In the Supreme Court of the State of California

SAMUEL HECKART, **Plaintiff-Appellant,** **v.** **A-1 SELF STORAGE, INC., et al.,** **Defendants and Respondents.**	Case No. S232322

Court of Appeal, Fourth Appellate District, Division One,
Case No. D066831

San Diego County Superior Court,
Case No. 37-2013-00042315-CU-BT-CTL
The Honorable John S. Meyer, Judge

BRIEF OF THE INSURANCE COMMISSIONER OF THE STATE OF CALIFORNIA, INVITED AMICUS CURIAE

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TABLE OF CONTENTS

TABLE OF CONTENTS
(continued)

Page

TABLE OF AUTHORITIES

TABLE OF AUTHORITIES
(continued)

Page

OTHER AUTHORITIES

ISSUES PRESENTED

The issues presented for review, as stated in the petition, are:

1. If a self-service storage facility's form storage rental agreements satisfy the elements of "insurance" under California Insurance Code, section 22, and satisfy all other elements of "insurance" under Code section 1758.75, are those storage rental agreements regulated "insurance" under the Code?

2. Is "principal object" a necessary element of every insurance contract under the Insurance Code?

3. Is an informal Department of Insurance staff decision regarding alleged "insurance" entitled to judicial deference where there is no evidence that the Department saw the contracts in question?

INTRODUCTION

"Insurance is a contract whereby one undertakes to indemnify another against loss, damage, or liability arising from a contingent or unknown event." (Ins. Code, § 22.) But, as this Court's longstanding precedents make clear, the Legislature did not intend every commercial transaction technically meeting this broad definition to be regulated under the Code. When, on review of the relevant provisions of the Insurance Code, it is unclear whether a particular transaction is "insurance" subject to regulation, courts may inquire into the transaction's "principal object." This inquiry helps to ensure that all commercial transactions are not made subject to insurance regulation merely because they contain some elements of risk allocation in the service of the overall transaction's non-insuring, primary purpose.

Where, however, the Legislature has expressly determined that a particular type of transaction is to be regulated under the Insurance Code, it is inappropriate to engage in a principal object inquiry to create a court-

made exception to such regulation, as occurred here. (Ins. Code, § 1758.75, see generally *id.* at § 1758.7, et seq.) The clear legislative intent should control.

But even if the Court engages in a principal object inquiry, that analysis does not allow defendants and respondents in this case to escape regulation. The principal object of the storage facility's "protection plan" is to provide insurance. The storage facility has created an additional product—an insurance product—to sell to the facility's renters. That product and its sale are subject to the requirements of Article 16.3 of the Insurance Code, sections 1758.7 et seq., governing self-service storage facilities' sale of insurance.

The Commissioner respectfully requests the Court give weight to his official, considered views of the law, as set forth in this brief, to the extent the Court finds those views reasonable and persuasive.

LEGAL BACKGROUND: RENTERS' INSURANCE FOR SELF-SERVICE STORAGE

Selling insurance without a license from the Department is against the law. (Ins. Code, § 700, subds. (a)-(b); *id.*, § 1631 [requiring valid license to solicit, negotiate, or effect insurance contracts]; see, e.g., *id.*, § 1861.05 [requiring approval of insurance rates and prohibiting excessive or inadequate rates].) In this state, certain licensed insurers that are not in the self-service storage business write and sell renters insurance directly to renters; to comply with the law, their rates must be approved by the Department. (See 1 CT 209, ¶ 40.)

In 2004, the Legislature recognized that self-service storage facilities had been selling insurance to their renters for many years without a license, in violation of the Insurance Code. (Department's Request for Judicial Notice ("RJN"), Ex. A [Sen. Comm. on Ins., Assem. Bill No. 2520 (2003-

2004 Reg. Sess.) as amended Apr. 27, 2004, pp. 3-4].) In response, the Legislature acted to create a licensing procedure (Ins. Code, § 1758.7 et seq.) that prescribed the authorized sale of insurance by self-service storage facilities to renters of storage units. (RJN, Ex. B [Sen. Rules Com., Off. of Sen. Floor Analyses, 3d reading analysis of Assem. Bill No. 2520 (2003-2004 Reg. Sess.) as amended Jul. 22, 2004, p. 4].) Although described in the legislative history as creating "a new limited line of insurance category" (*id.* at p. 2), the purpose of the new law was "[t]o create a limited agent license for self-service storage facilities to sell hazard insurance to renters of storage units" (*id.* at p. 4).

