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## **Court Of Appeals Holds That Insured's Failure To Cooperate Limits Coverage To The Financial Responsibility Minimum Of The State Where The Accident Occurred, Not Where Contract Was Issued**

By Timothy Bahorski

In *Farm Bureau Ins Co v Abalos*, \_\_\_ Mich App \_\_\_, released for publication October 18, 2007, the Michigan Court of Appeals hold that, although Michigan law governed the interpretation of the policy, which law allowed the insurer to reduce the coverage available to the insured as a result of the insured's noncooperation, the minimum coverage to be provided would be determined by the law of the state where the accident occurred.

The case arose out of an accident occurring in Ohio between the Castellanos, Ohio residents, Marco Abalos, a Michigan resident. The Castellanos filed suit in Ohio against the Abalos seeking recovery for injuries received in that accident. The Abalos failed to answer the Ohio lawsuit. Farm Bureau then sought a declaratory judgment that, because of the Abalos' lack of cooperation, Farm Bureau had no duty to defend or indemnify the Abalos under its insurance policy. Alternatively, Farm Bureau requested a declaration that reduced the Abalos' policy limits to Michigan's residual liability coverage \$20,000. The trial court concluded that Farm Bureau did not have a duty to defend or indemnify the Abalos but the Castellanos defendants were entitled to Michigan's statutory residual liability coverage. Farm Bureau appealed.

On appeal, the Court of Appeals affirmed, holding that the Abalos' failure to cooperate with Farm Bureau was not a defense to the extent that residual liability insurance is compulsory, but modified the trial court's ruling that the minimum amount of residual liability to the Castellanos is governed by Michigan's financial responsibility law.

### **Choice of Law:**

The first issue was which state's law would apply. Farm Bureau argued that the case should be treated as a hybrid action sounding in contract and tort. This argument was rejected by the court, which found that Farm Bureau did not seek a declaration regarding tort liability, but only its contractual obligation to pay insurance benefits

### **SECRET WARDLE NOTES:**

The decision is noteworthy in two respects. First, it clarifies that a declaratory judgment action regarding the scope of coverage under an insurance policy is a matter of contract law to be subject to contract conflict of laws analysis. Second, it clarifies which financial responsibility law will apply to determine the scope of coverage under that policy, namely it will be the law of the state where the injury occurs.

## CONTINUED...

to an Ohio resident whose vehicle was struck in Ohio by a vehicle owned and operated Michigan residents. The Court of Appeals noted that it was the Abalos' alleged failure to cooperate, not the automobile accident in Ohio, that was the triggering event for this lawsuit. The Castellanos' interest in the action, the court continued, arose only from their potential ability to reach insurance benefits available under plaintiff's insurance policy. Thus, the Court of Appeals concluded, the trial court properly treated this action as strictly a contract action.

### Failure to Cooperate:

Having determined that Michigan law would govern the interpretation of the contract, the court then addresses the impact of the insured's failure to cooperate on the scope of coverage under that contract. The Court of Appeals noted that, under Michigan, an insured's failure to cooperate with an insurer is not a valid defense against a third party seeking residual liability insurance benefits to the extent that the residual liability insurance is compulsory. Therefore, they agreed with the trial court that the Castellanos were entitled to residual liability insurance benefits. But because the involved accident occurred in Ohio, not Michigan, the Court of Appeals had to decide whether the applicable financial responsibility law would be that of Michigan or Ohio.

To answer this question, the Court of Appeals examined Michigan's statute, MCL § 500.3131(1) that reads:

Residual liability insurance shall cover bodily injury and property damage which occurs within the United States, its territories and possessions, or in Canada. This insurance shall afford coverage equivalent to that required as evidence of automobile liability insurance under the financial responsibility laws of the place in which the injury or damage occurs. In this state this insurance shall afford coverage for automobile liability retained by section 3135. [Emphasis is that of the court.]

The Court of Appeals notes that, under this statute, the scope of residual liability insurance is determined by the financial responsibility laws of the place where the injury occurs. Therefore, and because the accident occurred in Ohio, the court concluded, it follows that Ohio's financial responsibility law must be applied to determine the amount of compulsory residual liability insurance that is not subject to the defense of noncooperation.

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