Consistent Patterns Help Inform the Analysis

# Choice of Law in Bad Faith Claims

By John G. O'Neill

**Choice of law questions are a recurring and often outcome-determinative issue in bad faith litigation. With so much riding on the determination, it is important for counsel to understand the relevant principles and the various ways in which courts apply them.**

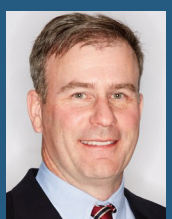
It is almost inevitable in modern practice, especially for attorneys who specialize in representing insurance companies, that they will encounter a dispute over which law governs a bad faith claim. In many cases, resolution of the choice of law issue can determine whether a plaintiff may maintain a bad faith claim against a client. This article is intended to provide a practical guide to analyzing conflict of laws issues in the context of bad faith litigation against liability insurers. (Unfortunately, bad faith claims arising out of property insurance, as well as underinsured, uninsured, and similar automotive coverages, are outside the scope of this discussion, and are excluded.) As will be seen below, the outcome of a choice of law analysis can depend upon the conflict of laws principles followed by the forum jurisdiction as well as the specifics of the claim advanced against the insurer.

## Analytical Framework

Although courts draw from a range of different principles to resolve conflict of laws issues in bad faith claims, they generally share a similar analytical framework. Usually, the first step is to determine whether there is an actual conflict between the laws of the competing jurisdictions. For example, conflicts have been found when the laws of the relevant states disagree over the following:

- Whether a third-party claimant is permitted to maintain a direct claim for bad faith against an insurer. *See Denham v. Farmers Ins. Co.*, 262 Cal. Rptr. 146, 147 (Cal. App. 1989).
- The level of misconduct that must be shown to recover. *See Mirville v. Allstate Indem. Co.*, 71 F. Supp. 2d 1106 (D. Kan. 1999).
- The types of recoverable damages. *See Ryder Truck Rental, Inc. v. UTF Carriers, Inc.*, 790 F. Supp. 637, 639–41 (W.D. Va.1992).

If a court finds that a conflict does exist, it will then typically move to the second step, which involves characterizing a bad faith claim as either an action in tort or in contract for the purposes of applying the forum state's corresponding conflict of laws principles. While this would seem to be a straightforward task, courts have sometimes struggled with characterization because claims for bad faith do not fit neatly into one category: tort or contract. As one court noted, "[t]he doctrinal roots of the obligation [of good faith] are notoriously elusive: one scholar has argued that



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actions for bad faith sound in 'conequitort,' suggesting the interaction among concepts of contract, equity, and tort." *Ryder Truck*, 790 F. Supp. at 641. *See also Ferrell v. Grange Ins.*, 354 F. Supp.2d 675, 677 (S.D. W. Va. 2005) (noting divergence of opinion whether bad faith claims sounded in tort or contract and evaluating choice of law issue under both analyses). Luckily, the issue has already been addressed in many jurisdictions, making it less likely that it will be a significant area of dispute.

Once a bad faith action has been characterized, the court will move to the third and final step in the analysis, which involves applying the corresponding conflict of laws principles as adopted by the forum state. A majority of jurisdictions follow the principles in the Restatement (Second) of Conflict of Laws (1971), though several jurisdictions continue to adhere to the Restatement (First) of Conflict of Laws (1934). A handful of jurisdictions apply other methodologies, such as the "choice-influencing considerations" developed by Professor Robert LeFlar, or the "governmental interests" approach developed by Professor Brainerd Currie. Courts are far from uniform in their application of these various choice of law principles to bad faith claims. Nevertheless, some general observations can be made that are helpful in analyzing choice of law issues in these types of matters.

## The First Restatement: "Vested Rights"

The traditional approach to resolving conflict of laws issues, sometimes referred to as the "vested rights" approach, is stated in the Restatement (First) of Conflict of Laws. The First Restatement has been criticized for being too mechanical in application and for sometimes selecting the laws of a jurisdiction that has little connection to the dispute. *See* William M. Richman and David Riley, *The First Restatement of Conflict of Laws on The Twenty-Fifth Anniversary of Its Successor: Contemporary Practice in Traditional Courts*, 56 Md. L. Rev. 1196, 1199 (1997). At present, only a small group of jurisdictions continue to adhere to the First Restatement approach.

### Torts: Lex Loci Delecti

Courts following the First Restatement approach to resolve choice of law issues for tort actions generally apply the rule of lex loci delicti. Under this rule, an action in tort is governed by the law of the place in which the wrongful conduct occurred. *See Restatement (First) of Conflict of Laws* §378 (1934); *American Guarantee & Liab. Ins. Co. v. Liberty Mut. Fire Ins. Co.*, 2014 WL 11514675, at *3 (D.N.M. March 24, 2014), *vac. in part on other grounds*, 2015 WL 11117309 (D.N.M. Feb. 17, 2015). Accordingly, if the forum state characterizes a bad faith action as a tort, it will generally follow the lex loci delicti rule to resolve choice of law issues and will seek to determine where the bad faith occurred.