Like any other entity, self-service storage facilities may not sell insurance in this state unless they do so in compliance with the insurance laws. Article 16.3 of the Insurance Code, sections 1758.7 et seq., and implementing regulations (Cal. Code Regs., tit. 10, § 2194.9 et seq.) provide a streamlined licensing scheme under which self-service storage facilities, acting as agents for authorized insurers, may offer or sell only certain "types of insurance and only in connection with, *and incidental to*, self-service storage rental agreements." (Ins. Code, § 1758.75, italics added.) The "types of insurance" self-service storage facilities may be licensed to offer or sell as agents for an authorized insurer already exist and are written and sold by standard insurance companies: "hazard insurance coverage to renters for the loss of, or damage to, tangible personal property in storage or in transit during the rental period" and "any other coverage the commissioner may approve as ... appropriate in connection with the rental of storage space." (Ins. Code, § 1758.75, subds. (a)-(b); see *id.*, §§ 100-120 [describing various broadly described classes, including "Miscellaneous"].) Similar kinds of insurance may occur within different classes but "classification of similar insurance may vary with the subject matter, risk, and connected insurances." (*Id.*, § 121.) Accordingly, a self-service storage

facility could be licensed either as a Fire and Casualty Broker-Agent or as a Self-Service Storage Insurance Agent. (1 CT 101.)[1]

FACTUAL AND PROCEDURAL BACKGROUND

The factual and procedural background is set out in detail in the court of appeal's decision and the parties' briefs. The Commissioner provides this brief summary for the Court's convenience.[2]

I. DEANS & HOMER'S MARKETING OF ITS "ALTERNATIVE LEASE PROGRAM" TO THE SELF-SERVICE STORAGE INDUSTRY

Respondent Deans & Homer, a licensed broker-agent, sells self-service storage renters' insurance directly to consumers in California. (1 CT 204, ¶19; 1 CT 209, ¶ 40.) Sometime in or around 2003, Deans & Homer developed a new model for selling personal property protection to self-service storage unit renters that would enlist the facility owner as the selling agent. (2 CT 267-271; 1 CT 205-207.) The proposed model was described as an "alternative lease program." (2 CT 286, ¶ 2.) Respondents A-1 Self-Storage Inc. and the Caster companies (collectively, A-1) own, operate, and manage more than 40 self-service storage facilities in California. (1 CT 203, ¶¶ 13-17.) Deans & Homer marketed its alternative lease program to A-1, providing it with templates and guidance to use in selling limited liability coverage to renters for their stored personal property. (1 CT 205-207.) A-1's "Customer Goods Protection Plan" ("Protection Plan") is comparable to an insurance policy offered by Deans & Homer directly to self-service storage unit renters (a "Customer Storage Insurance Policy"); the rates for

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[1] The "Fire and Casualty" Broker-Agent license is now referred to as Property Broker-Agent and Casualty Broker-Agent licenses.

[2] Because this case was dismissed at the pleadings stage, on appeal, plaintiffs' well-pled allegations of fact are taken as true. The statement of facts in this brief reflects that procedural posture.

such policy are required to be, and have been, approved by the Department. (1 CT 209-211.)

Concurrently, Deans & Homer sold insurance policies to A-1 to cover losses A-1 incurred covering renters' claims made under the Protection Plan for a premium of 74 cents per renter per month. (1 CT 206, ¶ 28.) Under the insurance policy sold by Deans & Homer, A-1 is covered for almost all of its liability under the Protection Plan. (*Ibid.*)

II. A-1'S STORAGE RENTAL AGREEMENT AND "CUSTOMER GOODS PROTECTION PLAN"

A-1's Storage Rental Agreement requires the renter to provide written proof of insurance for the actual cash value of the stored property or to purchase the Protection Plan from A-1. (2 CT 312, ¶ 12.) If a renter declines the Protection Plan, but fails to provide proof of insurance within 30 days, the renter is automatically enrolled in the Protection Plan. (2 CT 313.) Purchase of the Protection Plan satisfies the Rental Agreement's insurance requirement. (2 CT 314.)

The Protection Plan is characterized as an "addendum" to the Rental Agreement and provides that it is a "limited acceptance of liability" that modifies "the [landlord's] waiver of liability" that would otherwise apply. (2 CT 314; but see 2 CT 312, ¶ 13 [broad exculpatory clause unmodified by Protection Plan].) For $10 a month, the Protection Plan provides that A-1 "retain[s] liability for loss of or damage to Tenant's property while stored" of up to $2,500 for losses caused by specified hazards, including fire, theft, roof leak, windstorm or the collapse of the building where the property is stored. (2 CT 314, ¶ 2.) The Protection Plan excludes coverage of other specified hazards, such as flood, sewer overflow, insects or vermin, mold, earthquake, etc. (2 CT 315, ¶ 3.) It also identifies certain types of property it will not cover. (2 CT 315, ¶ 4.) The Protection Plan requires A-1 to pay

the actual amount the renter pays to repair the covered property or to replace it with property of similar quality, whichever is less, but does not prescribe a claims procedure. (2 CT 315, ¶ 5.)

The Protection Plan prominently disclaims in two places that it is a contract of insurance. (2 CT 314-315.) While A-1's Protection Plan is comparable to the self-service storage renters' insurance policy offered by Deans & Homer, it offers less coverage at a higher cost. (1 CT 209-211.) A-1 has more "than 15,000 California renters enrolled in the Protection Plan at any given time." (1 CT 206, ¶ 28.) During the five-year period preceding this action, A-1 netted about $1.6 million per year from Protection Plan sales, and paid out about $25,000 in claims per year. (1 CT 213, ¶¶ 49-51.)

