

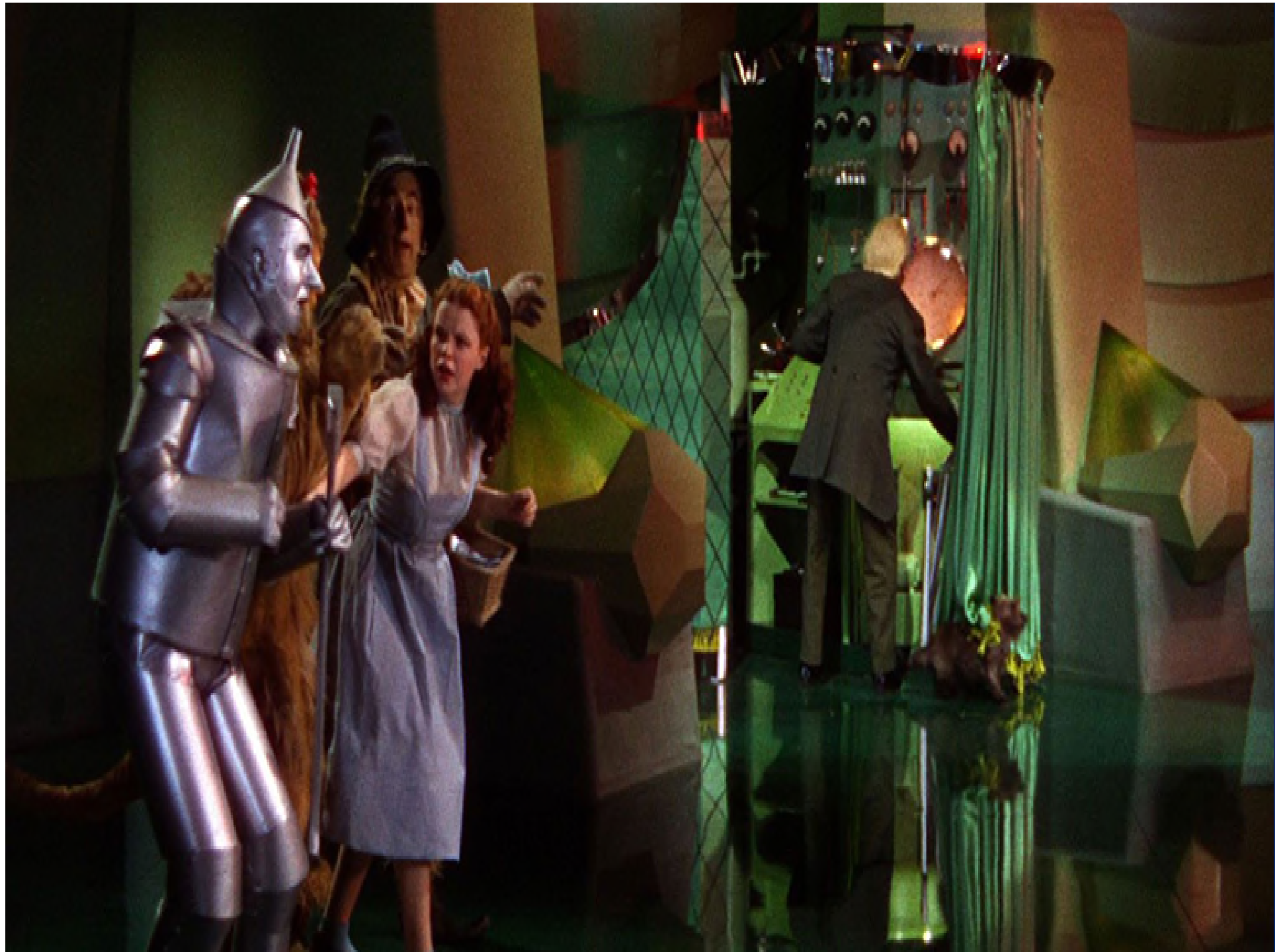
# Peeking Behind the Curtain: Use of Extrinsic Evidence in the Duty to Defend

Robert J. Witmeyer  
Cooper & Scully, P.C.  
900 Jackson Street, Suite 100  
Dallas, TX 75202  
Telephone: 214-712-9554  
[rob.witmeyer@cooperscully.com](mailto:rob.witmeyer@cooperscully.com)

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# EIGHT CORNERS RULE

- Duty to defend in Texas is generally based upon the four corners of the lawsuit and four corners of the insurance policy.
- Is this an inflexible rule?
- Exceptions for extrinsic evidence?