Although the rule is fairly straightforward, applying it to a bad faith claim can be challenging. *See Pen Coal Corp. v. William H. McGee and Co., Inc.*, 903 F. Supp. 980, 983 (S.D. W.Va. 1995) (discussing the difficulty of identifying the place where the wrong occurs in a bad faith claim). Depending on the nature of the claim, the wrongful conduct could be said to have occurred in several locations: at the office of the insurer's adjuster, where settlement negotiations occur, where the underlying tort action is litigated, or where the insured feels the economic effect of the alleged misconduct. *See id.* Many courts that adhere to the First Restatement approach have attempted to address this problem by deeming the wrongful conduct to have occurred in the jurisdiction where the last event necessary to create liability occurs. *See* Restatement (First) of Conflict of Laws §377 (1934); *Morgan v. Government Employees Ins. Co.*, 2012 WL 4377790, at *4 (M.D. Fla. Aug. 22, 2012).

In *Morgan*, a Georgia insured brought suit against her insurer for negligently and in bad faith failing to settle an underlying personal injury lawsuit in Florida, resulting in a substantial excess verdict against her. *See* 2012 WL 4377790, at *1. The insured argued that the insurer's bad faith had been committed in Georgia for purposes of the lex loci delicti rule because that was where she resided and suffered injury, which was the last event necessary to make the insurer liable. *Id.* at *3. The court rejected this argument, holding that the insured had suffered injury in Florida when the court in the underlying litigation entered judgment against her in excess of her policy limit. *See id.* at *5–6 (ruling that insured incurred "damages beyond the damages contemplated in her insurance contract" upon entry of judgment). The court concluded that the insured's bad faith claims were governed by Florida law.

Although it would be tempting to think that the "last event necessary" rule routinely results in the application of the law of the jurisdiction in which the underlying action is litigated, this is not always the case. One federal court reached a very different conclusion following the "last event necessary" rule in determining which law governed bad faith claims arising out of a personal injury suit brought in Indiana against a Michigan insured. *See Bristol West Ins. Co. v. Whitt*, 406 F. Supp. 2d 771 (W.D. Mich. 2005) (applying Indiana choice of law principles). The insurer had disclaimed coverage or any obligation to defend the tort suit, which was then resolved by the insured through a settlement and consent judgment exceeding the policy limit. *See id.* at 778–79. Citing the insurer's lack of involvement in the Indiana suit and any settlement discussions that occurred in connection with it, the court declined to hold that Indiana law governed the claim. *See id.* at 788–89. Instead, the court found that the last act necessary to make the insurer liable had occurred at an earlier point in Michigan, where the insurer had sent letters wrongfully denying coverage for the tort suit. *See id.* at 788. Accordingly, the court concluded that the bad faith claim was governed by Michigan law.

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In *Calderon v. Melhiser*, 458 F. Supp.2d 950 (S.D. Ind. 2006), a Kentucky claimant who was involved in an automobile accident with an Indiana insured brought suit in Indiana, alleging negligence against the insured and bad faith against his insurer for failing to effectuate a settlement after liability became clear in violation of a Kentucky statute. The insurer moved to dismiss, arguing that the bad faith claim was governed by Indiana law, under which an insurer owes no duty to act in good faith to a third-party claimant. *See id.* at 952. Following the "last event necessary" approach, the court held that the bad faith claim, which was premised upon the failure to make a good faith effort to settle, occurred in Kentucky, where the claimant and the insurer's representatives were located and where the settlement negotiations occurred. *See id.* at 952–53. Therefore, the claim was governed by Kentucky law, and the claimant could proceed under the Kentucky statute. *See id.* at 953.

**Application of the lex loci contractus rule can lead to selection of the law of a jurisdiction that has only a tenuous connection to the events that give rise to the bad faith claim.**

### *Observations*

The lex loci delicti rule offers a straightforward, though not always predictable, method for resolving conflict of laws issues in bad faith actions. The law selected will depend upon the specific misconduct of the insurer as well as the harm suffered by the plaintiff. Claims involving an excess verdict are likely to be subject to the law of the jurisdiction where the tort claim was litigated. Claims that are actionable upon the happening of some other event, such as the breach of a statutory duty to extend a settlement offer or the wrongful refusal to provide coverage, may be governed by the law of a different jurisdiction, such as the jurisdiction where settlement offers or coverage decisions were (or should have been) made.

### Contracts: Lex Loci Contractus

Courts following the First Restatement approach to resolve choice of law issues for contract actions generally apply the rule of lex loci contractus. Under this rule, a dispute over the parties' rights under a contract is generally governed by the law of the state in which the contract was formed. *See* Restatement (First) of Conflict of Laws §346 (1934); *Ryder Truck Rental, Inc. v. UTF Carriers, Inc.*, 790 F. Supp. 637, 638 (W.D. Va. 1992). A forum that characterizes a bad faith action as sounding in contract will apply the lex loci contractus rule and will seek to determine where the insurance contract was entered.

In *Ryder Truck*, an insured that had settled an underlying personal injury litigation in Virginia brought claims in a Virginia federal court, seeking punitive damages against its insurer for bad faith in refusing to provide coverage for the underlying action. *See* 790 F. Supp. at 638. The insurer argued that the bad faith claims were governed by the law of Virginia, where the underlying litigation occurred, which did not permit recovery of punitive damages. *See id.* at 640–41. The insured maintained that its claim was governed by the law of Connecticut or New York, where the insurance contract was arguably entered, which authorized recovery of punitive damages in bad faith actions. *See id.* After determining that Virginia characterizes bad faith actions as contractual in nature, the court applied the lex loci contractus rule and held that the bad faith claims were governed by either New York or Connecticut law and that the insured could proceed against the insurer for punitive damages. *See id.* at 641–42.

