Insurer's Duty to Defend in Texas: The Eight Corners Rule

University of Houston Law Foundation
Advanced Insurance Law

February 20 - 21, 2003: Houston, Texas
February 27 - 28, 2003: Dallas, Texas

Presented by:
Robert M. (Randy) Roach, Jr.
rroach@cookroach.com

COOK & ROACH, L.L.P.
1111 Bagby Street, Suite 2650
Houston, Texas 77002
(713) 652-2800
(713) 652-2029 Fax

COOK & ROACH, L.L.P.
1004 West Avenue
Austin, Texas 78701
(512) 656-9655
(512) 479-5910 Fax

Table of Contents

I. SCOPE OF ARTICLE . . . 1

II. GENERAL PARAMETERS OF DUTY TO DEFEND AND THE EIGHT CORNERS RULE . . . 1

A. Duty to Defend vs. Duty to Indemnify . . . 2

B. Standard Policy Wording Comprising Duty to Defend in Insurance Contract . . . 3

C. General Application of the Duty to Defend . . . 4

III. RULES OF CONSTRUCTION GOVERNING INSURANCE CONTRACTS . . . 5

A. General Rules of Contract Construction . . . 5

B. Special Rules of Contract Construction Applicable to Insurance Contracts . . . 7

C. "Eight Corners" Rule of Construction Applicable to Duty to Defend . . . 8

D. Eight Corners Rule in Action - - Duty to Defend Denied on Factual Allegations of Pleading . . . 9

E. Eight Corners Rule in Action - - Duty to Defend Imposed on Factual Allegations of Pleading . . . 10

IV. FACTUAL SPECIFICITY MEETS NOTICE PLEADING . . . 11

A. Historical "Fact" Pleading vs. Current "Notice" Pleading . . . 11

B. Liberality of "Notice" Pleading and the Duty to Defend . . . 12

C. Liberality of "Notice" Pleading vs. Preclusive Effect of Declaratory Judgments . . . 13

D. Duty to Defend by Amended Pleading - - *Reser* Case . . . 14

E. *Griffin* Finality Defeated by Subsequent Amendment of Pleadings? . . . 15

V. WHEN THE PLEADING IS INADEQUATE TO DETERMINE DUTY TO DEFEND. 15

A. Extrinsic Evidence on Coverage Facts Not Affecting Insured's Liability. 17

B. Extrinsic Evidence on Coverage Facts Overlapping with Liability Issues. 19

C. Practical Application of Extrinsic Evidence Exemplified. 20

D. Texas Supreme Court Interest in Resolving Extrinsic Evidence Question. 21

E. Extrinsic Evidence of Policy Drafting History to Determine Duty to Defend. . . 22

VI. CONCLUSION. 23

Insurer's Duty to Defend in Texas: The Eight Corners Rule

I. Scope of Article

This paper examines the development, purpose and application of the "Eight Corners" rule for determining an Insurer's Duty to Defend a Policyholder against third-party liability claims under Texas law.[1] The Eight Corners rule prescribes that courts look to the "four corners" of the precipitating pleading together with the "four corners" of the insurance policy wording, only, in deciding whether the factual allegations made against the Insured potentially are within the coverage afforded by the insurance. If so, the Insurer must defend the Insured; if not, no Duty to Defend is owed.

The scope of this paper includes:

- Reviewing the origin of the Duty to Defend in the insurance contract and examination of its practical application;
- Outlining the rules of contractual construction which have been developed by Texas courts regarding insurance policies generally and the Duty to Defend specifically;
- Following the development of the Eight Corners rule under Fact pleading and noting the potential complications this historical evolution poses under modern Notice pleading rules; and
- Examining the propriety of utilizing extrinsic evidence to augment the Eight Corners rule in circumstances where the pleading is unclear or simply does not allege facts sufficient to determine whether the policy potentially provides coverage.

II. General Parameters of Duty to Defend and the Eight Corners Rule

The Duty to Defend is, in the first instance, a creature of the contract between Insurer and the Policyholder. It is dependent upon and is defined by the particular wording of the insurance policy which comprises that contract. The scope of the Insurer's undertaking to defend its Insured - - as reflected in policy wording - - has changed relatively little over the years.

As further developed by Texas courts, the Insurer's Duty to Defend is said to be governed

---

[1] Throughout this Paper we refer to the "Policyholder" as an equivalent to an "Insured," referring to any person or entity entitled to insurance coverage; the term Insurer refers to any level or type of insurer involved in a policy that includes a duty to defend, unless otherwise specified.

solely by the "Eight Corners" rule, i.e., by the "four"corners of the contract (the insurance policy wording) in conjunction with the "four" corners of the pleading asserting a claim or suit against the Policyholder. The "Eight Corners" rule is sometimes also referred to as the "Complaint Allegation" rule.

When the pleading against the Insured squarely alleges matters that are clearly within or clearly outside the scope of coverage afforded by the insurance policy, the doctrine remains pristine. In those cases, courts are likely to rigorously enforce the Eight Corners rule by refusing to consider any information or evidence extrinsic to the pleading and policy wording. The picture is not quite so clear, however, when the allegations of the pleading and the wording of the policy do not neatly conform with each other nor cancel each other out.

When the alleged cause of action is neither clearly outside nor clearly within coverage, "the insurer is obligated to defend if there is, potentially, a cause under the complaint within the coverage of the policy." *Heyden Newport Chemical Corp. v. Southern General Insurance Co.*, 387 S.W.2d 22, 26 (Tex.1965). If there is doubt as to whether the complaint states a covered cause of action, such doubt "will be resolved in insured's favor." *Id.* The more difficult situation, though, is where the pleading simply does not state sufficient facts to determine whether there is potentially coverage under the policy.

A. Duty to Defend vs. Duty to Indemnify

The "Eight Corners" rule governing the Insurer's Duty to Defend contrasts with the approach that determines the Insurer's corollary "Duty to Indemnify". It is often said that the duty to defend and duty to indemnify are distinct and separate duties creating distinct and separate causes of action. *See Argonaut Southwest Ins. Co. v. Maupin*, 500 S.W.2d 633, 635-36 (Tex.1973). The Duty to Defend is predicated solely on the allegations of the pleading as to whether there is potential coverage for the claims as alleged, and is applied on that basis regardless of the true facts. The Duty to Indemnify, however, may - - indeed, must - - take into account all the evidence developed in the suit and through trial in order to determine whether the policy actually provides coverage for the liability of the Policyholder as adjudicated after trial or resolved through settlement.

For this reason, it is sometimes said that the Duty to Defend is "broader" than the Duty to Indemnify. In actual practice, however, the comparative breadth of the Duty to Defend and the Duty to Indemnify depends upon whether the facts alleged in the pleading prove to be true or not, and whether or not those allegations favor coverage on their face.

For example, if the pleading alleges untrue facts which bring the claim within an exclusion of the policy, there is no Duty to Defend even if the true facts would bring the claim within coverage and are known to the Insurer. In that circumstance, the Insurer may well owe a Duty to Indemnify the Policyholder once the true facts are established at trial and the exclusion is no longer implicated, even though the Insurer did not owe a Duty to Defend based on the inaccurate facts presented in the pleading. *See e.g., U.S. Fidelity & Guaranty Co. v. Baldwin Motor Co.*, 34 S.W.2d 815

(Tex.Com.App., 1931). Under this sort of scenario, the Duty to Indemnify clearly is the broader obligation in comparison with the moribund Duty to Defend.

