

Philadelphia Indemnity Insurance Co. v. Monte-Harris (S130717)

Arizona resident Alric Burke rented a car in California from Budget Rent-A-Car. As part of the transaction, Burke presented what appeared to be a valid Arizona driver's license, but the license had in fact been suspended more than two months earlier. At the time he rented the car, Burke purchased an insurance policy issued by Philadelphia Indemnity Insurance Company that provided \$1 million in third-party liability coverage, which was in "excess" of (or over) the minimum limits required by California's Financial Responsibility Law (\$15,000 per person and \$30,000 per accident for bodily injury or death). This so-called "excess liability policy," however, excluded coverage for injury arising out of the use of a rental car obtained through fraud or misrepresentation. Four days later, Burke got in a car accident that injured several people.

In a federal lawsuit, the district court entered judgment declaring that Philadelphia Indemnity had no liability for damages arising out of Burke's accident because: (1) Burke made at least a negligent misrepresentation to Budget that he had a valid driver's license; and (2) the excess liability policy excluded coverage for rentals obtained through misrepresentation. To help resolve the federal appeal of that judgment, we granted the Ninth Circuit Court of Appeals' request that we address the following question of California law: Does the duty of an insurer to investigate the insurability of an insured, as recognized in the California Supreme Court decision of *Barrera v. State Farm Mut. Automobile Ins. Co.* (1969) 71 Cal.2d 659 (*Barrera*), apply to an automobile liability insurer that issues an excess liability policy in the context of a rental car transaction?

Normally, California law allows an insurer to rescind an insurance policy if the person purchasing the policy (the insured) made misrepresentations in obtaining the policy. When the insurer is allowed to rescind an insurance policy, that means the policy may be declared void and unenforceable — as if it never existed — and the insurer does not have to pay the benefits owed under the policy. *Barrera* was a case that recognized an exception to this law. The *Barrera* decision essentially held that, even if misrepresentations were made, important public policy reasons justify limiting the right to rescind in cases involving automobile liability insurers, who issue policies that pay benefits when automobile drivers get in accidents that injure other persons using the streets and highways. For example, California's enactment of the Financial Responsibility Law demonstrates the state has a strong public policy favoring the compensation of persons injured in automobile-related accidents. Because of this and other public policy considerations, an insurer who sells this type of insurance cannot rescind a policy unless it conducted a timely and reasonable investigation of the "insurability" of the insured. Here, the persons injured by Burke argue that Philadelphia Indemnity should not be allowed to avoid its obligations to pay insurance benefits under the

excess liability policy it issued to Burke, because Philadelphia failed to undertake a timely and reasonable investigation (for example, through a DMV check) that would have led to the discovery of Burke's suspended driver's license.

In the present case there is a disagreement over whether, as in the *Barrera* case, the insurer should have an obligation to investigate insurability. Philadelphia Indemnity argues the *Barrera* rule should not apply in this case because unlike here, *Barrera* did not involve a rental car transaction or an accident that occurred only days after the policy's purchase. Moreover, the automobile liability policy in *Barrera* involved insurance benefits that fell within the minimum requirements of California's Financial Responsibility Law, while the policy here involves benefits that are in excess of that law's required amounts of \$15,000 per person and \$30,000 per accident. (Philadelphia claims the persons injured by Burke received the legally required monetary amounts from the company that rented the car to Burke.) Conversely, the persons injured by Burke argue the *Barrera* rule should apply because, as *Barrera* recognized, it would be unfair to allow insurers who did not investigate insurability to keep the money they received in payment for such policies but to not compensate the people injured by the drivers they insure.