III. DEPARTMENT STAFF'S LETTERS TO DEANS & HOMER

In 2003, counsel for Deans & Homer wrote to the Department inquiring whether a "modified lease" Deans & Homer proposed to offer under its "alternative lease program" for the self-service storage industry would be considered an insurance contract subject to regulation under the Insurance Code. (2 CT 286, ¶¶ 2-3; 2 CT 267-271.) There is no evidence in the record that the Department received any other materials with the original letter. (2 CT 330-332.) Department staff counsel responded by a one-page letter, summarily stating that "the proposed alternative lease provisions" would not be insurance and citing *Truta v. Avis Rent A Car System, Inc.* (1987) 193 Cal.App.3d 802. (2 CT 286, ¶ 3; 2 CT 273.)

In 2008, counsel for Deans & Homer in some unknown form again communicated with the same staff counsel about the alternative lease program and Deans & Homer's sale of insurance policies covering risks assumed by the self-service storage facility owners. (2 CT 286, ¶5.) There is no allegation that Deans & Homer sent any additional written materials

to the Department at that time. (*Ibid.*) By an even shorter letter, the Department staff counsel reconfirmed his prior statement that the arrangement would not constitute insurance. (2 CT 286-287, ¶ 6, 2 CT 275.) There is no evidence in the record (or in the Department's files) regarding what materials staff counsel reviewed, if any, before issuing the 2008 letter. (2 CT 275; Declaration of Lynell N. Wise, ¶ 6 [Department Custodian of Records].)

IV. HECKART'S LAWSUIT AND DECISIONS BELOW

Appellant Heckart, an A-1 renter, filed a class action lawsuit, alleging that the unlicensed sale of an insurance product by A-1 and Deans & Homer was unfair, unlawful and deceptive, and done in a manner specifically structured to avoid the costs of legal compliance and rate limitations imposed under the insurance laws. (1 CT 199, ¶ 1.) On that basis, Heckart alleged causes of action for unlawful and deceptive business acts and practices in violation of California Business & Professions Code section 17200 et seq. and the Consumer Legal Remedies Act (CLRA) (Civ. Code, § 1750 et seq.), as well as for negligent misrepresentation and civil conspiracy. (1 CT 198-230.)

The trial court sustained defendants' demurrer to Heckart's first amended complaint without leave to amend, and the court of appeal affirmed. (Slip op., p. 3.) The court of appeal held that the Protection Plan was not insurance subject to regulation under the Insurance Code because the "principal object" of the "entire transaction between the parties" was the rental of storage space. (Slip op., p. 10.) For that reason, the court held, the licensing requirements of Insurance Code section 1758.75 et seq. did not apply.

Consequently, the court of appeal held that the trial court properly sustained the demurrer to Heckart's unfair competition, negligent

misrepresentation, and civil conspiracy causes of action, because all were premised on the allegation that the Protection Plan was insurance. (Slip op., pp. 13-14.) The court also affirmed that the CLRA does not apply to the sale of insurance or the lease of real property. (Slip op., pp. 14-15.)

ARGUMENT

I. THE PRINCIPAL OBJECT INQUIRY CAN ASSIST COURTS IN DETERMINING WHETHER THE LEGISLATURE INTENDED THAT A TRANSACTION WITH INSURANCE ATTRIBUTES BE REGULATED

On its face and read in isolation, the definition of "insurance" in the Insurance Code is quite broad. Again, "[i]nsurance is a contract whereby one undertakes to indemnify another against loss, damage, or liability arising from a contingent or unknown event." (Ins. Code, § 22.) This Court has construed this provision to require two elements: "(1) a risk of loss to which one party is subject and a shifting of that risk to another party; and (2) distribution of risk among similarly situated persons." (*Metropolitan Life Ins. Co. v. State Bd. of Equalization* (1982) 32 Cal.3d 649, 654.)

Many common business ventures, however, entail some element of risk distribution or assumption. To prevent an overbroad reading inconsistent with the Legislature's intent, this Court has clarified that the shifting and distribution of the risk of loss "'does not necessarily mean that the agreement constitutes an insurance contract *for purposes of statutory regulation.*'" (*Sweatman v. Department of Veterans Affairs* (2001) 25 Cal.4th 62, 74 (*Sweatman*), citing *Title Ins. Co. v. State Bd. of Equalization* (1992) 4 Cal.4th 715, 726, italics added by *Sweatman.*) "'That view would cause . . . [the insurance statutes] to engulf practically all contracts, particularly conditional sales and contingent service agreements.'" (*Transportation Guarantee Co. v. Jellins* (1946) 29 Cal.2d 242, 249

(*Jellins*) quoting *Jordan v. Group Health Assn.* (1939) 107 F.2d 239, 247 (*Jordan*).)