A federal court in Kansas also applied the lex loci contractus rule to determine which law governed negligence and bad faith claims brought by automobile passengers against an insurer for failing to settle their personal injury action against the driver after an accident in Kansas. *See Mirville v. Allstate Indem. Co.*, 71 F. Supp.2d 1103 (D. Kan. 1999). The driver and the passengers, who were all from New York, had settled the personal injury claims with a consent judgment in excess of the policy limits and an agreement not to execute against the driver. The driver's insurer sought dismissal of the negligence claims, arguing that any action against it was governed by New York law, which required a showing of bad faith. *See id.* at 1107. Finding that it was undisputed that the insurance contract was entered in New York, the court ruled that the passengers' claims were governed by New York law and dismissed the negligence claim. *See id.* at 1108.

### Place of Contract Performance Rule

As can be seen from the *Ryder Truck* and *Mirville* decisions, application of the lex loci contractus rule can lead to selection of the law of a jurisdiction that has only a tenuous connection to the events that give rise to the bad faith claim. For this reason, and in view of the fact that the primary issues in bad faith claims are typically performance related as opposed to substantive, many states have moved away from strict application of the lex loci contractus rule and have instead applied an exception, the "place of performance" rule. Under this rule, when the dispute focuses on the manner or method of a party's performance, the claim is subject to the law of the place where that performance was to occur. *See* Restatement (First) of Conflict of Laws §358 (1934); *Moses v. Halstead*, 581 F.3d 1248, 1251 (10th Cir. 2009).

Determining the "place of performance" for an insurer's contractual obligations is again not always as simple as it might seem. As with the lex loci delicti rule, the place of performance could be said to be where the insurer's settlement or coverage decisions are made, where settlement negotiations occur, or where the underlying tort action is litigated. With some exceptions, decisions applying the "place of performance" rule have generally found that an insurer's obligations are to be performed where the underlying claim against the insured is brought and defended. *See Government Employees Ins. Co. v. Grounds*, 332 So.2d 13, 15 (Fla. 1976). As a result, these decisions have generally held that the bad faith claim against the insurer is governed by the law of the jurisdiction in which the underlying tort action is litigated.

In *MI Windows & Doors, LLC. v. Liberty Mut. Fire Ins. Co.*, 88 F. Supp.3d 1326 (M.D. Fla. 2015), a federal court considered whether a bad faith claim against an insurer for refusing to indemnify a Florida insured in connection with a judgment entered by an Alabama court was governed by Florida or Alabama law. The insured argued that application of the lex loci contractus rule resulted in Florida law governing its claims. The court noted, however, that the weight of Florida precedent held that a claim for bad faith "goes to… performance of the contract (or lack thereof)" and that it was therefore subject to the "place of performance" rule. *Id.* at 1328. The place of performance, the court observed, was typically found to be "where the [underlying] cause of action against [the insured] was maintained and defended by the [insurer]." *Id.* at 1331. Accordingly, the court concluded that the insured's bad faith claim was governed by the law of the state of Alabama, where the underlying action had been litigated. *Id. See also Government Employees Ins. Co. v. Grounds*, 332 So.2d 13, 15 (Fla. 1976) (applying "place of performance" rule to bad faith claim and determining that the place of performance was where underlying action was maintained and defended by insurer).

A similar result was reached in *Shin Crest Pte, Ltd. v. AIU Ins. Co.*, 2008 WL 728388 (M.D. Fla. March 17, 2008), in which the court found that Florida law governed a bad faith claim by a Taiwanese insured against its insurer arising out the insurer's settlement of claims brought against an additional insured in Florida. Although acknowledging that the insured's separate claim for coverage was governed by the law of Taiwan, where the insurance contract had been executed, the court held that the bad faith claim was a matter concerning the insurer's performance under the policy. *See id.* at *2. As such, the bad faith claim was governed by the law of the place of performance, which was Florida, where the underlying action had been maintained and defended. *See id. Accord Teachers Ins. Co. v. Berry*, 901 F. Supp. 322, 323 (N.D. Fla. 1995) (holding that claim against insurer for bad faith in failing to properly handle time-limit demand was governed by Florida law because that was where the underlying suit was brought against the insured and defended by the insurer, and where settlement negotiations occurred).

### *Merging the Lex Loci Contractus and the "Place of Performance" Rules*

While most jurisdictions following the First Restatement approach apply either the lex loci contractus rule or the "place of performance" rule, it should be noted that at least one decision has taken a slightly different approach and applied both rules. *See Moses v. Halstead*, 581 F.3d 1248 (10th Cir. 2009). In that case, a Kansas passenger brought suit against an insurer for failing to settle her claims against another Kansas resident for injuries that she suffered in a single-car accident that occurred in Missouri. After the insurer rejected her policy limits demand, the claimant filed suit and recovered an excess verdict against the driver in Missouri, and then brought suit against the insurer in Kansas for failing to settle her claims. The insurer argued that Missouri did not recognize a direct cause of action in favor of a claimant, and the claimant argued that her claims were governed by Kansas law.