Conversely, where the pleading alleges specific facts that bring the claim within coverage, the Insured will owe a Duty to Defend even where the Policyholder admits that the alleged liability facts are wrong. So, for example, the Insurer is required to defend where the pleading states a claim within the scope of coverage by alleging that a Policyholder is responsible for an accident involving a vehicle driven by the Policyholder's alleged "agent," even though the Policyholder admits that the driver was not, in fact, its agent at the relevant time. In that sort of circumstance - - where the pleading states a covered claim but it is unlikely the Insured will owe a Duty to Indemnify once the true facts are established at trial - - the Duty to Defend may indeed provide a "broader" benefit to the Policyholder. *Heyden Newport Chemical Corp. v. Southern General Insurance Co.*, 387 S.W.2d 22, 26 (Tex.1965).

B. Standard Policy Wording Comprising Duty to Defend in Insurance Contract

The Duty to Defend typically is found in the insuring agreement of policies affording primary layer insurance that protects the insured from liability asserted in claims by third parties. The policies include, most notably, Commercial General Liability (CGL) policies, Homeowners' policies, and Auto policies. For instance, a standard commercial general liability policy provides:

> We will pay those sums that the insured becomes legally obligated to pay as damages because of 'bodily injury' or 'property damage' to which this insurance applies. We will have the right and duty to defend any 'suit' seeking those damages.[2]

Even more specifically, a classic Homeowners policy formulation of the Duty to Defend, found in the Liability Coverage of the current Texas Homeowners Policy - Form HOB, states:

> If a claim is made or a suit is brought against an 'insured' for damages because of 'bodily injury' or 'property damage' caused by an 'occurrence' to which this coverage applies, we will: . . . Provide a defense at our expense by a counsel of our choice, even if the suit is groundless, false, or fraudulent.[3]

Similarly, the insuring agreement of the Texas standard Personal Auto Policy provides for

---

[2] *See e.g. C.U. Lloyd's of Tex. v. Main Street Homes, Inc.*, 79 S.W.3d 687, 691 n.6 (Tex. App.-Austin 2002, no pet. h.); *see also* Ellen S. Pryor, *Mapping the Boundaries of the Duty to Defend in Texas,* 31 Tex. Tech L. Rev. 869, fn 17 (2000) citing Alliance of American Insurers, Policy Kit for Insurance Professionals, at 1 (1993-94) (reprinting standard commercial general liability policy).

[3] *Id.*, Alliance of American Insurers, Policy Kit for Insurance Professionals at 29 (1993-94) (reprinting standard homeowners policy).

both a duty to defend and a duty to indemnify:

> We will pay damages for bodily injury or property damage for which any 'covered person' becomes legally responsible because of an auto accident. . . .We will settle or defend, as we consider appropriate, any claim or suit asking for these damages. In addition to our limit of liability, we will pay all defense costs we incur. Our duty to settle or defend ends when our limit of liability for this coverage has been exhausted.[4]

.

These insurance policy provisions link the defense obligation to what the plaintiff *alleges*, not to the truth or merits of the plaintiff's claim. Although the "groundless, false, or fraudulent" clause is most explicit, other versions also predicate the Duty to Defend on what the lawsuit merely claims or seeks. The Eight Corners rule reflects the Texas courts' interpretation and enforcement of the Insurer's undertaking to provide a defense pursuant to this sort of standard contract wording.

C. General Application of the Duty to Defend

The Duty to Defend is one of the emblematic and important features of the Primary layer of insurance. In many cases - - most notably in professional malpractice and intellectual property cases, but also in any multi-party, multi-issue case of serious value - - costs of defense may be very high and may even exceed the probable range of verdict or settlement. The Primary Insurer typically must continue to defend a suit until the limit of liability of the Primary policy has been exhausted through "payment of settlements or judgments." *See Am. States Ins. Co. of Tex. v. Arnold*, 930 S.W.2d 196 (Tex. App.-Dallas 1996, writ den.).

In contrast with excess liability insurance that offers coverage for higher limits and typically does not include a duty to defend - - at least not until the primary layer is exhausted - - the primary policy often is more expensive precisely because it must respond to every claim and must provide and pay for the Insured's defense until the claim is concluded or the primary limit is paid in full. This situation is described by the Texas Supreme Court in *Keck, Mahin & Cate v. Nat. Union Fire Ins. Co.*, 20 S.W.3d 692, 700 (Tex. 2000) (citations omitted):

> Excess insurers are able to provide relatively inexpensive insurance with high policy limits because they require the insured to contract for underlying primary insurance with another carrier. The primary carrier generally provides a much lower amount of coverage, but must insure against what is likely to be a greater number of claims and must provide a defense.

Excess or Umbrella Insurers also may be responsible to provide defense upon exhaustion of Primary limits, especially in cases involving significant damages and / or involving multiple claimants or multiple Policyholders / Insureds. *See Travelers Indem. Co. v. Citgo Petroleum Corp.*, 166 F.3d 761

---

[4] *Id*. at 3 (reprinting standard auto liability policy); also, attached to Janet K. Colaneri, *Mapping Your Way Through the Standard Texas Personal Automobile Policy*, 7th Annual Insurance Law Institute, University of Texas School of Law (2002).

(5th Cir. 1999).

If an Insurer owes a Duty to Defend any portion of a suit, the insurer must defend the entire suit. *See St. Paul Ins. Co. v. Texas Dept. of Transp*., 999 S.W.2d 881, 884 (Tex.App.-Austin 1999, rev. denied) (citations omitted). So long as the pleading alleges at least one claim that is potentially within the scope of coverage, the Insurer must defend the Policyholder from all claims alleged in the suit. *See Maryland Casualty Co. v. Moritz*, 138 S.W.2d 1095, 1097 (Tex.Civ.App.--Austin 1940, writ ref'd).

Those claims asserted in the most recent, current pleading are the only relevant allegations for determining the Duty to Defend; this principle finds perhaps its most cogent recitation in *Rhodes v. Chicago Ins. Co.*, 719 F.2d 116, 119 (5th Cir, 1983):

> Texas Rule of Civil Procedure 65 provides that amended pleadings completely supercede prior pleadings. Hence the duty to defend is determined by examining the latest, and only the latest, amended pleadings. A complaint which does not initially state a cause of action under the policy, and so does not create a duty to defend, may be amended so as to give rise to such a duty. Likewise, a complaint which does allege a cause of action under the policy so as to create a duty to defend may be amended so as to terminate the duty. In the first instance, the insurer may properly refuse to defend before the amended complaint is filed, and in the second, the insurer may properly withdraw after the amendment is made.

This rule makes perfect sense under Rule 65, Tex. R. Civ. P., which provides that an amended pleading by its very nature takes the place of the original, and that the instrument for which the amended pleading is substituted shall no longer be considered as a part of the pleading. *See also Canutillo Indep. Sch. Dist. v. National Union Fire Ins. Co. of Pittsburgh, Pa.,* 99 F.3d 695, 701 (5th Cir. 1996).

III. RULES OF CONSTRUCTION GOVERNING INSURANCE CONTRACTS

Because the Duty to Defend is a creature of the contract wording of the Insurance Policy, the potentiality of coverage for determining the Duty to Defend must be interpreted under legal rules applicable to contract construction generally. In addition to the general rules of contract construction, a number of specific rules applicable to insurance policy contracts have been developed in Texas statute and common law.

A. General Rules of Contract Construction

These general rules are applicable to all contracts, including insurance contracts, and comprise a familiar litany for the insurance coverage practitioner:

♦ The interpretation of insurance contracts in Texas is governed by the same rules as the

interpretation of other contracts.

- ♦ In determining the scope of an insurer's duty to defend under a particular policy, courts look to the language of the policy itself and the allegations in the petition / complaint against the insured.

- ♦ In construing the language used in a particular policy, courts look to the written expression of the parties' intent; all parts of the policy must be construed together to effectuate this intent.

- ♦ All the provisions of the policy must be given effect and the policy must be viewed in its entirety, with each clause being used to help interpret the others

- ♦ An interpretation that gives a reasonable meaning to all provisions is preferable to one that leaves a portion of the policy useless, inexplicable, or creates surplusage.