This Court has identified factors that can assist courts in determining whether the Legislature intended that a particular risk-shifting and risk-distribution arrangement be regulated as insurance. Courts consider the extent to which "'the specific transactions or the general line of business at issue involve one or more of the evils at which the regulatory statutes were aimed.'" (*Truta v. Avis Rent A Car System, Inc.* (1987) 193 Cal.App.3d 802, 812 quoting Keeton, Insurance Law (1971) § 8.2(c), p. 552.) The Insurance Code is designed to protect the insured, "'particularly those [regulations] relating to the maintenance of reserves and to the regulation of investments and financial operations. . . . Such regulations become important only if the insurer has assumed definite obligations.'" (*Truta, supra,* at p. 813 quoting *California Physicians' Service v. Garrison* (1946) 28 Cal.2d 790, 810 (*Garrison*).) The insurance laws "are not intended to apply where no risk is assumed and no default can exist . . . ." (*Ibid.*)

Relevant to this case, courts may also ask whether addressing the risk involved "'or something else to which it is related in the particular plan is its principal object and purpose.'" (*Jellins, supra,* 29 Cal.2d at p. 249, quoting *Jordan, supra,* 107 F.2d at p. 247.) "The question, more broadly, is whether, looking at the plan of operation as a whole, 'service' rather than 'indemnity' is its principal object and purpose." (*Garrison, supra,* 28 Cal.2d at p. 809.) While this inquiry is sometime referred to as a "test," it is perhaps better understood as an aid to courts in discerning legislative intent to regulate under the Insurance Code. (See *Wayne v. Staples* (2006) 135 Cal.App.4th 466, 475 (*Wayne*) [describing the principal object inquiry as an "analytic tool"].)

II. WHERE, AS HERE, A COMMERCIAL TRANSACTION IS CLEARLY SUBJECT TO REGULATION UNDER THE INSURANCE LAWS, THE PRINCIPAL OBJECT INQUIRY IS INAPPROPRIATE

When it is clear that a specific type of risk shifting and allocation arrangement is subject to regulation under the Insurance Code, engaging in an additional, separate principal object inquiry is unnecessary and—if used to contradict legislative intent—inappropriate.

For example, in *Sweatman*, this Court considered whether insurance coverages offered under the Cal-Vet home protection plan fell within the purview of the Insurance Code. (*Sweatman, supra,* 25 Cal.4th at pp. 68-75.) The court of appeal ruled that certain disability coverage required as part of a Cal-Vet home loan program was merely "an incidental benefit under the Cal-Vet loan contract," the principal object and purpose of which was the financing of a home purchase, and therefore such coverage was not regulated as insurance. (*Sweatman, supra,* 25 Cal.4th at p. 67; see also *id.* at p. 73.)

While this Court upheld the judgment, it rejected the "principal object" reasoning as support. (*Id.* at pp. 73-74.) What controlled, the Court held, was that "the Insurance Code appears to include an exception for the program of life and disability insurance under the Cal-Vet program." (*Id.* at p. 72, citing Ins. Code § 770.30.) And it was clear that "the Legislature has expressly vested administration of the Cal-Vet program '*solely in the Department of Veteran's Affairs*.' (Mil. & Vet. Code, § 987.54.)" (*Id.* at p. 74, italics original.) The Supreme Court held that "requiring the overlapping authority of the Department of Insurance in this specialized area, would appear inconsistent with the legislative mandate." (*Ibid.*; accord, *Garrison, supra,* 28 Cal.2d at p. 810 [statutes expressly providing for limited regulation of nonprofit physicians' service corporation necessarily exempted such organization from insurance laws].)

Similarly, in *Wayne*, the Court of Appeal for the Second District held that engaging in a principal object inquiry was inappropriate because it was undisputed that the defendant, an office supply store, was offering shipping customers regulated inland marine insurance in connection with its package shipping services. (*Wayne, supra,* 135 Cal.App.4th at p. 475, fn. 3.) The trial court held that because the principal object of the parties' transaction was to ship a package, the store's charge for "declared value coverage" fell out of regulation under the Insurance Code. (*Id.* at p. 475.) The court of appeal held this to be error, because "all insurance contracts, even if sold as a secondary or incidental facet of a transaction with another, primary commercial purpose, are regulated by the Insurance Commissioner and the Department of Insurance unless they fall within a specific regulatory exemption." (*Id.* at pp. 476-477.) A contrary rule would, for example, permit a real estate broker to sell homeowners insurance without being subject to regulation under the Insurance Code because the sale of insurance would be "incidental" to the purchase of a house. (*Wayne, supra,* 135 Cal.App.4th at p. 477.)

The *Wayne* court noted that using the principal object test to exempt the inland marine insurance contract from regulation was "particularly inappropriate" because this class of coverage is expressly regulated by the Insurance Code and likely to be offered "in connection with, and incidental to, the customer's primary purpose of shipping his or her goods." (*Wayne, supra,* 135 Cal.App.4th at p. 477; see Ins. Code, § 1635.) The "determinative question" was not whether the "customer's principal purpose is shipping his or her package, rather than obtaining insurance against loss or damage" but rather whether the facts of the case allowed the store to "enjoy[] the exemption from insurance licensing requirements contained" in Insurance Code section 1635. (*Wayne, supra,* 135 Cal.App.4th at p. 478.) In other words, the statute controlled.