The Tenth Circuit parsed the choice of law question into two components: (1) which state's law governed the existence of a duty of good faith, and (2) which state's law determined whether the insurer complied with any duty owed. *See id.* at 1252–53. As to the first issue, the existence of a duty, the court determined that it was substantive, and applying the lex loci contractus rule, found that it was governed by the law of Kansas, where the insurance contract was entered. *See id.* at 1254. As to the second issue, compliance with any such duty, the court found that it was performance related and governed by the law of the place of performance, which was also Kansas, where the claimant had made a settlement demand and the insurer had rejected it. *See id.* The court concluded that the claimant's bad faith claims were governed by Kansas law and that the claimant could therefore proceed against the insurer. *See id.*

### *Observations*

In the final analysis, the lex loci contractus rule normally selects the law of the jurisdiction where the insurance contract was entered, which may or may not have a significant connection to the matters at issue in the bad faith claim. The "place of performance" rule tends to select a state with a closer connection to the events giving rise to the bad faith claim. Similar to the lex loci delictis rule, predicting which law will be selected requires a careful examination of the nature of the insurer's misconduct and the claimed harm to the plaintiff. When the claim involves an excess verdict, there is a good chance that the "place of performance" will be the jurisdiction in which the underlying tort action was litigated. However, if the conduct at issue occurs before the filing of litigation or is sufficiently distinct from the underlying tort action, a court may find that the place of performance was in another jurisdiction.

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## The Second Restatement: Contacts and Policy Factors

A majority of jurisdictions follow the principles set forth in the Restatement (Second) of Conflict of Laws (1971), which provides a more nuanced approach to resolving choice of law issues. Under the Second Restatement, courts seek to determine which jurisdiction has the "most significant relationship" with the claim and the parties by evaluating various contacts with the competing jurisdictions in the context of several policy-based factors, which are intended to guide the choice of law deci-

sion. *See Dowis v. Mud Slingers, Inc.*, 621 S.E.2d 413, 415 (Ga. 2005). The factors include (1) the needs of the interstate system, (2) the relevant policies of the forum, (3) the relevant policies of other interested states and the relative interests of those states in the determination of the particular issue, (4) the protection of justified expectations, (5) the basic policies underlying the particular field of law, (6) the certainty, predictability, and uniformity of the result, and (7) the ease of the determination and application of the law to be applied. *See* Restatement (Second) of Conflict of Laws §6 (1971). The result is a complex, multi-step, balancing test that is less predictable and applied with considerably less uniformity than the analysis under the First Restatement. Shirley W. Wiegand, *Fifty Conflict of Laws "Restatements": Merging Judicial Discretion And Legislative Endorsement*, 50 La. L. Rev. 1, 4 (2004). As will be seen below, this is particularly the case with bad faith claims.

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**Torts: Section 145 Contacts Analysis**

Courts characterizing a bad faith claim as tortious in nature look to Restatement (Second) of Conflict of Laws §145 (1971). Section 145 governs torts generally, and it lists the following contacts to be taken into consideration when resolving choice of law issues:

1. The place where the injury occurred;
2. The place where the conduct causing the injury occurred;
3. The domicile, residence, nationality, place of incorporation, and place of business of the parties; and
4. The place where the relationship, if any, between the parties is centered.

Restatement (Second) of Conflict of Laws §145 (1971).

The relative importance to be assigned to each of these contacts depends upon the nature of the claim asserted. *See id.* at cmt. f. Although these contacts might in theory point to a number of different jurisdictions, as a practical matter, the analysis typically boils down to the question of whether a bad faith action is governed by the law of the state in which the underlying action against the insured was litigated or by the law of the state in which the insured or claimant is located.

In *Adams v. Rubin*, 964 F. Supp. 507 (D. Me. 1997), the court faced the question of whether a bad faith claim brought by Massachusetts claimants against a New York insurer for failing to settle an underlying legal malpractice action in Maine was governed by the law of Massachusetts, which permits third-party claims against insurers, or of Maine, which does not. In conducting a Section 145 contacts analysis, the court gave great weight to the fact that the claimants were Massachusetts residents and that they felt the effect of the alleged misconduct by the insurer in Massachusetts. *See id.* at 509. Although acknowledging that the claim arose out of the alleged misconduct of defense counsel in Maine, where the malpractice claim was litigated, the court emphasized its view that the primary issue was "the manner in which a New York insurance company proceeded with settlement of a claim made by Massachusetts residents." *Id.* at 510. The court ruled that because Massachusetts has an interest in protecting its citizens from unfair claims-settlement practices, and because Maine did not have a connection to the parties or a more significant interest in having its law applied, Massachusetts law would govern the claim. *See id.*