- ♦ The intent of the parties is derived by examining the words used, the subject matter to which they relate, and the matters naturally or usually incident to them.

- ♦ The words in a contract are given their ordinary meaning unless the policy clearly gives them a different meaning.

- ♦ Where the wording is plain and unambiguous, the terms of the contract alone express the parties' intent and they must be given their plain meaning and enforced as written without the aid of extrinsic evidence.

- ♦ The fact that the parties interpret the contract in different ways does not mean that the contract is ambiguous, and neither conflicting expectations nor disputation creates an ambiguity.

- ♦ Wording in insurance provisions is ambiguous when an uncertainty exists about which of two or more meanings was intended; only then will the courts adopt the interpretation most favorable to the insured.

See generally Forbau v. Aetna Life Ins. Co., 876 S.W.2d 132, 133 (Tex. 1994); *Balandran v. Safeco Ins. Co. of Am*., 972 S.W.2d 738 (Tex. 1998); *Kelley-Coppedge, Inc. v. Highlands Ins. Co.*, 980 S.W.2d 462, 464 (Tex.1998); *Liberty Mut. Ins. Co. v. American Employers Ins. Co.*, 556 S.W.2d 242, 245 (Tex.1977).

B. Special Rules of Contract Construction Applicable to Insurance Contracts

In one respect, however, insurance contracts are different from other contracts: In other sorts of contracts, ambiguous language generally creates a fact question regarding the parties' intent, but with insurance policies a presumption is applied in favor of coverage.

This presumption exists because the policy virtually always is written on the insurer's form, and therefore the rule of contra proferentum requires that ambiguities be construed against the drafter. *See Texas Ass'n of Counties County Government Risk Management Pool v. Matagorda County,* 52 S.W.3d 128, 136 (Tex. 2000) (citing *Gonzalez v. Mission Am. Ins. Co.*, 795 S.W.2d 734, 737 (Tex.1990) for the proposition that, if a policy provision is vague or ambiguous, the fault lies with the insurer as the policy's drafter); *see also Excess Underwriters At Lloyd's v. Frank's Casing Crew & Rental Tools, Inc.*, 2002 WL 1404705, *2 (Tex.App.-Hous. [14 Dist.] 2002, pet. for review filed). The presumption also may be implicated in the special relationship created by the relative disparity in bargaining power and position between the insured and the insurer. *See Arnold v. National County Mut. Fire Ins. Co.*, 725 S.W.2d 165 167 (Tex. 1987) ("In the insurance context a special relationship arises out of the parties' unequal bargaining power and the nature of insurance contracts which would allow unscrupulous insurers to take advantage of their insureds' misfortunes.").

The wording of the insurance policy is ambiguous only if - - after application of other general principles of contract construction have failed to reveal an unambiguous intent - - both the Insurer and the Policyholder have conflicting interpretations of the policy, and both interpretations are reasonable. In such circumstances, a Texas court must resolve the ambiguity in favor of the construction that provides coverage to the insured. Moreover, the presumption operates in favor of the insured even if the Policyholder's version is LESS reasonable than the Insurer's interpretation. *See Glover v. National Ins. Underwriters*, 545 S.W.2d 755, 761 (Tex. 1977) *citing Continental Casualty Co. v. Warren*, 152 Tex. 164, 254 S.W.2d 762, 763 (1953), and *Insurance Co. of North America v. Cash*, 475 S.W.2d 912 (Tex. 1972). Unless the policy language is susceptible of two reasonable interpretations, however, the language is not ambiguous and the canon requiring liberal construction in favor of an insured is inapplicable. *Ranger Ins. Co. v. Bowie*, 574 S.W.2d 540, 542 (Tex.1978).

For purposes of this paper, perhaps the most notable statutory rule applicable to the Duty to Defend is Art. 21.58, Tex. Ins. Code, which establishes that the Insurer always has the burden of proof as to any avoidance or affirmative defense that must be affirmatively pled under Rule 94, Tex. R. Civ. P., specifically including any exclusion or exception to coverage. This rule bolsters the concept that the policy is construed against the Insurer where there is any question as to the proper interpretation of the policy wording.

C. Eight Corners Rule of Construction Applicable to Duty to Defend

Additional special rules of contract construction apply to the Duty to Defend as a specific aspect of the insurance policy. For example, as noted above, the typical wording of the insurance policy provides that an Insurer assumes the Duty to Defend any claims made against the Policyholder that are within the scope of the policy's coverage, whether the claims are false or fraudulent, and regardless of the truth of those assertions. This standard wording gives rise to the Eight Corners rule, whereby an Insurer's Duty to Defend is determined by comparing the factual allegations in the pleadings to the language of the insurance policy.

The following, interrelated general rules have been developed through judicial implementation of the Eight Corners rule:

♦ An Insurer's contractual Duty to Defend must be determined solely from the face of the pleadings, without reference to their truth or falsity and without reference to any facts outside the pleadings or to what the parties know or believe to be the true facts.

.

♦ The Duty to Defend "is not affected by facts ascertained before suit, developed in the process of litigation, or by the ultimate outcome of the suit."[5]

♦ When deciding if a Duty to Defend exists, courts must act as if all the facts alleged in the (third party) plaintiff's petition against the Policyholder are true, and the task of the court is to determine if the claims fall within the scope of the policy coverage.

♦ The factual allegations within a petition are liberally interpreted when determining if a petition alleges facts that potentially state a claim within the coverage of a policy for purposes of the Duty to Defend.

♦ When applying the Eight Corners rule, if the court finds the policy is vague, it construes the policy against the Insurer in favor of finding a Duty to Defend.

♦ Any doubt as to whether the allegations state a cause of action within the coverage of the policy is resolved in the Policyholder's favor.

♦ The focus of the inquiry is on the facts alleged, not the legal theories asserted. In reviewing the underlying pleadings, the court must focus on the factual allegations that show the origin of the damages rather than on the legal theories alleged.[6]

---

[5] *American Alliance Ins. Co. v. Frito-Lay, Inc.*, 788 S.W.2d 152, 154 (Tex.App.--Dallas 1990, writ dism'd).

[6] *Adamo v. State Farm Lloyds Co.*, 853 S.W.2d 673, 676 (Tex.App.--Houston [14th Dist.] 1993, writ denied) ("It is not the cause of action alleged that determines coverage but the

- ♦ The factual allegations against the insured should be considered in light of the policy provisions without reference to their truth or falsity and without reference to what the parties know or believe to be the true facts.[7] However, the court may not read facts into the pleadings, may not look outside the pleadings, and may not imagine factual scenarios which might trigger coverage.

- ♦ The rule of contra proferentum applies to contractual interpretation of the insurance policy in favor of the Insured, but does not extend so far as requiring that the third-party pleading against the Policyholder be strictly interpreted against the Insurer.[8]

- ♦ Whether an insurance carrier owes a duty to defend under an insurance policy is a question of law that the appellate court reviews de novo.

See generally Heyden Newport Chemical Corp. v. Southern General Ins. Co., 387 S.W.2d 22, 24-25 (Tex.1965); *see also Nat. Union Fire Ins. Co. v. Merchants Fast Motor Lines, Inc.*, 939 S.W.2d 139, 141-42 (Tex. 1997).

D. Eight Corners Rule in Action - - Duty to Defend Denied on Factual Allegations of Pleading

At this juncture, it would be instructive to review how the courts actually utilize the Eight Corners rule in the context of determining the Duty to Defend by reference to the pleading and the policy, only. The recent, important opinion in *Farmers Tex. County Mut. Ins. Co. v. Griffin*, 955 S.W.2d 81, 83 (Tex. 1997) is typical of the Eight Corners approach where the court determines that the pleading does not allege facts potentially within coverage.

