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Insurance Law

CONFLICTS OF LAW RAISE QUESTIONS OF COVERAGE

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OVER THE LAST several years, state and federal courts in New York have developed an increasingly uniform methodology for resolving conflicts of law underlying commercial insurance coverage disputes. To highlight this trend, this article presents a brief overview of New York choice of law rules for contracts cases while examining several recent decisions applying these rules to commercial coverage litigation.

Background

The operations and markets of even small businesses are rarely confined to a single state. A typical manufacturer may have its executive headquarters in Pennsylvania, a production facility in Ohio and distribution centers in Illinois, while its products are sold in all 50 states. A typical investment firm may have its headquarters in New York, a processing facility in New Jersey, and a network of registered representatives or brokers based around the country who solicit business in their home states.

Businesses may therefore be exposed to loss and liability in many different states, and numerous insurance products are available to protect them from such risk without regard to the location of the insured occurrence. In this environment, insurance coverage disputes frequently require courts to resolve conflicts of law to determine which state laws should be controlling.

The conflicts of law issue is particularly sensitive to the insurance bar given the significant disparities between the insurance laws of the various states. As a common example, New York law permits an insurer to decline coverage where notice of loss is not submitted within a "reasonable" time or as required under the policy, while California, Texas and other states will only uphold a "late notice" defense in many situations. As such, if a New York corporation fails to submit timely notice for a loss incurred in California, the corporation will inevitably argue for the application of California law while the insurer would be expected to champion New York law.

By way of background, New York courts will generally resolve conflicts of law in contracts cases with reference to the law of the state having a prevalence of "significant contacts" with the facts and circumstances at issue.[FN1] Within this context, increasing emphasis has been placed on accommodating any "governmental interests" or state policy considerations affected by the choice of law. The court's ultimate objective is to determine which state has the greatest "nexus" with the dispute, a process combining factual analysis with more abstruse value judgments.

Recent published decisions from state and federal courts in New York have established a practical framework for resolving conflicts of law as they pertain to insurance coverage disputes, which decisions largely address policies issued to corporations.

Specifically, New York courts have identified certain factors attendant to insurance coverage disputes as the “significant contacts” which should be given the most weight in determining applicable law. These relevant factors encompass the location of the insured risk; the insured's principal place of business; where the policy was issued and delivered; the location of the broker or agent placing the policy; where the premiums were paid; and the insurer's place of business.[FN2]

Notwithstanding the uniform criteria discussed above, the necessary analysis may not be reduced to a mathematical equation so that the state having the majority of contacts is automatically the source of applicable law. Rather, courts strive to discern the “center of gravity” for a given insurance contract, which may mean assigning disproportionate weight to a single contact if circumstances warrant.[FN3]

Similarly, policy considerations establishing a “center of gravity” in a given state may override numerous factual contacts with another state. This notion of a “center of gravity” is largely an abstraction and a true sense of how insurance conflicts of law are resolved is best developed through a review of prevailing precedent. To that end, the remainder of this article examines several recent New York decisions in this area.

‘Stolarz’

In Matter of Allstate (Stolarz v. Manufacturers Insurance Company),[FN4] the Court of Appeals determined that New Jersey law should be applied to interpret an automobile insurance contract issued by a New Jersey insurer to a New Jersey corporation, even though the vehicle was garaged in New York and the accident which precipitated the litigation occurred in New York.

Katherine Stolarz and her husband were injured in a two-car automobile accident in Woodbury, N.Y. on Feb. 1, 1989. Mrs. Stolarz was driving a vehicle leased by her employer, a New Jersey corporation, which she garaged at her home in New York. The vehicle was registered in New Jersey and insured by a New Jersey insurer under a policy issued to the employer. The Stolarzes sought additional coverage under the employer's policy.

The accident was apparently the fault of the other driver, whose insurer paid the Stolarzes $20,000, the full limit of liability under its policy. Thereafter, the Stolarzes sought additional coverage under the Blue Cross/Blue Shield policy issued to Mrs. Stolarz's employer.

Pursuant to an “uninsurance/underinsurance clause” in its policy, the employer's insurer contended that it was entitled to offset the $20,000 payment from the other driver's insurer against the $35,000 limit of liability it provided. Both the Supreme Court and the Appellate Division concluded that this issue presented a conflict between New Jersey and New York law, in that the former permitted such an offset while the latter held the offset to be void. Both courts went on to rule that New York law applied and that the offset was void, permitting the Stolarzes to recover the full limit of liability under the employer's policy.

The Court of Appeals reversed, emphasizing at the outset that there was no conflict of law since the offset was permissible under New York law as well as New Jersey law. Noting with disapproval the application of New York law by the lower courts, the court went on to instruct that New Jersey law should have been controlling in any event, suggesting that the “spectrum of significant contacts” indicated that New Jersey was the “center of gravity” of the case.

Despite its expansive language, the Court ultimately narrowed its focus to the five "significant contacts" delineated in the Restatement of Conflicts of Law[FN5] for contracts matters, being "the place of contracting, negotiation and performance; the location of the subject matter of the contract; and the domicile of the contracting parties."

The Court concluded that four of these five factors favored application of New Jersey law in that the policy was negotiated and made in New Jersey, the insured automobile was registered in New Jersey, and the parties were both New Jersey corporations. The only factor unrelated to New Jersey, place of performance, was characterized as "irrelevant" since there was "no issue as to performance."

The Court minimized the significance of any state policy considerations, reasoning that New York had little public interest in the enforcement of insurance contracts sold in New Jersey to a New Jersey corporation. While acknowledging that automobile insurance may implicate both the "private economic interests of the parties" and "governmental interests in the enforcement of its regulatory scheme," the Court suggested that, as a general rule, public policy considerations were more germane to resolving conflicts of law in tort cases.