In *West American Ins. Co. v. RLI Ins. Co.*, 698 F.3d 1069 (8th Cir. 2012), the court was required to decide whether claims by an excess insurer against a primary insurer for failure to settle were governed by the law of Kansas, where the insured purchased coverage, or the law of Missouri, where an underlying personal injury claim was arbitrated, resulting in an excess verdict. Noting that the excess insurer stood in the shoes of its insured for purposes of its claim, the court evaluated various contacts under Section 145 as though the claim had been brought by the insured. *See id.* at 1073. The court found that the insured was located in Kansas and suffered injury there and that these contacts favored the application of Kansas law. *See id.* The court rejected the primary insurer's argument that the conduct causing the injury occurred in Missouri, where the arbitration was held, because the bad faith claim focused upon the insurer's failure to settle before the commencement of suit, and there was no evidence that any of the pre-suit negotiations occurred in Missouri. *See id.* The court also observed that Kansas's interest in protecting its residents from misconduct by insurers outweighed any contrary interest that Missouri might have in ensuring that litigants make good faith attempts to settle, particularly when the alleged misconduct occurred before any suit was filed in that state. *See id.* at 1073–74. Accordingly, the court concluded that Kansas law governed the excess insurer's claim. *See id.*

As shown in the cases discussed above, when a court places greater weight on the location of the insured/claimant and the place where the injury occurred (which

are typically the same state), the Section 145 analysis is likely to result in the selection of the law of the state in which the insured/claimant is located. However, as will be seen below, when a court does not place weight on these contacts, or the facts make these contacts less important, the Section 145 analysis is more likely to favor application of the law of the place where the underlying lawsuit occurred.

Such was the case in *American Guarantee and Liability Ins. Co. v. U.S. Fidelity & Guar. Co.*, 668 F.3d 991 (8th Cir. 2012), which involved a suit by an excess insurer against a primary insurer for bad faith failure to settle an underlying personal injury action that resulted in an excess verdict. The court conducted a Section 145 contacts analysis to determine whether the bad faith claim was governed by the law of Washington, where the insured had been headquartered, or in Missouri, where the tort action had been litigated. *See id.* at 996. The insured corporation had been dissolved several years before the entry of the adverse verdict, and this factored heavily into the court's analysis. *See id.* at 997–98. In evaluating the first contact, the court concluded that the dissolution of the insured weighed against the selection of Washington as the place where the injury occurred. *See id.* at 997–99. The court noted that the second contact, the place where the conduct causing the injury occurred, pointed toward Missouri because nearly all of the settlement discussions occurred there. *See id.* at 999. The third contact, the place of the parties, did not favor Washington or Missouri because neither of the insurers were located in those states, and as noted, the insured had been dissolved. *See id.* at 1000. The court found that the final contact favored Missouri because the relationship between the two insurers was centered in that state, due to the underlying litigation. *See id.* at 1001. It also found that the Section 6 policy factors, previously listed above, favored application of Missouri law because Washington would have little interest in the application of its law to a dispute between litigants who were not residents of the state. *See id.* at 1002. Therefore, the court ruled that the bad faith claim was governed by Missouri law.

A similar result was reached in *West Side Salvage, Inc. v. RSUI Indemnity Co.*, 2016 WL 6124637 (S.D. Ill. Oct. 17, 2016), in which the court considered whether a claim against an insurer for refusing in bad faith to settle, resulting in an excess verdict, should be governed by the law of the state in which the insured was located, Iowa, or by the law of the state where the underlying personal injury action was litigated, Illinois. In applying Section 145, the court ruled that the first contact, the place where the injury occurred, did not favor application of Iowa law because the insured had not paid the excess verdict for which it sought recovery. *See id.* at *5. It further found that the disparate locations of the parties, with the insured in Iowa and the insurer in New Jersey, did not weigh in favor of either jurisdiction over Illinois. *See id.* The court determined that the remaining contacts, the place where the conduct causing the injury occurred and the place where the parties' relationship was centered, both favored Illinois because Illinois was the location where the case was litigated, and where any opportunity for settlement occurred, and also the location of the "relevant" relationship between the parties regarding the litigation. *See id.* Considering the Section 6 factors, the court ruled that Illinois had a greater interest in having its law applied than Iowa or other jurisdictions and that application of Illinois law was predictable and met the parties' expectations. *See id.*

Another consideration that can influence the outcome of a Section 145 analysis is the nature of the bad faith claim. The cases discussed above all involved an insurer's alleged failure to settle a claim against an insured. When the alleged bad faith arises out of other conduct, such as an allegedly wrongful refusal to provide coverage, a contacts analysis under Section 145 may be less focused upon the location in which the underlying claim was litigated and more likely to point toward the jurisdiction in which the insured is located.

This was the case in *Aspen Specialty Ins. Co. v. Technical Indus., Inc.*, 2015 WL 339031 (W.D. La. 2015). There, the court considered whether an insured's claims for bad faith against its insurers for wrongfully denying coverage were governed by the law of Texas, where the underlying action was litigated, or Louisiana, where the insured was located. In conducting a Section 145 contacts analysis, the court found that the place of injury was Louisiana, where the insured was located, and that the conduct causing the injury did not occur in Texas. *See id.* at *4. The court further found that none of the parties was located in Texas and that the parties' relationship was centered in Louisiana, "where the insurance policy was presumably negotiated, issued and delivered." *Id.* Lastly, the court noted that the insured seemed to expect that Louisiana law would apply, since it had couched its bad faith claims, in part, upon the violation of a Louisiana statute. *See id.* The court concluded that Louisiana law governed the bad faith claims against the insurers. *See id.* at*5.