In that case, the claimant's pleading alleged that he was hit with gunfire from shots fired by two passengers of the vehicle the Insured was driving. The Court looked to the pleading and focused on specific allegations that:

> Suddenly and without warning, a vehicle driven by [the Policyholder] approached [Plaintiff]. Several rounds of gunfire were discharged from the vehicle in the direction of the Plaintiff.

The pleading continued:

> This drive-by shooting was a random act of violence which has permanently injured and

---

facts giving rise to the alleged actionable conduct.")

[7] *See Argonaut Southwest Ins. Co. v. Maupin*, 500 S.W.2d 633, 635 (Tex.1973).

[8] *Feed Store, Inc. v. Reliance Ins. Co.*, 774 S.W.2d 73, 75 (Tex.App.-Hous. [14 Dist.] 1989, writ denied); *Taylor v. Travelers Ins. Co.*, 40 F.3d 79 (5th Cir., 1994).

scarred the plaintiff.

Section III of the pleading alleged that the defendants were liable for negligence including: failure to operate a motor vehicle in a safe manner; negligent transportation of armed persons; failure to control the acts of those being transported; failure to stop and render aid; failure to take evasive action to avoid injury to the Plaintiff; and; other acts to be specified in detail at the time of trial.

Section VI of the petition, seeking punitive damages, alleged that plaintiff's injuries were caused by "gross negligence, conscious indifference, and utter disregard for the safety and welfare of the Plaintiff."

Despite the plaintiff's obvious efforts to frame the Policyholder's conduct in terms of legal theories of "negligence" and "gross negligence," the Court nonetheless rejected this characterization. Instead, the Court concluded that the plaintiff's factual allegations demonstrated the origin of his damages was intentional behavior, and that the pleading contained no factual contention that could be properly characterized as negligent behavior by the Insured The applicable auto policy excluded coverage for any person who "intentionally causes bodily injury or property damage." The Court determined that all the operative facts alleged in the pleading came within this exclusion. Therefore, the pleading did not describe a claim within the scope of the policy's coverage, and the Eight Corners rule absolved the Insurer of any Duty to Defend.

Moreover, the Court found the factual description of the incident did not comprise an "automobile accident" for purposes of coverage under the relevant auto policy. This provided another, independent basis for the Insurer to properly deny any Duty to Defend the suit.

E. Eight Corners Rule in Action - - Duty to Defend Imposed on Factual Allegations of Pleading

The opinion in *St. Paul Fire & Marine Ins. Co. v. Green Tree Fin. Corp.*, 249 F.3d 389, 392 (5th Cir. 2001) illustrates the same approach to the Eight Corners rule, but with a finding that the factual allegations of the pleading were sufficiently clear to impose the Duty to Defend.

There, the Insured was the plaintiff, Green Tree, who filed a suit to collect a debt related to the purchase of a mobile home. Defendants asserted counterclaims against Green Tree for wrongful debt collection practices and specifically alleged that Green Tree made frequent rude and abusive telephone calls over a long period of time in an attempt to collect the debt. Defendants' counterclaim pleaded causes of action for negligence, for statutory and common law unfair debt collection practices, and under the Deceptive Trade Practices Act, and requested actual damages, costs, and any other relief to which Defendants claimed to be legally entitled.

The insurance policy issued to Green Tree provided coverage (under Coverage "B" of the CGL policy) for personal injury arising from various "offenses," including "violation of the right of privacy." The pleading did not, however, specifically plead such an offense nor did it overtly seek

damages on the basis of a cause of action for "invasion of privacy."

Like the Texas Supreme Court in *Griffin*, the Fifth Circuit in *Green Tree* did not stop at the facial characterization of relief sought in the pleading. Rather, the court examined the legal elements of a cause of action for "invasion of privacy" to determine if the factual allegations described in the pleading potentially comprised such a claim, even if "invasion of privacy" was not overtly alleged as a legal theory or cause of action for relief. The court decided that the factual allegations of the pleading described such an offense, based on the description of the nature and extent of harassing telephone calls whereby the Insured attempted to collect the alleged debt, even though "invasion of privacy" was not pled in Defendants' counterclaim as a particular cause of action. Accordingly, the court imposed a Duty to Defend on the Insurer based on factual allegations that could potentially describe a covered claim for "violation of the right of privacy."

IV. Factual Specificity Meets Notice Pleading

As illustrated by the respective deliberations of the Court in *Griffin* and *Green Tree*, courts often must exercise significant interpretive powers in order to determine defense coverage under the Eight Corners rule. Part of this difficulty may be attributable to the shift in procedural practice from an older requirement of "Fact" pleading to the development of modern "Notice" pleading.

A. Historical "Fact" Pleading vs. Current "Notice" Pleading

Historically, "Fact" pleading (also known as "Cause-of-Action" pleading) began to replace even earlier, more highly technical pleadings about the middle of the nineteenth century and then began waning with the adoption of Federal Rules of Civil Procedure in 1938.[9]

> Under Fact Pleadings systems, a pleading was defective if it failed to state an ultimate fact which was an element of the causes of action upon which the plaintiff meant to proceed. Discovery was limited by the pleadings. What the jury could do was limited by the pleadings. The judgment had to reflect the pleadings. If one element of a cause of action was left out, it was not possible to prove one of the facts which was absolutely necessary to generate the right of recovery. The law assumed that if the fact was not pleaded it could not be proved.[10]

---

[9] I am indebted to Michael Sean Quinn's paper "Pleading Texas Insurance Cases" presented at the Third Annual Insurance Law Institute (2000), University of Texas School of Law, for the historical background and development from "Fact" to "Notice" pleading described in this section of the paper. The reader is referred to Mr. Quinn's paper and to the sources cited therein for further explication comparing the respective forms of pleading.

[10] *Id.* at 9.

Essentially, then, under Fact Pleadings all facts necessary to the plaintiffs cause of action must be pleaded specifically in order to conduct discovery, submit issues to the jury, and obtain a judgment for relief on that cause of action.

In contrast, under modern "Notice" pleading it is not necessary to articulate the plaintiff's cause of action with specificity as to each element of the causes of action asserted. Rather, it is sufficient for the pleading simply to put the defendant on notice of the outlines of the claim so that the defendant may conduct appropriate discovery and defend against the claim. A pleading need only "consist of a statement in plain and concise language of the plaintiff's cause of action." It is not grounds for objection to a pleading "that an allegation be evidentiary evidentiary or be of a legal conclusion . . . when fair notice to the opponent is given by the allegations as a whole." Rule 45, Tex. R. Civ. P.

While in practice a pleading may nonetheless include substantial factual description - - especially in more complicated or egregious cases - - only facts sufficient to give " fair notice" of claims for relief are required under Rule 47, Tex. R. Civ. P.[11] In contrast to requirements under prior "Fact" pleading rules, "Notice" pleading under Rule 45 does not require that the plaintiff set out in his pleadings the evidence upon which he relies to establish his asserted cause of action. *Paramount Pipe & Supply Co. V. Muhr*, 749 S.W.2d 491, 494-95 (Tex. 1988).

B. Liberality of "Notice" Pleading and the Duty to Defend

Why is this historical development important, one might ask?

Consider, that when the Eight Corners rule was initially developed the rules of "Fact" pleading required that every pleading include each and every fact necessary to support the cause(s) of action asserted for relief. In that context, the Eight Corners rule seems virtually foolproof - - if sufficient facts must be alleged to support each cause of action asserted, then it should generally be an easy matter to match the relatively extensive facts with the wording of the policy as issued in the insurance contract.