In this case, the court of appeal's use of the principal object inquiry in disregard of legislative intent is similarly inappropriate. Taking the plaintiff's allegations as true, the Legislature has clearly expressed its intent to regulate the self-service storage industry's sale of the very type of coverage A-1 is offering. The Protection Plan creates an obligation for one party—A-1—to compensate another party—the renter—for specified loss or damage to the renter's personal property, regardless of whether the loss or damage would be attributable to A-1. Contrary to the Protection Plan terms, A-1 is not agreeing to "retain" liability. A-1 would not have liability for damage to the *renter's property* unless and until a court of law so ruled. For a profit, A-1 carves out and *assumes* limited liability for loss or damage to the *renter's* stored personal property resulting from specified hazards or perils, including fire, theft, roof leak, windstorm or building collapse (CT 314, ¶ 2 [Protection Plan]; CT 213 [first amended complaint, alleging approximately $8 million in profit over five years].) Under the Protection Plan, A-1 agrees to pay the renter's cost to repair or to replace the property, up to a capped amount. (CT 315, ¶ 5).

This type of coverage is directly comparable to property and casualty insurance policies offered by licensed insurers. (See, e.g., Ins. Code, § 2071 [California Standard Form Fire Insurance Policy, allowing for other perils to be insured against by added written endorsement].) Indeed, other insurers, including those represented by Deans & Homer, offer substantially similar—but better and less costly—insurance products directly to renters. (CT 209-211, ¶¶ 40-42.) Whether something is insurance does not depend on who is offering it.

If the Protection Plan sold by A-1 is not "hazard insurance" because it may be considered incidental to the Rental Agreement, then it is unclear what transactions *would* be subject to licensing under Insurance Code section 1758.7 et seq., given that every transaction other than the Rental

Agreement is in a sense subsidiary or secondary to the Rental Agreement. That construction must be rejected. The form of the Protection Plan reflects only the parties' drafting choices and appears to be designed to avoid regulation under the Insurance Code. (CT 205-206, ¶¶ 22-27.) The parties should not be able to unilaterally avoid the law through manipulations of form. A-1 is selling, without a license, "hazard insurance coverage to renters for the loss of, or damage to, tangible personal property in storage... during the rental period." (Ins. Code, § 1758.75, subd. (a).) The offering or sale of this type of insurance "in connection with, and incidental to" a self-service storage agreement, is expressly regulated. (Ins. Code, § 1758.75, subd. (a).)[3]

III. EVEN IF THE PRINCIPAL OBJECT INQUIRY APPLIES, PROPER ANALYSIS ESTABLISHES THAT THE PROTECTION PLAN IS SUBJECT TO REGULATION AS INSURANCE

In light of the express provisions of Article 16.3 of the Insurance Code, engaging in a separate principal object inquiry is inappropriate. But, properly applied, the inquiry supports the conclusion that the Protection Plans at issue in this case are subject to regulation. Below, the Commissioner attempts to clarify and organize the law surrounding the

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[3] The 2003 and 2008 staff letters suggesting otherwise are not the result of "careful consideration by senior agency officials" but rather reflect an interpretation prepared "in an advice letter by a single staff member. . . ." (*Yamaha Corp. of America v. State Bd. of Equalization* (1998) 19 Cal.4th 1, 13.) The letters are addressed only to Deans & Homer, a single stakeholder with an obvious interest in the outcome, and are based solely on Deans & Homer's description of the proposed program, with no input from other interested parties as would have occurred in a quasi-adjudicatory proceeding or in a rulemaking that is subject to notice and comment. Nor are the letters public opinion letters within the meaning of Insurance Code section 12921.9, signed by the Commissioner or the Chief Counsel of the Department.

principal object inquiry, and explains why, in his view, A-1 is selling insurance without a license.

A. The Non-Regulated Risk-Shifting Provisions in *Jellins* and Its Progeny Are Distinguishable

The Protection Plan's provisions are distinguishable from the risk-shifting provisions that were found not to be subject to regulation under the insurance laws in *Jellins* and its progeny.

1. *Transportation Guarantee Co. v. Jellins* (1946) 29 Cal.2d 242

Under the motor truck maintenance contracts at issue in *Jellins*, plaintiff contractor agreed to maintain the trucks in mechanical repair, to garage and fuel them, and to cause each motor vehicle to be insured "for Owner in an authorized insurance company selected by Contractor. . . ." (*Jellins, supra,* 29 Cal.2d at p. 246.) This Court found that the contracts, on their face, were not unlawful because they did not support an interpretation that plaintiff itself was acting as the insurer. (*Id.* at p. 248.) "[T]he major part of Contractor's service is the supplying of labor'" and that purpose—service—was the "controlling object of each contract," not insurance. (*Id.* at pp. 252 & 249.) The plaintiff contractor's breach of its obligation to maintain collision insurance might, in the event of a collision, make plaintiff liable for the loss, "but such liability would not transmute its truck maintenance business into an insurance business." (*Id.* at pp. 252-253.) The fact that the maintenance contractor agreed to insure the vehicles with an authorized insurer, *not to act as the insurer*, was key. (*Id.* at pp. 248 & 254.)

