**The Fifth Circuit, Again, Certifies a Duty to Defend Extrinsic Evidence Question to the Texas Supreme Court**

**This time it will be difficult for the Texas Supreme Court to Avoid Addressing the Issue**

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            Under the Texas eight-corner duty to defend rule, an insurer’s duty to defend is determined by comparing the four-corners of the policy with the four-corners of the plaintiff’s pleadings. Assuming the allegations in the pleadings to be true, if they invoke coverage under the policy, then the insurer owes a duty to defend.

A recurring issue in Texas Insurance law, however, involves the role of evidence outside of the pleadings, i.e., “extrinsic evidence,” in determining an insurer’s duty to defend. On the one hand, for insureds, it is possible that extrinsic evidence could invoke coverage under the policy that is not implicated under the allegations of the pleadings. On the other hand, for insurers, utilizing extrinsic evidence might allow them to deny a defense in cases not justified solely by the allegations in the pleadings.

One area in which these questions arise involves the timing of an incident when the allegations in the pleadings are silent on the subject. Indeed, in *Bitco General Ins. Co. v. Monroe Guaranty Ins. Co.,* the date of the incident was undisputedly prior to the inception of the Monroe Guaranty policy; however, the allegations in the pleadings were silent in that regard. After the district court refused to consider the extrinsic evidence and held that Monroe Guaranty owed a duty to defend, Monroe Guaranty appealed that decision to the Fifth Circuit Court of Appeals. In its Orders of March 12, 2021, the Fifth Circuit  certified the questions surrounding the possible use of extrinsic evidence to decide whether the insurer owes a duty to defend to the Texas Supreme Court.

The Texas Supreme Court began taking an interest in the potential utilization of extrinsic evidence to determine the duty to defend in 2006 in *GuideOne Elite Ins. Co. v. Fielder Road Baptist Church,* 197 S.W.3d 305 (Tex. 2006). In *GuideOne,* the insurer of a church being sued for the alleged sexual harassment of one of its ministers could show by extrinsic evidence that the minister had left the church prior to the inception of its policy and so, it filed a declaratory judgment action seeking a declaration that it did not owe the church a duty to defend. *Id.* at 307. The Texas Supreme Court recognized that although some of Texas’ courts of appeals had carved out certain exceptions to the eight-corner rule, the Texas Supreme Court had never done so. *Id.* at 308.

The Texas Supreme Court considered adopting a “true-facts” exception to the eight-corner rule in order to prevent the rule’s recurring use as a tool for fraud; however, rejected it because the record did “not suggest collusion or the existence of a pervasive problem in Texas with fraudulent allegations designed solely to create a duty to defend.” *Id.* at 311. In the end, the Texas Supreme Court refused to consider the extrinsic evidence and held that the insurer owed the church a duty to defend. *Id.* at 311. It is interesting to note that four members of the court, including then Justice Don Willett (now a Fifth Circuit judge), joined in a concurring opinion, which commented that there was “no need to consider what exceptions the [eight-corner] rule might have, and given the importance of this difficult issue, I would express no opinion on it.” *Id.* at 314.

Next up at the Texas Supreme Court on extrinsic evidence and the eight-corner duty to defend rule was *Pine Oak Builders, Inc. v. Great American Lloyds Ins. Co.,* 279 S.W.3d 650 (2009). This unanimous decision, in an opinion authored by then Justice Don Willett, analyzed whether to consider extrinsic evidence showing that the subcontractor’s work exception to the “your work” exclusion for completed operations was invoked to preclude the application of the exclusion to deny a defense to the insured. *Id.* at 653. In other words, the refusal to consider extrinsic evidence deprived the policyholder from a defense in a situation in which the insurer owed a duty to indemnify. *Id.* at 655-56. The Texas Supreme Court held that while extrinsic evidence may be important in determining the insurer’s duty to indemnify, it is irrelevant in determining the duty to defend. *Id.*

In the 2019-2020 Texas Supreme Court term, the Court heard two cases regarding the eight-corner rule for determining an insurer’s duty to defend. While the Texas Insurance Law bar braced for the potential of a wholesale change about the role or non-role of utilizing extrinsic evidence to determine an insurer’s duty to defend under Texas law, the results of the two cases hardly registered a whimper in terms of developing the law on this issue.