The dissent harshly criticized the majority's opinion, accentuating the unpredictable analysis that conflicts of law issues may generate despite the judicial consensus as to the appropriate criteria for consideration.

The dissent especially complained that the majority ignored the "location of the risk," which is characterized as the "contact of prime significance." Since the car in question was garaged in New York at the Stolarzes' residence and an accident would be more likely to occur in New York, the dissent concluded that the "risk" was in fact located in New York.

Conversely, the dissent concluded that the majority relied excessively on the place of negotiation and delivery of the policy, which it described as having "relatively little significance" since the matters in dispute involved "performance" of a contract for the benefit of a New York resident rather than "interpretation" of the original contract language. The dissent asserted further that the majority failed to grasp that New York in fact has an important public interest in maximizing insurance benefits payable to one of its own residents.

The difference between the majority and minority opinions is attributable largely to the "public policy" issue. The majority minimized the importance of "public policy" considerations, focusing on the fact that a foreign corporation was the insured party. By contrast, the dissent was preoccupied with the beneficiaries under the policy, New York residents, and in effect treated the case as if the policy had been issued to them personally.

'Munzer'

The Third Department applied Vermont law to resolve a coverage dispute concerning liability for mercury pollution between a Minnesota insurer and an insured New York corporation, adopting a "significant contacts" analysis that focused heavily on Vermont's public interest in its environment.

In Munzer v. St. Paul Fire and Marine Ins. Co.,[FN6] a New York corporation purchased general liability policies for itself, four subsidiaries and two principal officers over a number of years. Each of the insured officers resided in New York, while one of the insured subsidiaries was a New York corporation. Both the parent company and the

subsidiaries maintained their principal place of business in Poultney, Vt., to where the policies were always forwarded and from where all premiums were paid.

Coverage was procured through a New York-based broker, although this individual traveled to the insureds' offices in Vermont to negotiate renewals each year. The insured corporation's only New York facility was an unheated warehouse used for storage several miles over the border. During certain of the years in question, the policies provided coverage to vendors based in various states, reflecting a nationwide distribution system for the insured's products that was not concentrated in any one area.

The court did not elaborate on the nature of the coverage dispute, which apparently involved claims arising from the discharge of pollution in Vermont. To resolve a conflict between unspecified New York and Vermont laws, the court applied a "significant contacts" analysis which focused on the insureds' business presence in Vermont and on that state's compelling interest in imposing "financial responsibility for mercury pollution in Poultney, Vermont."

The court concluded that Vermont was the jurisdiction "most intimately concerned with the outcome of the case" and held that Vermont law should be controlling. In so holding, the court minimized the insured's contacts with New York and emphasized that New York had no public policy interest in "what was essentially a Vermont problem."

'Schuster'

As noted above, the "significant contacts" doctrine requires consideration of state policy interests in addition to the strictly factual contacts with each state. While recognizing the importance of the latter, the court in Fireman's Fund v. Schuster Films Inc.[FN7] largely emphasized the importance of public policy considerations.

This case centered on an insurance policy issued to a movie studio for the production of "Rock 'N Roll Hotel," which policy included protection for lost or destroyed film footage. The insured studio was a New York corporation, but the policy was issued in California through a California insurance broker. The movie was to be filmed largely in Virginia with development and editing entrusted to Movielab, a corporation with laboratory facilities in California and New York.

After filming had proceeded for some three months, the production was shut down due to lack of funds. When production was resumed several years later, it was discovered that 38,000 feet of film from the original shoot had been lost or destroyed by Movielab at an unknown location. Thereafter, the insured delayed nearly 14 months before providing notice of loss to the insurer.

In the ensuing litigation, the insured studio contended that California's "prejudice" requirement should be a condition for the late notice defense, while the insurer advocated the application of New York's antithetical standard that timely notice of loss is a condition precedent for coverage regardless of any prejudice to the insurer.

As a threshold inquiry, the court examined the "intention" of the contracting parties as manifested by the policy language, noting that there was no "forum selection" clause in the policy. Concluding that there was "nothing probative" as to the parties intentions and that such would not be dispositive in any event, the court turned to a significant contacts analysis, placing particular emphasis on competing state interests.

The court observed that the policy was delivered to a New York insured and that at least a portion of the risk, being the stored film, was located there. Moreover, the court noted

that while the insurer was a California corporation, it conducted business in all 50 states, including New York.

In this context, the court found that New York had a substantial interest in "promoting diligence" by its insureds as respects providing timely notice of loss, and that California had virtually no competing interest since the insured was a New York corporation. As such, the court applied New York's notice requirement and held that coverage was not available.

Conclusion

The cases described above represent only a small selection of recent decisions resolving conflicts of law underlying insurance coverage disputes. While the principles enumerated by these cases have been widely adopted, given the fact-sensitive nature of the relevant inquiry, the practitioner should orient his or her research toward locating the published decision based on the most closely analogous facts and circumstances to the matter he or she is litigating.

FN1. Auten v. Auten, 308 NY 155 (1954).

FN2. See, e.g., Olin Corporation v. Insurance Company of North America, 743 F.Supp. 1044 (SDNY 1990), aff'd 929 F2d 62 (2d Cir. 1991).

FN3. See, e.g., Employers Mutual Casualty Company v. Key Pharmaceuticals Inc., 871 F.Supp. 657 (SDNY 1994).

FN4. 81 NY2d 219 (1993).

FN5. See Restatement (Second) of Conflicts of Laws §188[2].

FN6. 203 AD2d 770 (3d Dept. 1994).

FN7. 811 F.Supp. 978 (SDNY 1993).

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8/28/95 NYLJ 5, (col. 1)

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