Under modern "Notice" pleading, however, the pleader has considerably more opportunity to craft the factual assertions to describe - - or, more importantly perhaps, to fail to describe - - claims that potentially are within coverage, or not. Since the plaintiff if the master of his "Notice" pleading, he may decide to plead specific facts within coverage of the policy, or may omit facts that might implicate an exclusion or other defense to coverage, in order to trigger the duty to defend and involve the insurer in the suit. Conversely, a pleader aware of the coverage wording may design the

---

[11] *See Horizon/CMS Healthcare Corp. v. Auld*, 34 S.W.3d 887, 896-7 (Tex. 2000) ("Texas follows a 'fair notice' standard for pleading, which looks to whether the opposing party can ascertain from the pleading the nature and basic issues of the controversy and what testimony will be relevant. . . . A petition is sufficient if it gives fair and adequate notice of the facts upon which the pleader bases his claim.") (citations omitted).

factual assertions of the pleading to allege or omit facts for the purpose of defeating the duty to defend and leave the defendant without the benefit of insurance to defend against the suit.[12]

As exemplified by the *Griffin* and *Green Tree* cases, a pleader's own characterization of his claim may not always prevail over the court's own interpretation of the factual allegations in the pleading. Where the pleader is cognizant of the wording of the insurance policy issued to a defendant, however, "Notice" pleading provides significant latitude for the pleader to influence whether an Insurer will have to defend the Policyholder-defendant or not.[13]

C. Liberality of "Notice" Pleading vs. Preclusive Effect of Declaratory Judgments

The liberality of "Notice" pleading procedure presents a particularly difficult jurisprudential problem where the Insurer seeks a declaratory judgment that there is no duty to defend because a pleading fails to articulate a claim within the potential coverage of the policy.

Longstanding Texas precedent formerly restricted the Insurer to declaratory relief on the Duty to Defend, alone, and prohibited any declaration on the Duty to Indemnify as premature. *Firemen's Insurance Co. v. Burch*, 442 S.W.2d 331 (Tex.1968) (no justiciable controversy regarding the insurer's duty to indemnify before a judgment has been rendered against an insured; thus, declaratory judgment to determine whether insurer had such a duty was premature).

The *Griffin* case famously overturned *Burch*, holding that the Duty to Indemnify is justiciable before the Policyholder's liability is determined in the liability lawsuit "when the insurer has no duty to defend and the same reasons that negate the duty to defend likewise negate any possibility the insurer will ever have a duty to indemnify."[14] On the facts as alleged in that case, the *Griffin* court determined that "[n]o facts can be developed in the underlying tort suit that can transform a drive-by shooting into an 'auto accident'", and therefore the Insurer not only had no Duty to Defend but also,

---

[12] As noted above, however, even though an Insurer may not have a duty to defend based on the facts alleged or omitted in the pleading, that does not necessarily mean that the Insurer is relieved of its potential duty to indemnify the Policyholder based upon the facts that are actually developed and presented in the suit.

[13] *See e.g.* Quinn, supra fn. 4, at 37 - 41; *but see, e.g.*, *Metropolitan Prop. & Cas. Co. v. Murphy*, 896 F.Supp. 645 (E.D.Tex. 1995) (claimant's petition alleging that insured, in whose house she lived for over one year, secretly watched her shower, bathe, dress and sleep through holes he had drilled in her bathroom and bedroom walls did not allege conduct satisfying definition of "occurrence" in insured's homeowner's policy, as alleged conduct was on its face intentional, not accidental, even though claimant obviously was attempting to bring the claim within potential insurance coverage by characterizing the claim as one for "negligent" invasion of privacy).

[14] 955 S.W.2d at 84.

for the same reasons, had no possibility of a prospective Duty to Indemnify.

To the extent that the facts as alleged in a particular pleading cannot ever make out a claim within coverage - - as the *Griffin* court determined to be the case for the pleading and circumstances it considered - - this approach allows the Insurer to determine the full extent of coverage in a single declaratory action as to both the Duty to Defend and the Duty to Indemnify. This very approach may prove ill-advised under modern Texas procedural rules, however, where the pleading may be amended virtually as a matter of right up to a week before trial, and leave is liberally granted to file amendments immediately prior to or even during trial unless the amendment would operate as an unfair surprise to the defendant. Rules 63, 66, Tex. R. Civ. P. A pleading may be amended even after trial to conform to issues tried without objection, and the court may order a repleader in order to make the pleading substantially conform to the rules. Tex. R. Civ. P. 67, 68.

The guidance provided in *Griffin* seems to wholly ignore the effect of these liberal pleading rules. Thus, an Insurer might obtain a declaratory judgment that it has no Duty to Defend nor any Duty to Indemnify, only to have the plaintiff allege additional (or fewer) facts to defeat the declaratory relief by bringing the amended pleading within the scope of coverage. This anomaly creates a potential conflict between the ordinarily preclusive and dispositive res judicata effect of the judicial declaration absolving an Insurer of both its Duty to Defend and its Duty to Indemnify, over against the clear rule that prior pleadings are wholly superseded and replaced by an amended pleading and that the Duty to Defend must be determined anew if the amended pleading now alleges facts that are potentially within coverage.

D. Duty to Defend Controlled by Amended Pleading - - *Reser* Case

Certainly, where the pleading is amended to delete any allegation comprising a covered claim, the Insurer is entitled on the basis of the pleading, alone, to declaratory judgment that it has no Duty to Defend. Under the Eight Corners rule, as we have seen, only the facts as alleged in the pleading are determinative of the Duty to Defend, and not any facts or knowledge otherwise known or available to the Insurer or Policyholder.

This precept is illustrated by *Reser v. State Farm Fire & Cas. Co.*, 981 S.W.2d 260 (Tex. App.-San Antonio 1998, no pet.), in which the Insurer withdrew defense after the plaintiff initially alleged a covered claim for defamation, but then deleted that claim in an amended pleading. The court sustained the Insurer's right to withdraw the defense on the basis that:

> [T]he critical issue is what claims were actually asserted against [the Policyholder]. . . [The plaintiff] had the burden of asserting its claim, and ultimately, in its amended counterclaim, [plaintiff] asserted neither facts nor legal theories stating a defamation claim. In the absence of a stated claim against its insured, [the Insurer] was not obligated to defend its insured.[15]

---

[15] *Id.* at 266.

Thus, the effect of the court's decision in *Reser* was to hold that the Insurer had no Duty to Defend, even though both the Insured and the Policyholder knew of facts that would potentially support a covered claim of defamation as described in the prior pleading. Rather, the coverage determination was made strictly on the basis of the most recent pleading which no longer alleged a covered cause of action nor any facts that would potentially support the covered claim.

E. *Griffin* Finality Defeated by Subsequent Amendment of Pleadings?

The opposite of the *Reser* situation is precisely the circumstance rife with potential difficulty under *Griffin.* What if, after the decision had been issued in a *Reser*-type situation, the claimant had re-amended the pleading to reinstate the defamation claim, or had presented evidence of defamation without objection at trial? In that circumstance the Insurer's Duty to Defend presumably would likewise have to be reinstated to comport with the then-current amended pleading, and the declaratory judgment obtained under a prior pleading necessarily would become null and void.

No case has as yet been presented to the Texas courts raising these issues in the aftermath of *Griffin*, and therefore Texas jurisprudence has not yet developed any further guidance on the interplay between the presumably res judicata effect of a *Griffin* ruling on the basis of facts alleged in a pleading, when those facts are expanded or curtailed in a later amended pleading prior to, during, or even after trial.

Ordinarily, the prospect for such an anomaly might counsel that an Insurer refrain from filing for declaratory relief at all, unless it could be virtually certain that no facts could possibly be alleged - - neither in the current pleading nor in any later amendment - - that could bring the suit within potential coverage of the policy. However, this conservative approach often may be untenable insofar as the Texas Supreme Court has indicated that the Insurer is expected to pursue and obtain declaratory relief where possible to determine coverage prior to resolution of the underlying suit when the Duty to Defend / Duty to Indemnify is in dispute and the Insurer has issued a reservation of rights. *State Farm Fire & Cas. Co. v. Gandy*, 925 S.W.2d 696, 714 (Tex.1996) (requiring an Insurer to either accept coverage without reservation or make a good faith effort to resolve coverage before adjudication of the plaintiff's claim).