# EARLY SUPREME COURT AUTHORITY

- Early Texas Supreme Court authority made no mention of and did not consider the use of extrinsic evidence. The earliest case, *Heyden Newport Chem. Ins. Co. v. Southern Gen'l Ins. Co.* (1965), referred only to the eight-corners rule implying that only the pleadings and the policy could be considered.

## TEXAS COURTS PERMIT EXTRINSIC EVIDENCE IN LIMITED CIRCUMSTANCES

- *International Service Ins. Co. v. Boll*, 392 S.W.2d 158 (Tex. Civ. App.--Houston [1st Dist.] 1965, writ ref'd n.r.e.)
- *Cook v. Ohio Cas. Ins. Co.*, 418 S.W.2d 712 (Tex. Civ. App.--Texarkana 1967, no writ)
- *State Farm Fire & Cas. Co. v. Wade*, 827 S.W.2d 448 (Tex. App.--Corpus Christi 1992, writ denied)

# EXCEPTION IN FEDERAL COURTS

- “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).

# EXCEPTION IN FEDERAL COURTS

- *Ooida Risk Retention Grp v. Williams*, 579 F.3d 469 (5th Cir. 2009) (allowing extrinsic evidence in the absence of sufficient allegations to determine application of fellow employee exclusion)
- *Star-Tex Resources, LLC v. Granite State Ins. Co.*, 553 F. Appx 366 (5th Cir. 2014) (allowing consideration of extrinsic evidence to in absence of sufficient allegations to determine application of auto exclusion)
- *Evanston Ins. Co. v. Kinsale*, 7:17-cv-327(S.D. Tex. July 12, 2018) (“[T]he Court also agrees with Defendant that this is a situation in which the extrinsic evidence exception applies. The alleged date of construction goes solely to a fundamental issue of coverage and does not implicate the merits or depend on the truth of the facts alleged.)

## EXTRINSIC EVIDENCE ALLOWED

- Who Is An Insured
- Who Is An Additional Insured
- Exclusions
- Date of Loss



# TEXAS SUPREME COURT TRILOGY

- *GuideOne Elite Ins. Co. v. Fielder Road Baptist Church*, 197 S.W.3d 305 (Tex. 2006)
- *Zurich Am. Ins. Co. v. Nokia, Inc.*, 268 S.W.3d 487 (2008)
- *Pine Oak Builders v. Great American Lloyds*, 279 S.W.3d 650, 655 (Tex. 2009)

# RULE #1

- Rule #1-Extrinsic evidence will not be allowed to contradict specific allegations in the pleading. In both *GuideOne* as well as *Pine Oak*, there were specific pleadings that went to the coverage issue that was involved. In *GuideOne* it was the dates of employment of Evans. In *Pine Oak*, it was allegations that the home had been built by *Pine Oak* and not by subcontractors. In *GuideOne* the court noted that “the extrinsic evidence here concerning Evans’ employment directly contradicts the plaintiff’s allegations that the Church employed Evans during the relevant coverage period.” In *Pine Oak*, the supreme court noted that “the extrinsic fact Pine Oak seeks to introduce in this coverage action contradicts the facts alleged in the Glass suit.” Therefore, it is clear that extrinsic evidence will not be allowed to contradict specific pleadings to the contrary.