The first of the two cases, *State Farm Lloyds v. Richards,* 2019 WL 4267354 (5th Cir. 2019), came to the Texas Supreme Court by certified question from the Fifth Circuit and it analyzed whether the absence of the policy language requiring an insurer to defend its insured when the allegations are “groundless, false and fraudulent” permits an insurer to consider extrinsic evidence to seek a denial of a defense obligation. The Texas Supreme Court simply ruled that there was not a plain language exception to the 8-corner rule.

The second of the two cases, *Avalos v. Loya Ins. Co.,* 2018 WL 3551260 (Tex. App.—San Antonio 2018, pet. granted) involved whether an auto insurer can rely on extrinsic evidence to withdraw from a defense of its policyholder in a car wreck case when it learns that the insured and the third-party suing the insured colluded to falsely represent that an excluded driver, and not the insured, was driving the car at the time of the accident to create coverage that would not otherwise exist. Here, the Supreme Court of Texas, for the first time ever, specifically recognized an exception to the "eight corners" rule, holding that extrinsic evidence is admissible to determine the duty to defend in the very limited situation when undisputed evidence demonstrates that the insured and the third-party suing the insured collude to make false representations in a suit to create coverage that would not otherwise exist.

In the parallel universe of the federal courts deciding insurance cases under Texas law, the Fifth Circuit has predicted that if the Texas Supreme Court were to recognize an exception to the eight-corner rule, it would be the narrow *Northfield* exception “when it is initially impossible to discern whether coverage is potentially implicated *and* when the extrinsic evidence goes solely to a fundamental issue of coverage which does not overlap with the merits of or engage the truth or falsity of any facts alleged in the underlying case.” *Northfield Ins. Co. v. Loving Home Care, Inc.,* 363 F.3d 523, 531 (5th Cir. 2004) (emphasis in original).

With this background, the Fifth Circuit has certified the following questions to the Texas Supreme Court:

1. Is the exception to the eight-corners rule articulated in *Northfield Ins. Co. v. Loving Home Care, Inc.*, 363 F.3d 523 (5th Cir. 2004), permissible under Texas law?
2. When applying such an exception, may a court consider extrinsic evidence of the date of an occurrence when (1) it is initially impossible to discern whether a duty to defend potentially exists from the eight-corners of the policy and pleadings alone; (2) the date goes solely to the issue of coverage and does not overlap with the merits of liability; and (3) the date does not engage the truth or falsity of any facts alleged in the third party pleadings?

As noted by the Fifth Circuit panel: “[r]eceiving a definitive answer to this question is important because ascertaining the date of an occurrence is a frequently encountered “gap” in third party pleadings. Tactically, the omitted date can be key to the question of the duty to defend the underlying suit.”

                As a practical matter, these coverage questions, unanswered by the pleadings, also arise in a variety of different contexts including whether a particular vehicle is covered and whether a person is actually insured under the policy.

Texas Insurers are definitely encouraged that the proposed exceptions to the anti-extrinsic evidence rule will allow them to deny defenses and coverage. There are many jurisdictions that only allow the use of extrinsic evidence to invoke a duty to defend and not to permit an insurer from denying a defense. Also, if extrinsic evidence is allowed to be considered, that result will significantly increase the use of declaratory judgment actions in the denial of defenses.

Next up will be whether, as expected, the Texas Supreme Court accepts the certified question. Its ruling on whether to accept the certified questions will be announced as part of their weekly orders handed down on Fridays while they are in term. If the Texas Supreme Courthears the arguments of the case during this current term (that goes until July), its internal policy is to decide the case and render its opinion during this term. Conceivably, the fact that this certified question comes in so late in the term may delay the court from considering the case until next term (beginning in August).