A similar ruling was made on a slightly different issue in *T-Mobile USA, Inc. v. Selective Ins. Co. of America*, 2016 WL 1464468, at *1 (W.D. Wash. April 14, 2016), which considered whether a claim for bad faith refusal to afford coverage to a company claiming additional insured status was governed by the law of Washington, where the additional insured was located, or New Jersey, where the named insured was located. Acknowledging that there was a divergence in judicial opinions on the subject, the court first determined that the place of injury contact weighed "slightly" in favor of Washington, the location of the additional insured. *See id.* at *10. It went on to find that the place where the wrongful conduct occurred favored New Jersey, where the insurer made and communicated its decision to deny a defense. *See id.* at *11. According to the court, the location of the parties was neutral: the additional insured was located in Washington, and the insurer was located in New Jersey. *See id.* Noting that the policy had been issued and delivered to the named insured in New Jersey and the insurer's rejection of the additional insured's tender occurred there, the court determined that the parties' relationship was centered in New Jersey. *See id.* Because it found the most significant contacts between the additional insured and the insurer were in New Jersey, the court ruled that the bad faith claim was governed by New Jersey law. *See id.* at 12.

Of course, there are no absolutes in choice of law, and at least one court has reached the opposite conclusion, finding that an insured's claim for bad faith refusal

to pay the full hourly rate of independent counsel was governed by the law of the state in which the underlying action was litigated. *See IMS Health Inc. v. Zurich American Ins. Co.*, 2015 WL 9653012 (Pa. Com. Pl. Dec. 15, 2015). In that case, the insurer argued that the claim was governed by the law of Connecticut, where the insured was headquartered, while the insured argued that it was governed by the law of Pennsylvania, where the claim was pending. In its conflicts analysis, the court found that Pennsylvania was the place of injury because that was where the insurer was supposed to defend the insured from the underlying claim, but had not done so. *See id.* at *6. For largely the same reasons, the court also found that the place of the injurious behavior was Pennsylvania. *See id.* Although the court found that the location of the parties favored Connecticut, because this was where the insured was headquartered, it found that the parties' relationship was centered in Pennsylvania, due to the pending litigation. *See id.* The court also noted Pennsylvania's interest in protecting insureds doing business in the state, without specifically discussing any countervailing interests of Connecticut. *See id.* The court concluded that Pennsylvania law governed the bad faith claim.

**For claims involving** an excess verdict, the Section 145 contacts will often point toward either the location of the insured/claimant or the location of the underlying litigation.

***Observations***

Section 145 permits a flexible, fact-driven analysis of choice of law issues for bad faith claims that often turns upon the specific circumstances of a case. For claims involving an excess verdict, the Section 145 contacts will often point toward either the location of the insured/claimant or the location of the underlying litigation. If greater weight is given to the place of injury and the location of the insured/claimant, the analysis is likely to select the law of the jurisdiction in which the insured/claimant is located. If greater weight is instead given to the place where the wrongful conduct occurred and the place where the parties' relationship was centered, the analysis is more likely to select the law of the jurisdiction in which the underlying action was litigated. For other types of claims, such as bad faith in refusing to provide coverage, the analysis is more likely to select the law of the jurisdiction in which the insured is located. Although the choice of law analysis is supposed to include evaluation of the Section 6 policy factors, any discussion of these factors is usually limited to confirming that the law selected by the Section 145 contacts is appropriate.

**Contracts: Section 188 (and Sometimes Section 193) Contacts Analysis**

Jurisdictions that characterize a bad faith action as contractual in nature will apply Restatement (Second) of Conflict of Laws §188 (1971). Section 188 includes the following contacts to be considered:

1. The place of contracting;
2. The place of negotiation of the contract;
3. The place of performance;
4. The location of the subject matter of the contract; and
5. The domicile, residence, nationality, place of incorporation, and place of business of the parties.

Restatement (Second) of Conflict of Laws §188(2) (1971). These contacts are to be evaluated according to their relative importance with respect to the particular issue. *Id.*

Application of a Section 188 contacts analysis is demonstrated in *AT&T Wireless Svcs., Inc. v. Federal Ins. Co.*, 2007 WL 1849056 (Del. Sup. June 25, 2007), which considered which law governed a claim for bad faith refusal to defend an insured in connection with a shareholder action arising out of a merger. The parties disputed whether the bad faith claim was governed by the law of Virginia, where the insured had been located before the merger, or Washington, where the newly merged entity was located. Noting that the policy was issued to the insured in Virginia and incorporated Virginia amendatory endorsements, the court found that the place of contracting was Virginia. *See id.* at *4. Turning to the place of performance, the court rejected the parties' arguments in favor of Washington and Virginia and instead found that this contact favored Delaware, where the underlying suit was litigated and where a defense to the insured was due. *See id.* at *5. The court found that the third contact, the location of the subject matter of the contract, weighed in favor of Virginia because the policy insured the conduct of the directors, and the conduct that formed the basis for the underlying lawsuit occurred in that state. *See id.* at *6. After finding that the final contact, the location of the parties, also favored Virginia, the court concluded that Virginia law governed the bad faith claim. *See id.*

Although the *AT&T* court relied solely upon Section 188 to determine the law governing a bad faith claim, other courts have sometimes incorporated Section 193 into the choice of law analysis. Section 193 addresses the law governing insurance contracts and provides:

> The validity of a contract of fire, surety or casualty insurance and the rights created thereby are determined by the local law of the state which the parties understood was to be the principal location of the insured risk during the term of the policy, unless with respect to the particular issue, some other state has a more significant relationship under the principles stated in §6 to the transaction and the parties, in which event the local law of the other state will be applied.

