunderstood by the "ordinary reasonably objective person." Second, if circumstances somehow caused by the insurer deceive an ordinary and reasonable insured into believing that he has coverage, when he does not, then the relevant policy is subject to invalidation, in whole or in part. Perhaps most interesting: this unanimous court opinion rejects the view that applying the doctrine of reasonable expectation requires an ambiguity or other unclarity in the subject policy. In other words, the doctrine—applied alone with respect to the language of the policy—can alter coverage in restricted ways if a complained of policy provision is manifestly unfair. This means that external evidence can not only fill in but override some policy language under some circumstances. Of course, the insured would bear the burden of proof as to this matter.

Bottom-Line Application. In the end, Colorado's

relatively generous version of the reasonable expectations doctrine did not help the Baileys establish coverage under Juhl's SLI policy. There was nothing at all anywhere in the rental agreement, including the insurance sections, which could lead a reasonable person to believe that the SLI coverage would not contain a criminal acts exclusion. One reason the court gives for this view is quite simple and direct: no person with elementary common sense could believe that such a thing was available. It is therefore impossible to have a reasonable expectation that conduct like that of Juhl which caused the bodily injury would be covered for those injuries. The court pointed out that even in cases where an insurer engaged in a "concerted effort" to hide an exclusion, giving rise to a reasonable expectations of coverage under the "deception" prong of the reasonable expectations test, the exclusion at issue was one the insured would not expect. // Quinn

Flood Insurance/Preemption

Federal Law Preempted Questions of Issuance and Administration of Flood Insurance Policy

Claim of Breach of Standard Flood Insurance Policy Was Properly Removed to Federal Court

Davis v. Nationwide Mutual Fire Insurance, ___ F.Supp.2d ___, 2011 WL 1792595 (E.D. Va. May 5, 2011)

Case at a Glance

Federal law preempted plaintiff's claims with respect to policy issuance and administration of a Standard Flood Insurance Policy contract issued by a FEMA-regulated "Write Your Own" flood insurance company on behalf of the National Flood Insurance Program. An insured's claims that the SFIP was illegal, that the insurer discriminated based on date of the covered home's construction, that the insurer failed to disclose exclusions, and that of negligent procurement or reformation were dismissed as preempted by federal law.

A claim that an insurer breached a Standard Flood

Insurance Policy contract by denying coverage with respect to certain flood damage to plaintiff's home involved a substantial issue of federal law, and a district court accordingly possessed federal question subject matter jurisdiction over the claim. The court denied plaintiff's objection to removal of the claim to federal court.

Summary of Decision

Plaintiff sued his insurer, Nationwide Mutual Fire Insurance, in a New York state court alleging non-payment of an insurance claim. Plaintiff alleged that defendant breached his Standard Flood Insurance Policy (SFIP) contract by refusing to pay his claim for flood damages. He asserted four additional causes of action distinct from the contract claim, alleging that the policy was illegal, that defendant failed to disclose coverage limitations, that the insurer sold a policy that was more expansive than needed for his property, and that the insurer discriminated against him based on the construction date of his home. The insurer removed the case to federal district court in Virginia, then moved to dismiss for failure to state a claim upon which relief could be granted.

The district court granted the insurer's motion to dismiss the plaintiff's extra-contractual and tort claims as state law claims preempted by federal law. The court denied the plaintiff's motion to remand the remaining contract claim to state court, concluding that federal court's had exclusive jurisdiction with respect to litigation concerning payment of National Flood Insurance Program (NFIP) claims.

Defendant operated as an insurance carrier under FEMA's Write-Your-Own (WYO) program. The court noted that the extent of preemption of state law claims by the federal National Flood Insurance Act (NFIA) had been addressed by only one U.S. Court of Appeals, the Fifth Circuit, which determined in *Campo v. Allstate Insurance Co.*, 562 F.3d 751 (5th Cir. 2009) that federal law does not preempt state law tort claims alleging negligent misrepresentation by a WYO company in connection with procurement of flood insurance. FEMA subsequently issued its own interpretation of the applicable regulations, concluding that federal preemption should apply not just to NFIP claims handling activities, but also to policy administration. Specifically, preemption should apply to the nationally uniform and FEMA-mandated