Unlike the maintenance contractor, A-1 is not agreeing to obtain insurance from an authorized insurer to cover damage to the renter's property. Rather, on its face, the Protection Plan is compatible with an interpretation that A-1 is acting as the insurer.

2. *Truta v. Avis Rent A Car System, Inc.* (1987) 193 Cal.App.3d 802

The collision damage waiver in *Truta* is also distinguishable. *Truta* addressed whether a car rental company's collision damage waiver offering to assume liability for damage or loss to the rental car in an amount up to $1,000 for an additional fee was an illegal contract of insurance. (*Truta, supra,* 193 Cal.App.3d at p. 807.) The court held that the renter's option, for an additional consideration, to allocate the risk of loss to the car rental company was only "peripheral" to the car rental agreement's "principal object and purpose"—the rental of an automobile. (*Id.* at p. 814.)

Key to the decision was the fact that—unlike A-1—the car rental company was *not agreeing to pay any liabilities or costs incurred by the renter*; it was releasing the renter from responsibility for damage to the rental company's car during the course of the lease, and agreeing to take the property back in a damaged condition. The car rental company was not agreeing "'to pay anybody anything'" so regulation under the insurance laws regarding such things as the accumulation of reserves and the solvency or insolvency of the rental company was unnecessary. (*Truta, supra,* 193 Cal.App.3d at p. 815 [quoting Department's analysis].)

Unlike the collision damage waiver in *Truta*, the Protection Plan obligates A-1 to pay the renter for loss or damage to the renter's property. The Protection Plan shifts the renter's risk of property damage to A-1, providing coverage for the renter's property and paying claims to the renter up to a capped amount.

3. *Automotive Funding Group, Inc. v. Garamendi* (2003) 114 Cal.App.4th 846

For the same reasons, the loss damage waiver program at issue in *Automotive Funding Group, Inc. v. Garamendi* (2003) 114 Cal.App.4th 846 (*Garamendi*) is distinguishable from the Protection Plan. *Garamendi* was a

debt cancellation program whereby the lender held a lien on the used car as security for the car loan and required the car buyer to obtain insurance for physical damage and theft, or to participate in the lender's loss damage waiver program. (*Garamendi,* 114 Cal.App.4th at pp. 849-850.) Under the program, *no liability coverage was provided*; rather, the lender could declare the car a loss, repossess the car, and cancel the debt, or at its sole discretion, repair the car, paying the costs of repair directly to the body shop. (*Id.* at p. 850.) Presumably, the lender would not agree to pay repair costs if they made the loan unprofitable.

The court determined that the purpose of the debt cancellation program was to protect the lender's security interest in the cars it finances. (*Garamendi,* 114 Cal.App.4th, p. 855.) That purpose—protecting the lender's security interest—was a "secondary objective" effectuated through either third-party insurance or the loss damage waiver program; the program was in furtherance of the "primary objective of [the lender's] transactions"—i.e., the lender's financing of a used car purchase. (*Ibid.*) Key to its decision, however, was the lack of any risk-shifting: the court found that the arrangement could not be insurance because the lender did not agree to shift the buyer's risk to itself or anyone else; no risk was shifted from one party to another by the program. (*Garamendi,* 114 Cal.App.4th, pp. 856-857.)

Accordingly, *Garamendi* is distinguishable on the same grounds as *Truta.* Unlike the loss damage waiver program in *Garamendi*, the Protection Plan provides property coverage and shifts the renter's risk of property damage to A-1.

4. *Title Ins. Co. v. State Bd. of Equalization* (1992) 4 Cal.4th 715

Where the decisions in *Jellins, Truta,* and *Garamendi* turned on the lack of any risk assumption or risk shifting within insurance concepts, the

underwritten title companies in *Title Ins. Co. v. State Bd. of Equalization* (1992) 4 Cal.4th 715 were not in the business of insurance because the agreements lacked the element of risk distribution among similarly situated persons. (*Id.* at p. 726; but see *id.* at pp. 739-740 [insurers, not title companies, "are primarily and ultimately liable" under the insurance policy for the payment of claims, so no risk transferred] (dis. opn. of Kennard, J.).) Through an underwriting agreement, the title insurer and the underwritten title company "agreed to allocate the labor, risk, liability, and premium involved in the preparation and issuance of a contract of title insurance." (*Id.* at p. 725.) Under the agreement with the title insurer, the underwritten title company was obligated to pay some portion of claims made under the title insurance agreements between the title insurer and insured parties. (*Id.* at p. 720.) The underwritten title company was not a party to the insurance contract and only the licensed title insurer was authorized to issue title insurance. (*Id.* at p. 725.)

Analyzing the principal object of the underwriting agreement with respect to the title companies' assumption of risk, the Supreme Court determined the main function of the agreements was not to require the title company to provide insurance, "but instead to require the underwritten title company to perform a title search and examination carefully and diligently as well as to carry out the formalities involved in the issuance of title insurance policy." (*Title Ins. Co. v. State Bd. of Equalization, supra*, 4 Cal.4th at p. 726.)