# RULE #2

- Rule #2-Extrinsic evidence will be allowed only when relevant to independent and discrete coverage issue, not touching on the merits of the underlying third-party claim. In the *GuideOne* decision, the supreme court also referenced the rule announced in *Northfield Ins. Co. v Loving Home Care, Inc.* That decision referenced the rule set out above plus added another requirement: “when it initially impossible to discern whether coverage is potentially implicated.” However, when the Texas Supreme Court was reiterating its *GuideOne* decision holding in the *Pine Oak* decision, it omitted this element. This distinction is important. The Supreme Court seems to say that extrinsic evidence may be allowed if it does not touch on the merits of the underlying case, even if the parties are initially able to discern whether coverage is implicated.

## RULE #3

- Rule #3-Extrinsic evidence will be admitted to both create coverage as well as to defeat coverage. Pine Oak argued that a different rule should apply when a party was trying to use extrinsic evidence to create coverage than when extrinsic evidence was being used to defeat coverage. The court held that “[t]his distinction is not legally significant.”

# RULE #4

- Rule #4-Extrinsic evidence may be used if collusion can be shown. This exception was referenced in both *GuideOne* (“the record before us does not suggest collusion. . . .”) and *Pine Oak* (“Our analysis in *GuideOne Elite* did not consider whether an exception to the eight-corners rule might exist where the parties to the underlying suit collude to make false allegations that would invoke the insurer’s duty to defend, because the record did not indicate collusion.”) It should be pointed out that collusion does not equate to false allegations in the petition. The plaintiff may try to plead the case in the coverage and allege facts that are known to be false. The insurer in this case still has a duty to defend even if the allegations are false or fraudulent. Collusion in the context of *GuideOne* and *Pine Oak* means an agreement between the plaintiff and the insured in the underlying case. The involvement of the insured is essential to trigger the collusion exception.

# RULE #5

- Rule #5-The traditional burden of proof issues will apply. The insured initially has the burden of showing that the case falls within the coverage. The insurer will have the burden of showing the application of an exclusion or breach of a condition. What does this mean? In a case where there is no date alleged as to the bodily injury or property damage, the insured would have the burden of bringing forth evidence showing the date of the bodily injury. Similarly, if the injured plaintiff is an employee of the insured but there are no allegations in the petition, the insurer should have the burden of bringing forth extrinsic evidence showing the application of the employee exclusion. If the party with the burden of proof fails to bring forth the evidence where the pleading is silent, summary judgment will be appropriate against that party for failing to carry their burden.

# RULE #6

- Rule #6-If the pleadings are silent, there will be no duty to defend until the insured brings forward evidence establishing that bodily injury occurred within the policy period. The insured cannot wait until the end of the case and then present the evidence to the insurer and argue that there was a duty to defend from the initial tender even though the extrinsic evidence had not been tendered. If the pleadings are silent, no duty to defend will commence until the extrinsic evidence has been proffered. Likewise, if there are no allegations regarding whether the injured plaintiff was an employee of the insured, the insurer would have an obligation to defend until it presented evidence regarding the plaintiff's employment status.

# Rule #7

- Rule #7-What if the insurer and insured produce extrinsic evidence that is contradictory? It is not the policy where the rules of construction would apply. No Texas court has addressed this particular situation. However, consistent with the rules governing the duty to defend, if there is credible extrinsic evidence that would arguably create a duty to defend, the insurer must defend.



# RULE #8

- Rule #8-Under Texas law, an insurer has no duty to attempt to search out extrinsic evidence that would potentially create a duty to defend. However, the issue arises as to what is the duty of the insurer if it discovers credible extrinsic evidence that would trigger a duty to defend, even if the burden of producing such evidence is not on the insurer. Under the duty to defend Texas law has imposed no such duty on the part of the insurer. However, consistent with the duty to defend if there is potentially a cause of action stated, the insurer would have a duty to defend if the evidence was credible.

# EXAMPLE #1

- Worker suffers tragic death on construction project in 2016.
- Estate sues general contractor in 2018 and does not allege DOL.
- General contractor had Insurer A from 2010-2014, Insurer B from 2015-17, and Insurer C from 2018-present.
- All three insurers receive a tender from general contractor/insured.
- Texas is an actual injury/injury-in-fact trigger state (i.e., when the injury actually happens).
- Which carrier(s) should defend?