Unless and until this problem is articulated and addressed by the Texas courts, an Insurer may risk incurring the costs of a declaratory action under *Griffin* to satisfy the demands of *Gandy*, only to have the declaratory judgment mooted and the Duty to Defend / Duty to Indemnify renewed by a differently articulated amendment to the pleading as was done in *Reser*.

V. WHEN THE PLEADING IS INADEQUATE TO DETERMINE DUTY TO DEFEND

From an Insurer's perspective, if a petition does not allege facts within the scope of coverage, an Insurer is not legally required to defend a suit against its Policyholder. *See Am. Physicians Ins. Exch. v. Garcia*, 876 S.W.2d 842, 848 (Tex. 1994). Or as stated in *Griffin*: "Even though we do not

look at the specific legal theories alleged to determine the duty to indemnify, if the underlying petition does not raise factual allegations sufficient to invoke the duty to defend, then even proof of all of those allegations could not invoke the insurer's duty to indemnify."[16]

As we have also discussed above, however, "Where the complaint does not state facts sufficient to clearly bring the case within or without coverage, the general rule is that the insurer is obligated to defend if there is, potentially, a case under the complaint within the coverage of the policy." *Nat'l Union Fire Ins. Co. of Pittsburgh, Pa. v. Merchants Fast Motor Lines, Inc.*, 939 S.W.2d 139, 141 (Tex. 1997). But, the allegations must at least be specific enough to "create that degree of doubt which compels resolution of the issue for the insured", and the court will not "imagine factual scenarios which might trigger coverage." *Id.* at 142.

So, how is the Duty to Defend determined when, after applying all the relevant rules of contract construction, it is still not clear from the factual allegations of the pleading whether or not the claim is, potentially, covered by the policy?

In other words, what happens when the factual allegations of the pleading are simply insufficient to determine whether the policy potentially provides coverage or not, even after allegations are liberally interpreted in favor of the Policyholder? Is it permissible in those circumstances for the court to entertain and consider evidence extrinsic to the pleading, despite the general prohibition under the Eight Corners rule from reviewing anything beyond the pleading itself and the policy wording?

This is a difficult question, and one which recently has generated some thought in academic and professional insurance circles in Texas.[17]

Without belaboring the various strands of judicial resolution of this issue, the developing rule seems to be that the allegations of the pleading control absolutely where the Insurer seeks to avoid its Duty to Defend on the basis that the Insured is not liable to the claimant, and facts extrinsic to those alleged in the pleading may not be used to controvert those allegations. But, where the basis for the refusal to defend is that the events giving rise to the suit are outside the coverage of the insurance policy, facts extrinsic to the claimant's petition may be used to determine whether a Duty to Defend exists.

---

[16] 955 S.W.2d at 82-83

[17] For more comprehensive discussions of the extrinsic evidence problem, see Ellen S. Pryor, *Mapping the Boundaries of the Duty to Defend in Texas,* 31 Tex. Tech L. Rev . 869, fn 17 (2000), and; Karen L. Keltz, *Extrinsic Evidence: Can You Use It and Where Do You Find It*, 7th Annual Insurance Law Institute, University of Texas School of Law (September 5-6, 2002).

A. Extrinsic Evidence on Coverage Facts Not Affecting Insured's Liability

If the Insurer's question of coverage involves questions pertaining, for example, to an exclusion based upon Insured's ownership or lack of ownership of the instrument of injury and damage alleged in the pleading, then extrinsic evidence ordinarily should not be allowed because the issue of ownership or control may be relevant to the basis of liability asserted against the Insured. *See Gonzales v. American States Ins. Co.*, 628 S.W.2d 184 (Tex. App.--Corpus Christi 1982, no writ). Of course, the pleading must be liberally construed in favor of the Insured and coverage when determining whether the alleged facts include the possibility of coverage. *Id.* at 187; *Tri-Coastal Contractors, Inc. v. Hartford Underwriters Ins. Co.*, 981 S.W.2d 861, 864 (Tex. App.-Houston[1st Dist.] 1998, no pet.) (any uncertainty in the pleading is to be resolved in favor of the insured without reference to extrinsic evidence).

Similarly, the Fifth Circuit refused to consider extrinsic evidence pertaining to overlapping coverage and liability facts in *Gulf Chemical & Metallurgical Corp. v. Associated Metals & Minerals Corp.*, 1 F.3d 365, 371 (5th Cir. 1993). The pleading alleged that one the Insured was liable because it had sold or shipped a toxic chemical, molyoxide. The pleading alleged the plaintiff had been exposed to the chemical during the policy period, but did not specifically state when the defendant was involved in actually shipping molyoxide. The Insurer attempted to present extrinsic facts establishing that the Insured did not ship molyoxide until after expiration of the insurance policy. The Fifth Circuit rejected the use of extrinsic evidence to determine the Duty to Defend, stating that Texas authority prohibited consideration of extrinsic evidence that affected the Insured's liability in the underlying suit.

On the other hand, where the question of coverage calling into doubt the Duty to Defend involves an issue solely affecting coverage under the Policy and not liability in the underlying suit, such as whether the defendant is included as an Insured in the Policy, then extrinsic evidence on that issue may be allowed. Thus, when the question of a Duty to Defend hinges on whether the defendant is an insured under the Policy, extrinsic evidence may be entertained when those coverage facts are not alleged in the pleading and do not affect or involve liability issues alleged in the pleading. *See International Service Ins. Co. v. Boll*, 392 S.W.2d 158 (Tex. Civ. App. - Houston 1965, writ ref'd n.r.e.) (affidavit identifying driver of vehicle as Insured's son allowed, where Policy specifically excluded son from coverage as an insured); *Cook v. Ohio Cas. Ins. Co.*, 418 S.W.2d 712, 714 (Tex. Civ. App. - Texarkana 1967, no writ) (same, involving exclusion hinging on whether insured was driving a vehicle owned by a relative who was also a member of the same household); *John Deere Ins. Co. v. Truckin' USA*, 122 F.3d 270, 272-73 (5th Cir. 1997) (affirming district court's use of extrinsic evidence to show that neither the vehicle in question nor the party seeking defense were covered by the insurance policy, and citing *Wade*, infra and *Cook* supra, to support holding that the "complaint allegation rule" is inapplicable where the live pleading in the underlying suit fails to allege facts sufficient to determine coverage under the policy even if taken as true).

It is important to note that this line of cases involves situations where the pleading is silent on the particular coverage fact which would determine the status of the defendant as an insured or

not; where the pleading does allege facts which specify the relationship of the defendant and thereby brings the case within coverage or excludes coverage, the allegation of the pleading cannot be collaterally attacked by extrinsic evidence regardless of the true state of affairs. *See U.S. Fidelity & Guaranty Co. v. Baldwin Motor Co.*, 34 S.W.2d 815 (Tex.Com.App. 1931); *Gonzales v. American States Ins. Co.*, 628 S.W.2d at 187.

The approach allowing "coverage only" facts has been expanded beyond mere identification of the defendant as an Insured. The principal case undoubtedly is *State Farm Fire & Cas. Co. v. Wade*, 827 S.W.2d 448, 452 (Tex. App.--Corpus Christi 1992, writ denied), where the duty to defend depended on a fact not alleged in the pleading: whether the insured vessel was being used for personal pleasure or in an excluded "business pursuit" at the time of the accident. The distinction between the vessel's use for personal or business reasons was of no consequence to the liability issues asserted against the Insured in the underlying suit. The court accepted extrinsic evidence developed in a declaratory judgment action to determine that the exclusion applied, recognizing that where the pleading does not allege facts sufficient for a determination of whether those facts, even if taken as true, are covered by the policy, then additional evidence may also be considered.