The underwriting agreement was not a contract of insurance because it did not "distribute the risk of liability for claims among similarly situated persons" as required under Insurance Code section 22. (*Title Ins. Co. v. State Bd. of Equalization, supra*, 4 Cal.4th at p. 726.) "Under the contract, the underwritten title company agrees to indemnify the insurer for a portion

of its liability. There is no indication that the underwriting agreements distribute the risk among similarly situated title insurers." (*Ibid.*)

Unlike the indemnification provisions in the underwriting agreement, the Protection Plan allows A-1 to assume a risk of claims payment that is distributed among all similarly situated renters, who number more than 15,000 at any given time. (CT 206, ¶ 28.)

B. The Principal Object Inquiry Supports Regulation of A-1's Protection Plan

The court of appeal reasoned that the Protection Plan was not insurance subject to regulation under the Insurance Code because the "principal object" of the "entire transaction between the parties" was the rental of storage space. (Slip op., p. 10.) Because the Protection Plan was an "addendum" to the Rental Agreement and "would not exist and would have no purpose" without the Rental Agreement, the court of appeal looked "at the Rental Agreement and Protection Plan as a whole" and determined that the principal object of the entire transaction was the rental of storage space. (Slip op., p. 10.) Because, in its view, the primary objective of the Rental Agreement was storage rental, the court reasoned that the fact that the parties also contracted to allocate risk—whether through the indemnification clause or the Protection Plan—did not make the Protection Plan insurance. (Slip op., p. 10.) And because the Protection Plan was not insurance, the Insurance Code provisions barring unlicensed storage facilities from offering or selling insurance "in connection with, and incidental to, self-service storage rental agreements" (Ins. Code, § 1758.75) were inapplicable. (Slip op., p. 10.)

The court of appeal erred in its application of the principal object inquiry. While this Court in *Sweatman* decided that case based on statute, it also discussed the elements of the principal object inquiry in the course of

distinguishing the collision damage waiver provision held not to be regulated as insurance in *Truta*. As articulated by this Court in *Sweatman*, a court may consider, for example, whether the arrangement or transaction is comparable to existing types of insurance specifically regulated by the Insurance Code in determining whether the arrangement represents "merely 'a tangential risk allocation'" between the two contracting parties or, instead, "a spreading of the risk within insurance concepts." (*Sweatman*, *supra*, 25 Cal.4th at pp. 73-74.) In this case, the relevant factors weigh in favor of regulation.

First and foremost, the court allowed form to prevail over substance. Comparable insurance policies *do* exist and are sold separately to renters by authorized insurers. (CT 204, ¶19; CT 209, ¶ 40.) *Who* is selling the insurance should not determine whether it is insurance. As demonstrated in *Sweatman* and *Wayne*, the principal object inquiry does not operate to exempt a contract "sold as a secondary or incidental facet of a transaction with another, primary commercial purpose" from regulation under the Insurance Code if that contract represents the spreading of risk within insurance concepts. (*Wayne*, *supra*, 135 Cal.App.4th at p. 476; see *Sweatman*, *supra*, 25 Cal.4th at pp. 65 & 73-74 [distinguishing *Truta*, even though disability coverage was part of home loan program and acted as added security for the loan].) Contractual provisions can be insurance even when offered as "incidental" to a commercial transaction such as a package shipping agreement or a storage lease.

A-1's assumption of liability for loss or damage to the renter's personal property is not in furtherance of, or incidental to, any "service" under the Rental Agreement. A-1 is not servicing, renting, or buying the renter's personal property under the Rental Agreement. The Rental Agreement is a lease of A-1's real property, not a sale of goods or services. (See Slip op., pp. 14-15.) The subject of the Protection Plan is the renter's

personal property, not A-1's real property. The Protection Plan makes no promises regarding improved security services or anything else respecting A-1's obligations under the Rental Agreement to provide a storage unit; a renter who successfully declines enrollment in the Protection Plan still receives the same storage unit. Nor does the Protection Plan decrease the likelihood of disputes under the lease, for its claims process (or lack thereof) is more likely to lead to disputes than the standard disclaimers in the unmodified lease agreement.

As demonstrated in *Jellins* and its progeny, the key to the analysis is whether the arrangement represents the transfer and spreading of risk within insurance concepts. Here, the court of appeal mistakenly considered the Rental Agreement's indemnification clause to be the equivalent of the Protection Plan's provisions, characterizing both as methods for the parties to the Rental Agreement to allocate the risks incidental to their contractual relationship. (Slip op., p. 10.) They are not comparable. The indemnification clause in the Rental Agreement merely absolves A-1 from any liability to the renter arising out of the contractual relationship. It is merely an allocation of risk by contractual agreement, and is not governed by the insurance laws. (*Jellins, supra,* 29 Cal.2d at p. 248 [providing comparable examples, including "[t]he lessee who agrees to hold his lessor harmless"].) In contrast, the Protection Plan obligates A-1 to act as an insurer. It shifts the renter's risk of property damage to A-1, obligating A-1 to pay costs incurred by the renter for loss or damage to the renter's property. The Protection Plan represents the transfer and spreading of risk within insurance concepts.