Restatement (Second) of Conflict of Laws §193 (1971).

In *Bristol West Ins. Co. v. Whitt*, the court conducted a mixed Section 188 and Section 193 analysis to determine whether a claim for bad faith denial of coverage and failure to settle brought by a insured was governed by the law of Michigan, where the insured resided, or Indiana, where an underlying tort action arising out of an automobile accident was litigated. *See* 406 F. Supp.2d 771, 785–86 (W.D. Mich. 2005) (applying Indiana choice of law principles). The court found that the place of contracting

for the insurance policy was Michigan, where the "application [was] made, the premium [was] paid, and the policy [was] delivered." *Id.* at 786–87. Although noting that the policy appeared to have been issued from Ohio, the court downplayed the significance of the place of negotiation, noting that this contact was less important because the parties did not meet in person. *See id.* at 787. The court found that the place of performance was normally "where the funds from the policy would be put to use," which would be Indiana, but that this factor was to be given little weight because at the time of contracting it was "uncertain or unknown." *Id.* In evaluating the location of the subject matter of the contract, the court looked to Section 193 of the Restatement, which provides that a policy is to be governed by "the local law of the state which the parties understood was to be the principal location of the insured risk." *Id.* The court observed that for automobiles, this is normally where the vehicle is "principally garaged" at the time the policy is issued, which in this case was Michigan, the state in which the insured resided. *See id.* Because the majority of contacts weighed in favor of Michigan, the court concluded that to the extent that the bad faith claim sounded in contract, it was governed by Michigan law.

The court in *Schwartz v. Liberty Mut. Ins. Co.*, 539 F.3d 135, 152 (2d Cir. 2008), also conducted a mixed analysis under Sections 188 and 193. At issue was whether bad faith claims brought by two excess insurers (as equitable subrogees of the insured) were governed by the law of California, where the policy was issued and where the named insured maintained the majority of its operations, or New York, where the underlying securities class action was litigated and where many of the insured company's executives worked. Evaluating the location of the insured risk under Section 193, the court found that some contacts, such as the issuance of the policy and the presence of a majority of the company's employees in the state, pointed to California, while the fact that all but one of the company's executives worked in Manhattan pointed to New York. *See id.* at 152. Because the insurance covered risks spread throughout several locations, the court concluded that Section 193 was not determinative. *See id.* The court next evaluated the location of the subject matter under Section 188, which it framed as referring to the subject matter of the bad faith claim, not the subject matter of the insurance policy. *See id.* The court easily found that the majority of events relevant to that claim, such as the underlying litigation, mediation, settlement conferences, and the insurer's alleged failure to settle, occurred in New York. *See id.* The court also held that New York had a greater interest in applying its law, which afforded primary insurers greater latitude in handling claims, and that application of California's lower standard for imposing liability would offend New York's policy choice. *See id.*

#### *Observations*

On balance, the Section 188 contacts tend to favor application of the law of the jurisdiction in which an insured is located. A court that evaluates all of the contacts in the context of a bad faith claim brought by an insured is likely to reach this conclusion. If a bad faith claim is brought by a third party, or if a court limits its analysis to a few of the contacts, it may be more likely to find that the claim is governed by the law of another jurisdiction, such as the state where the underlying litigation occurred.

### Other Approaches: Policy-Focused Analyses

While a majority of jurisdictions follow one of the Restatements to resolve choice of law issues, a few jurisdictions follow other approaches, such as the "governmental interests" approach, or the "choice-influencing considerations" approach. These approaches share some similarities with the Second Restatement in that they consider many of the same factors and involve weighing the interests of competing jurisdictions.

#### The "Governmental Interests" Approach

Under the "governmental interests" approach, a court analyzes the interests of the competing states to determine the law that most appropriately applies to the issues in a case. *See Dowis v. Mud Slingers, Inc.*, 621 S.E.2d 413 414–15 (Ga. 2005). In performing the analysis, a court will (1) identify the law in each state bearing on the disputed issue, (2) determine policies that the laws were designed to serve, and (3) determine how those policies are affected by each state's contacts with the litigation and the parties. *See Woessner v. Air Liquide Inc.*, 242 F.3d 469, 472 (3d Cir. 2001); *McCann v. Foster Wheeler LLC*, 225 P.3d 516, 527 (Cal. 2010). Then the court evaluates the strength of each jurisdiction's interest in the application of its own law to determine which state's interests would be more impaired if its law were not applied. *See id.*

