California Supreme Court Rules Self-Storage Tenant-Protection Plans Aren't Subject to Insurance Code

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Update 4/24/18 – The Supreme Court of California ruled unanimously yesterday that self-storage tenant-protection plans don't constitute insurance. In *Heckart v. A-1 Self Storage Inc.*, the court determined the protection plan available to the plaintiff was "purely incidental" to the rental agreement and adjusted risks between A-1 and its tenants, meaning A-1 indemnified Heckart, not a third-party such as an insurance carrier.

In coming to a decision, the court applied a "principal object and purpose test" to determine whether protection plans fell under Article 22 of the California Insurance Code, which defines insurance as "a contract whereby one undertakes to indemnify another against loss, damage or liability arising from a contingent or unknown event," according to a source.

"A-1 assumes risks that arise directly from the rental relationship, and it does not provide indemnification beyond damages that might occur to property while it is stored in the rented space," wrote Chief Justice Tani G. Cantil-Sakauye, who authored the court's opinion. "Therefore, the protection plan has no purpose independent of the rental agreement, and is purely incidental to the rental agreement."

The court also pointed out that the protection plan was optional and extended "only to risks over which A-1 has some control, such as fires, roof leaks, criminal activity and damage to the building. A-1 can reduce these risks by taking steps to prevent fires or the spread of fires, to increase

security, and to strengthen the building. Therefore, the protection plan serves an additional purpose of providing an incentive to minimize the risks to stored property."

The justices also concluded that the "significantly" lower cost of the protection plan illustrated that the principal purpose of the transaction between Heckart and A-1 was for the rental of storage space.

In its opinion, the court rejected the CDI's interpretation of Article 16.3 of the insurance code, which argued the legislature could regulate protection plans as insurance. "The protection plan does not constitute insurance subject to regulation under the insurance code," Cantil-Sakauye wrote. "The legislature's enactment of Article 16.3 enables self-storage facilities to act as agents for insurance companies with respect to the narrow category of insurance described in Article 16.3, but it does not prohibit the parties' indemnification agreement set forth in the protection plan. Because plaintiff's claims are premised on his contention that the protection plan is subject to regulation under the insurance code, his claims fail."

The protection plan offered by A-1 provides $2,500 in protection for $10 per month, according to its website.

"The ruling affirms the lower courts' decision that tenant protection is not insurance," noted Jacquelyn Nash, director of On The Move Insurance Agency, which offers a tenant protection plan to self-storage operators. "We would like to thank both Brian Caster of A-1 Self Storage and Deans & Homer for vigorously defending tenant protection on behalf of the entire industry since April 2013. We could not be happier with this positive ruling and would also like to thank our customers for weathering the storm with us."

10/5/17 – Providers of self-storage tenant-protection plans received a potential blow last month when the California Department of Insurance (CDI) changed its previous stance on the definition of these programs in a legal brief filed in connection to the case *Heckart v. A-1 Self Storage Inc.*, which is currently before the state supreme court. At issue is whether protection plans constitute insurance.

In the brief filed Sept. 12, CDI reversed its "previous and long-standing legal position" that protection plans didn't equate to tenant insurance, according to a statement released by Deans & Homer, the insurance underwriter, agent and broker that provided A-1 with its template for selling protection plans.

"The specific issue before the court is does a self-storage facility's storage rental agreement offering an addendum under which the facility assumed liability for damage to stored property constitute insurance subject to regulation under the insurance code when the principal object of the agreement between the parties was the rental of storage space rather than the shifting and distribution of risk?" Deans & Homer officials said.

An Oct. 3 filing in rebuttal to the CDI brief by attorneys from Sheppard Mullin Richter & Hampton LLP, the law firm representing A-1 in the case, discredits the CDI's contentions, arguing that "the commissioner's views in the amicus curiae brief are not entitled to deference because no position or argument in the brief is grounded in the commissioner's expertise, technical knowledge or experience. Nor does the commissioner offer any facts that might assist the court in evaluating the dispute from a public policy perspective."

The A-1 brief also notes the California legislature hasn't taken any action to regulate protection plans and implores the court to reaffirm the December 2015 decision by the California Court of Appeal, which determined that the rental agreement and addendum in the A-1 case didn't constitute insurance regulated under the state's insurance code. "The addendum was dependent on the rental agreement whose principal object was the rental of storage space. Thus, the storage facility that offered the addendum did not engage in the unlicensed sale of insurance," justice James A. McIntyre wrote in the court's opinion.

"These determinations are in line with other cases in which courts have long affirmed the right of contracting parties to allocate risk within their agreements when incidental to the principal object of such agreements," Deans & Homer officials said. "Deans & Homer respectfully disagrees with opinions expressed by the California Department of Insurance in its amicus brief, and it strongly believes that the fundamental legal tenets that led to the development of this program are valid. Deans & Homer continues to believe that the protection program does not constitute insurance."

The lawsuit was filed by tenant Samuel Heckart, who rented a unit from A-1 in July 2012. "The protection plan reiterated terms of the rental agreement, including that the tenant assumed the sole risk of loss or damage to stored property, A-1 was not liable for loss or damage to stored property, and the tenant must insure his or her stored property," McIntyre wrote. The protection plan also stipulated that Heckart could pay $10 per month to have A-1 retain the liability for loss or damage to his property up to $2,500. Heckart initialed the plan's option to decline participation in the plan and acknowledged he was covered by his own insurance plan, according to the lower court's ruling.

Protection plans began to emerge in 2002 as an alternative to traditional self-storage tenant insurance. They've been used widely by facility operators in states that haven't granted storage businesses limited-lines licenses to sell tenant insurance. Among the biggest difference between coverage types is protection plans are a contractual relationship between the tenant and the storage operator, not the tenant and an insurance carrier.

Deans & Homer developed the concept of protection plans for the self-storage industry "after consultation with the legal division" of the CDI, according to the company's statement.

"The protection agreement is not insurance, it is not a warranty, and does not require the owner/operator to have an insurance license," according to Ted Dobbs, protection sales leader for Deans & Homer. "The agreement is part of the rental agreement and is simply the transfer of some limited liability for loss or damage to stored property back from the tenant to the owner in exchange for additional rent. The facility owner may retain all of the potential liability created by this agreement, or they may transfer part of or all of that risk to an insurance company by purchasing a separate policy of contractual liability insurance."

Based in Phoenix, Deans & Homer has more than 35 years of experience insuring the self-storage industry. The firm offers programs specifically for the protection of facility owners and tenants, including a package policy to protect the facility, direct mail-in tenant insurance and tenant-protection programs.

Sources:

Supreme Court of California, Heckart v. A-1 Self Storage
The Recorder, Self-Storage Company's "Protection Plan" Was Not Insurance Subject to State Insurance Code, California Supreme Court Rules

Court of Appeals of California, Fourth District, Division One, Heckart v. A-1 Self Storage

Inside Self-Storage, Self-Storage Protection Plans: Helping Tenants and Facilities Manage Risk