Sweatman also considered relevant the fact that the disability insurance coverage was offered separately, was required, and was not a simple matter of checking the box. (*Sweatman*, *supra*, 25 Cal.4th at pp. 73-74.) But "[e]ach contract must be tested by its own terms as they are

written, as they are understood by the parties, and as they are applied under the particular circumstances involved." (*Jellins, supra,* 29 Cal.2d at p. 248.) An arrangement or transaction may be subject to regulation as insurance even if it is as "simple" as the Protection Plan and offered in connection with, and incidental to, some other commercial transaction. (Ins. Code, § 1758.75; see *Wayne, supra,* 135 Cal.App.4th at pp. 471-472 & 475, fn. 3 [insurance offered in connection with package shipping services].)

C. This Arrangement Implicates the Very Evils the Insurance Code Was Designed to Address

Even if this Court were to determine that the principal object inquiry leads to inconclusive results, the Protection Plan should be regulated under the Insurance Code because the Protection Plan directly implicates the evils at which the regulatory insurance statutes were aimed. Here, A-1 is agreeing to shift the renter's risk of loss to itself for an additional, allegedly excessive consideration, implicating the need to ensure that the storage facility charges fair rates and will have sufficient reserves to meet its obligations. (Compare *Truta, supra,* 193 Cal.App.3d at p. 815 [no need for reserves when lessor simply agrees not to hold lessee liable].)

A-1 is in the business of selling insurance, and its customers should be protected by the laws that govern that business. During the five-year period preceding the lawsuit, A-1 netted about $1.6 million per year in Protection Plan premiums, while paying out only about $25,000 in Protection Plan claims per year. (1 CT 213, ¶¶ 49-51.) While A-1 has contracted for insurance with Deans & Homer, it need not have. And Deans & Homer claims it owes no duty to Heckart. (2 CT 302:22 – 303:3.) An insurer covers A-1 for claims made under the Protection Plan for a premium of 74 cents per renter per month, while a renter pays A-1 $10 per month. (1 CT 206, ¶ 28; 1 CT 207, ¶ 30.) Accordingly, renters are paying a rate that is

more than 13 and half times higher. (Ins. Code, § 1861.05 [requiring approval of insurance rates and prohibiting excessive or inadequate rates].) Although it would be required under the Insurance Code (Ins. Code, § 1758.72 [setting forth training requirements]; *id.*, § 1758.76 [requiring numerous disclosures]), A-1 employees are not given instruction regarding ethical sales practices and A-1 does not inform its renters that the Protection Plan may duplicate coverage already provided under some other source of insurance coverage. (CT 213-214, ¶ 52.)

A-1 argues the Protection Plan presents no potential for abuse because it is comparable to a vendor who "makes promises reasonably addressing risks inherent in the [sales] relationship and over which the vendor has some control—like a shipper agreeing to pay up to a certain sum for damage to goods in its possession—the agreement is reasonably related to a non-insurance principal object." (A-1's Answer Brief on the Merits, p. 48.) Ironically, A-1 is describing an inland marine insurance contract like the one in *Wayne.* That insurance contract, like the insurance coverage A-1 is selling, is governed by the Insurance Code.

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CONCLUSION

The Commissioner respectfully requests that the Court clarify that the principal object inquiry does not create an exception to regulation expressly intended by the Legislature. Where the principal object inquiry is applied, it must serve, and not undermine, legislative intent.

Dated: September 11, 2017

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

I certify that the attached **BRIEF OF THE INSURANCE COMMISSIONER OF THE STATE OF CALIFORNIA, INVITED AMICUS CURIAE** uses a 13 point Times New Roman font and contains 6771 words.

Dated: September 11, 2017

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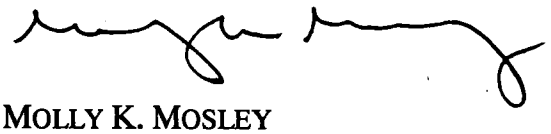

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DECLARATION OF SERVICE BY OVERNIGHT COURIER

Case Name: **Samuel Heckart v. A-1 Self Storage, Inc. et al.**

No.: **S232322**

I declare:

I am employed in the Office of the Attorney General, which is the office of a member of the California State Bar, at which member's direction this service is made. I am 18 years of age or older and not a party to this matter; my business address is: 1300 I Street, Suite 125, P.O. Box 944255, Sacramento, CA 94244-2550.

On September 11, 2017, I served the attached **BRIEF OF THE INSURANCE COMMISSIONER OF THE STATE OF CALIFORNIA, INVITED AMICUS CURIAE** by placing a true copy thereof enclosed in a sealed envelope with the GOLDEN STATE OVERNIGHT, addressed as follows:

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I declare under penalty of perjury under the laws of the State of California the foregoing is true and correct and that this declaration was executed on September 11, 2017, at Sacramento, California.

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