Application of the "governmental interests" analysis is demonstrated in *Denham v. Farmers Ins. Co.*, 262 Cal. Rptr. 146, 147 (Cal. App. 1989), where the court considered which law governed a bad faith action by California residents against the insurer of a Nevada resident who had injured them in an automobile accident in Nevada. The court first determined that there was a conflict between the law of California, which permits third-party bad faith claims, and Nevada, which does not. *See id.* at 148. The court next determined that there was a "true" conflict because each of the states had an interest in the application of its law. *See id.* California had a legitimate interest in protecting its residents from unfair practices by insurers, and Nevada had an interest in protecting its insurers from third-party claims, which were not permitted in the state and which would adversely affect insureds by increasing the costs of insurance. *See id.* Undertaking a "comparative impairment" analysis, the court considered the fact that the California decision that authorized third-party bad faith claims had recently been overturned, which suggested that the policy underlying the rule was no longer as strongly held. *See id.* at 149. The court determined that application of California law would abrogate Nevada's interest in the application of its law to a claim involving an insurance policy written in Nevada, insuring a Nevada resident for an accident that occurred in that state, and for alleged insurer misconduct that occurred in that state. *See id.* Accordingly, the court concluded that Nevada law governed the bad faith claim.

Another court applied a similar analysis in *Geo. M. Martin Co. v. Royal Ins. Co. of America* when it evaluated whether a bad faith claim brought by a California insured

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over an excess verdict entered in a Minnesota litigation was governed by California or Minnesota law. *See* 2006 WL 3804379 (D. Minn. Dec. 22, 2006) (applying California law). The court determined that a conflict existed because California permits recovery of punitive damages and damages for emotional distress, while Minnesota limits recovery to the amount of the excess verdict. *See id.* at *4. However, the court found that this was not a "true" conflict because the policy behind Minnesota's law was not to deny claimants full recovery but to protect Minnesota residents from "excessive financial burdens or exaggerated claims." *Id.* at *5. Because the defendant insurer was not located in Minnesota, the state had no interest in the application of its law. *See id.* In contrast, the court found that California had a strong interest in the application of its law to protect California insureds and to deter wrongful conduct against them. *See id.* at *6. Accordingly, the court resolved the choice of law question in favor of California law.

### The "Choice-Influencing Considerations" Approach

The "choice-influencing considerations" approach involves evaluation of five factors, including: (1) predictability of results, (2) maintenance of interstate and international order, (3) simplification of the judicial task, (4) advancement of the forum government's interests, and (5) application of the better rule of law. *See Bell v. Kansas City Fire and Marine Ins. Co.*, 616 F. Supp. 1305, 1306 (D. Ark. 1985). The weight attached to each of these choice-influencing considerations varies with the facts of each case. *See* Mark Thomson, *Method or Madness: The Leflar Approach To Choice Of Law As Practiced In Five States*, 66 Rutgers L. Rev. 81, 89 (2013).

In *JSI Indus., Inc. v. Steadfast Ins. Co.*, a court applied the "choice-influencing considerations" approach to resolve a choice of law question about whether a bad faith refusal to defend was governed by the law of Wisconsin, where the insured was located, or the law of Minnesota, where the underlying lawsuits had been prosecuted. *See* 2004 WL 1088334, at *1 (D. Minn. May 13, 2004). In evaluating the predictability of results, the court noted that "an insurer should expect courts to apply law of the state where the incidents giving rise to the obligation to defend occurred," and determined that this consideration favored application of Minnesota law. *Id.* at *2–*3. Turning to the maintenance of interstate order, the court found that this consideration did not favor either jurisdiction because both had substantial contacts with the claim; the insured was based in Wisconsin, and the underlying litigation occurred in Minnesota. *See id.* at *3. The next factor, simplification of the judicial task, did not weigh in favor of either state's law because the court was able to apply both laws properly. *See id.* The fourth consideration, advancement of the forum's governmental interest, favored application of Minnesota law, as the state's interest in policing insurance agreements and its decision not to recognize a claim for bad faith prevailed over the countervailing policy of Wisconsin. *See id.* Finding that two considerations weighed heavily in favor of the application of Minnesota law and that none of them weighed in favor of Wisconsin law, the court ruled that there was no need to consider the last factor, the better rule of law, which applied only when the first four factors did not resolve the issue. *See id.* at *4. The court concluded that the bad faith claim was governed by Minnesota law.

### Observations

The policy-focused analyses utilized in the "governmental interests" and "choice-influencing considerations" tests makes it difficult to draw any firm conclusions about the law that they are likely to select in the context of a bad faith claim. It is worth noting that both approaches have been criticized as permitting judges to favor application of the law of the forum over competing jurisdictions. *See* Gregory E. Smith, *Choice of Law in The United States*, 31 Hastings L. J. 1041, 1048–49 (1987). Closely analyzing the laws at issue and the policies that underlie them is necessary to evaluate the likely outcome for any given dispute.

## Conclusion

At first blush, conflict of laws issues in bad faith cases can seem perplexing, but they do not have to be. Counsel must understand how the forum characterizes bad faith claims and the choice of law principles that it follows. While, as discussed above, there is some variation in the way that courts apply choice of law principles in bad faith cases, there are some consistent patterns that help inform the analysis. Understanding these patterns and applying them to the specific facts of a case should enable counsel to provide a thoughtful analysis of any choice of law issue.