## EXAMPLE #2

- Petition alleges that Plaintiff was injured on worksite.
- Plaintiff sues general contractor and employer/subcontractor/insured who is a non-subscriber to workers compensation in Texas.
- The policy contains the standard employer's liability exclusion (no coverage for bodily injury that occurs in the course and scope of employment).
- Can we use extrinsic evidence if the petition alleges (incorrectly) that the general contractor is the employer and not the subcontractor?

# EXAMPLE #3

- Petition alleges property damage to a single-family house. No dates of property damage alleged.
- Plaintiff sues general contractor. GC sues subcontractor/insured.
- The policy contains prior completed work exclusion.
- Job file establishes sub completed work in 2014.
- Certificate of occupancy for project issued in 2015.
- Insurer comes on the risk in 2016.
- Can we use extrinsic evidence to deny defense?

## TWO NEW TXSC CASES – *State Farm v. Richards*

- Jayden Meals was killed in an all-terrain vehicle accident while under the temporary care of his grandparents, the Richards. Jayden's mother sued the Richards in Texas state court, essentially alleging they were negligent in failing to supervise and instruct Jayden. The Richards sought a defense from State Farm Lloyds pursuant to their homeowner's insurance policy.

# Richards

- Insurance policy required State Farm to provide a defense “[i]f a claim is made or a suit is brought against an insured for damages because of bodily injury . . . to which this coverage applies, caused by an occurrence.”
- State Farm initially defended this suit pursuant to a reservation of rights, but later sought a declaration that it had no duty to defend or indemnify the Richards. In a summary judgment motion, State Farm argued that two exclusions barred coverage.

# Richards

- The first, the “motor-vehicle exclusion,” exempts coverage for bodily injury “arising out of the . . . use . . . of . . . a motor vehicle owned or operated by or loaned to any insured.” The policy defines “motor vehicle” to include an “all-terrain vehicle . . . owned by an insured and designed or used for recreational or utility purposes off public roads, while off an insured location.” The policy defines “insured location” to mean “the residence premises.”

# Richards

- In support of its summary judgment motion, State Farm attached a vehicle crash report showing that the accident occurred away from the Richards' premises, as well as the Richards' admissions that the accident occurred off an insured location.



# Richards

- The district court permitted extrinsic evidence and granted summary judgment for State Farm. The district court also held that State Farm had no duty to indemnify.

# Richards

- According to the district court, the eight-corners rule does not apply if a policy does not include language requiring the insurer to defend “all actions against its insured no matter if the allegations of the suit are groundless, false or fraudulent.”
- Fifth Circuit certified to TXSC based upon policy language.

## *Loya Insurance Company v. Avalos*

- Loya issued policy to wife but specifically excluded husband.
- Claimants and husband got into an accident.
- Claimants and husband agreed that Claimants would file suit that alleged wife caused accident.
- Wife agreed to plot, until after her husband died and shortly before her deposition.

# Loya

- Based on the wife's admission that she knowingly lied about driving the insured vehicle to secure coverage and avoid the named driver exclusion, Loya considered any coverage forfeited, denied the claim, and withdrew its defense of Guevara in the underlying lawsuit.

# Loya

- Despite their complicity in the fraud, Claimants pursued their claim against wife and obtained a default judgment awarding them \$450,343.34, prejudgment interest, and costs. Wife assigned her rights against Loya to Claimants.
- Claimants filed suit against Loya.

# Loya

- Claimants, as assignees, alleged (1) negligent claims handling, (2) breach of contract, (3) breach of the duty of good faith and fair dealing, and (4) violations of the Texas Deceptive Practices Act.
- Trial court granted summary judgment in favor of Loya.
- But appellate court reversed, relying upon eight corners rule. Loya appeals to TXSC.

# QUESTIONS?

Rob Witmeyer

214-712-9554

[rob.witmeyer@cooperscully.com](mailto:rob.witmeyer@cooperscully.com)