Insurers have cited the *Wade* line of cases to support their effort to use extrinsic evidence in determining the duty to defend. In general, federal courts, applying Texas law, have accepted the argument.[18] On the whole, Texas courts have rebuffed these efforts.[19]

---

[18] *See Guaranty Nat'l Ins. Co. v. Vic Mfg. Co.*, 143 F.3d 192, 194 & n.16 (5th Cir. 1998) (stating that Texas law allows the use of extrinsic evidence in certain circumstances, and citing *Gonzales*); *Hill & Wilkinson, Inc. v. American Motorists Ins. Co.*, 1999 WL 151668, at *5 n.7 (N.D. Tex. 1999) (slip op.) (citing *Gonzales* as including one exception to the strict complaint allegation rule, but concluding that the exception does not apply on these facts); *Southwest Tank & Treater Mfg. Co. v. Mid-Continent Cas. Co.*, 2003 WL 223445 (E.D.Tex., Feb. 4, 2003). *But cf. St. Paul Guardian Ins. Co. v. Centrum GS Ltd*., 283 F.3d 709 (5th Cir.(Tex.) Mar 11, 2002) (citing *Gulf Chemical* on the inviolability of the Eight Corner rule, but finding that the pleading sufficiently described "business activities" so as to trigger the insured's duty to defend).

[19] *See Tri-Coastal Contractors, Inc. v. Hartford Underwriters Ins. Co.*, 981 S.W.2d 861 (Tex. App.-Houston [1st Dist.] 1998, pet. denied); *Spruiell v. Lincoln Ins. Co.*, 1998 WL 174722 (Tex. App.-Amarillo 1998, pet. denied) (rejecting the insurer's request to consider the insured's arson conviction in determining the duty to defend); *Calderon v. Mid-Century Ins. Co.*, 1998 WL 898471 (Tex. App.-Austin 1998, pet. denied) (distinguishing several of the extrinsic evidence cases as involving "stipulated or undisputed facts which excluded the claims from coverage," and finding *Gonzalez* "unpersuasive"). *But cf. Mid-Continent Cas. Co. v. Safe Tire Disposal Corp.*, 16 S.W.3d 418 (Tex.App.-Waco 2000, rev. denied) (citing *Gonzales* to justify reliance on the agreed facts upon which the insured and insurer had tried their declaratory action, for purposes of determining whether "fire" or "pollution" exclusions precluded the duty to defend underlying action where pleading apparently did not allege facts sufficient to determine the applicability of those exclusions).; *see also Utica Lloyd's of Texas v. Sitech Engineering Corp.*, 38 S.W.3d 260

B. Extrinsic Evidence on Coverage Facts Overlapping with Liability Issues

Virtually alone among Texas courts, the federal Northern District of Texas has conceived that extrinsic evidence may be utilized to fill in gaps of an insufficiently detailed pleading, even if those facts affect and overlap with issues of the Insured's liability in the underlying suit.

For instance, in *Ohio Casualty Insurance Co. v. Cooper Machinery Corp.*, 817 F. Supp 45, 47-8 (N.D. Tex. 1993) the insurer argued that it had no duty to defend the insured in a product liability action because the policy contained a provision denying coverage for bodily injury occurring away from the insured's premises and arising out of the insured's completed work. The plaintiff's amended petition, however, alleged that the insured defendant had " 'failed to properly complete and finish the manufacturing' " of the product. Judge McBryde first noted that this allegation, even if taken as true, would not avoid application of the exclusion, since the exclusion barred coverage if the injury occurred away from the defendant's premises. In addition, Judge McBryde argued as follows:

> While an insurance company cannot avoid the policy defense obligation on the ground that extrinsic facts establish that its insured is not liable to the claimant, it can avoid the defense obligation if the extrinsic facts show that the alleged facts pertaining to coverage are false and that under the true facts there is no coverage under the policy. [E]ven if there were allegations of facts that would indicate the existence of coverage, the insurance company would be entitled in the declaratory judgment action to establish that the facts are false and that, therefore, there is no obligation under the policy, either to defend or to pay.[20]

The allegation that the defendant had failed to properly complete the operation arguably was an overlapping one: it related both to liability and to coverage. Yet the court allowed the insurer to use extrinsic evidence on this point. Thus, the court went farther than any other Texas state courts has yet gone with respect to allowing extrinsic evidence.[21] As a reading of Texas law, then, this

---

(Tex.App.-Texarkana 2001, no pet. h.) (citing *Wade*, et al,. for proposition that where the terms of the policy are ambiguous, or where the petition in the underlying suit does not contain factual allegations sufficient to enable the court to determine whether the claims are within the policy coverage, the court may consider extrinsic evidence to assist it in making the determination; however, the court actually looked only to the factual allegations of the pleading and to the wording of the policy in determining there was no duty to defend because alleged liability arose from excluded "professional services.")

[20] *Id.* at 48 (quoting from defendants' responses to the insurer's motion for summary judgment).

[21] Judge McBryde has issued other opinions to the same effect. *See, e.g., McLaren v. Imperial Cas. and Indem. Co.*, 767 F. Supp. 1364 (N.D. Tex. 1991), aff'd, 961 F.2d 213 (5th Cir. 1992), cert. denied, 113 S. Ct. 1269 (1993); *Blue Ridge Ins. Co. v. Hanover Ins. Co*., 748 F.

approach does not stand on firm ground.

C. Practical Application of Extrinsic Evidence Exemplified

One of the better examples for explicating and applying extrinsic evidence in determining the Duty to Defend is found in the recent case of *Harken Exploration Co. v. Sphere Drake Ins. PLC*, 261 F.3d 466 (5th Cir. 2001). In that suit, the Insured was an oil and gas exploration and production company that brought a declaratory judgment action seeking determination as to whether its liability Insurers had duty to defend it in lawsuits brought by owners of ranch property on which Harken held an oil and gas lease.

The court recited the standard propositions of the Eight Corner rule, that "an insurer's duty to defend is usually determined solely from the allegations in the most recent petition and the language of the insurance policy" and that "the general rule is that the insurer is obligated to defend [its insured] if there is, potentially, a case under the complaint within the coverage of the policy. *Id.* at 471. Looking only to the allegations of the pleading and construing the policy wording in accordance with Texas law, the court determined that the pleading effectively described an accident or occurrence within the scope of the insuring agreement and met the indica for "sudden and accidental" pollution damages. Faced with competing reasonable interpretations of additional pollution and saline contamination clauses, the court similarly followed well-established Texas principles that "If multiple interpretations [of the policy] are reasonable, [we] must construe the [policy] against the insurer." *Id.* at 475 (citations omitted).

However, the pleading was devoid of any express allegation that property damage occurred during the pertinent policy period. In order to determine if the damages alleged in the pleading occurred during the period the policy was in effect, the court adopted the Insured's reasoning that in order for Harken to have caused the property damage, it must have been operating on the Ranch; and in order for Harken to have been operating on the Ranch, it would have had to have a lease. The Insurer did not dispute that Harken purchased the lease prior to the Policy period, but it contended that the court was not entitled to consider extrinsic facts establishing when the Insured purchased the lease because that date is not in the complaint, petition, or in the insurance Policy. *Id.* at 466.

The Fifth Circuit further determined in *Harken* that: "when the petition does not contain

---

Supp. 470, 473 (N.D. Tex. 1991); *see also First Texas Homes, Inc. v. Mid-Continent Cas. Co.*, 2001 WL 238112, *4 (N.D.Tex. Mar 07, 2001) (Kaplan, Magistrate Judge, NO. 3-00-CV-1048-BD) (utilizing extrinsic affidavit testimony from the insured to establish involvement of a subcontractor in precipitating the loss where allegations of the ongoing underlying suit were not clear, for purposes of determining on summary judgment that exception to "business risk" exclusions required insurer to defend, citing *Mid-Continent Casualty Co. v. Safe Tire Disposal Corp.*, 16 S.W.3d at 421, which utilized extrinsic evidence to distinguish for coverage purposes between "hostile" and "friendly" fire and to determine whether recycled materials constituted "waste").

sufficient facts to enable the court to determine if coverage exists, it is proper to look to extrinsic evidence in order to adequately address the issue," citing *Western Heritage Ins. Co. v. River Entertainment*, 998 F.2d 311, 313-15 (5th Cir. 1993) and *State Farm Fire & Cas. Co. v. Wade*, 827 S.W.2d 448, 452-53 (Tex. App.-Corpus Christi 1992, writ denied). By considering the extrinsic evidence of the lease, the Fifth Circuit concluded that the damage alleged in the pleading occurred during the Policy period.[22] Since the pleading otherwise alleged a covered occurrence and property damage during the Policy period, the court found the Insured owed a Duty to Defend against the underlying lawsuits. *Id*. at 476-77.

D. Texas Supreme Court Interest in Resolving Extrinsic Evidence Question

To date, the Texas Supreme Court has not expressed a position on the use of extrinsic evidence to assist in determining the Duty to Defend when the pleading does not allege facts sufficient to address threshold questions of potential coverage. The prior pronouncements of the Court, as noted elsewhere above, simply recite the Eight Corners rule and stand for the proposition that the Duty to Defend must be determined from an examination of the pleading and policy, alone, with all possible inferences favoring the Policyholder and coverage.

There is some indication that the Court is ready to consider the extrinsic evidence problem when the right case comes before it. Recently, the court accepted for review a case from the Fort Worth court of appeals which would have squarely addressed the issue. *ITT Hartford Ins. Co. v. Home Depot, USA, Inc*., No. 2-00-130-CV (Tex. App. - Fort Worth, May 17, 2001, pet. dism'd by agr.). Unfortunately, the petition was dismissed by agreement after briefing but before the Supreme Court heard oral argument, and the intermediate appellate decision remains unpublished.

The underlying suit against Home Depot and Fantec apparently alleged injuries to a customer caused by a defective Fantec bracket, and Home Depot sought coverage as an insured under Fantec's liability insurance policy. The Insurer urged the court to consider extrinsic evidence to prove that the defective bracket was not, in fact, a Fantec bracket. The Fort Worth court noted that the pleading described Home Depot's and Fantec's liability on the basis that they were the designers, manufacturers, and distributors of the Fantec bracket that injured her. The court cited the Eight Corners rule and declined to accept extrinsic evidence to controvert these "liability facts" actually alleged in the pleading.[23]

---

[22] *See also Essex Ins. Co. v. Redtail Prods., Inc.*, 1998 WL 812394 (N. D. Tex. 1998) (extrinsic evidence examined to determine whether publication first occurred within policy period for purposes of coverage as advertising injury, where allegations of pleading were insufficient to make that determination).

[23] I am indebted to Karen L. Keltz for her recitation of the facts and intermediate appellate holding in *ITT Hartford*, in her article *Extrinsic Evidence: Can You Use It and Where Do You Find It*, 7th Annual Insurance Law Institute, University of Texas School of Law (September 5-6, 2002)

Presumably, the Texas Supreme Court must be interested in resolving the extrinsic evidence problem, since it accepted review of the *ITT Hartford* case but was prevented from addressing the issue when the parties settled. No doubt the court will be afforded another opportunity to consider this issue before too long.

E. Extrinsic Evidence of Policy Drafting History to Determine Duty to Defend

Ever since the Texas Supreme Court's decision in *National Union Fire Ins. Co. v. CBI Industries, Inc.*, 907 S.W.2d 517, 519 (Tex. 1995), lower courts have been reluctant to look to the drafting history in order to interpret policy wording. *CBI* instructs that extrinsic evidence such as the drafting history cannot be used to create an ambiguity in the policy where the wording at issue is otherwise plain and unambiguous.[24]

However, *CBI* also stated that extrinsic evidence was admissible for the limited purpose of illuminating the parties' intent in light of the circumstances present when the contract was entered.[25] Citing this "loophole," more recent Supreme Court decisions have not hesitated to examine the policy drafting history of particular provisions in order to understand them "in light of the circumstances" surrounding the drafting of the policy and imposition of those terms on the Policyholder.

So, for example, in *Balandran v. Safeco Ins. Co. of America*, 972 S.W.2d 738 (Tex.1998), the Texas Supreme Court considered a question certified from the Fifth Circuit involving insurance coverage for foundation damage under a standard form of homeowners' policy approved by the Texas Insurance Commission. The Court examined not only the text of the insurance provision at issue, but also considered the drafting history and administrative agency comments as applicable "circumstances" surrounding the promulgation of this policy form.[26]

Likewise, in the very recent case of *King v. Dallas Fire Ins. Co*., 85 S.W.3d 185, 192 (Tex. 2002), the Court cited ritually to the Eight Corners rule but did not feel it necessary to provide even a cursory justification before undertaking an extensive examination of the evolution of the standard liability policy's wording pertaining to coverage of the alleged incident as an "occurrence." The Court reviewed the history of policy wording modifications since 1966, including the stated rationale for many of the interim changes in policy wording over the evolution of later forms, in order to augment the Court's determination that the policy wording unambiguously provided coverage to the

---

[24] *See also In Re American Home Assur. Co.*, 2002 WL 1969266 (Tex. App. - Texarkana August 27, 2002, no pet.) (limiting discovery of extraneous evidence as to the meaning of the insurance policy's pollution coverage provision, pending determination by the trial court as a matter of law that the provision is ambiguous).

[25] 907 S.W.2d at 520.

[26] *Id.* at 741-42.

Policyholder against claims alleging derivative liability for the acts of the Policyholder's employee. This looks on its face very like the sort of drafting history the Court refused to consider for very similar purposes in *CBI*, yet the Court in *King* makes no attempt to justify or distinguish its reliance on such extrinsic evidence in order to interpret the import of unambiguous policy wording.

Given the developments trending away from *CBI*'s approach, as exemplified in *Balandran* and *sub silencio* in *King*, the time may be ripe for reconsideration of the role of drafting history in determining the purpose and effect of problematic insurance policy provisions for purposes of determining the duty to Defend, whether such provisions are found to be actually ambiguous or not.

VI. CONCLUSION

The Duty to Defend originates in the contract of insurance in third-party liability policies. Under longstanding Texas law, courts determine whether the Insurer has a Duty to Defend by examining only the factual allegations of the most recent pleading together with the insurance policy wording. If the pleading states even a single claim potentially within the coverage of the policy, the Insurer must defend the entire suit, whether the allegations are true or not, and regardless of the Insurer's or Policyholder's knowledge of the true facts.

Thus, the Duty to Defend is often said to be "broader" than the Duty to Indemnify, which is determined on the basis of actual evidence and testimony developed in discovery and at trial. Whether or not the Duty to Defend is broader, narrower, or coextensive with the Duty to Indemnify depends, however, on the interplay between the allegations of the pleading and the actual facts supporting the Policyholder's liability for the damages asserted.

In order to interpret the insurance policy, courts utilize standard rules of contract construction, as well as several rules of construction particularly applicable to insurance which invariably disfavor the Insured and favor the Policyholder and coverage. When implementing the Eight Corners rule, Texas courts examine the factual allegations of the pleading and not the legal theories asserted. The court is not bound by the characterization given to facts asserted by the claimant, but is free to apply the alleged facts as appropriate to the legal remedies asserted and the coverage afforded by the policy. In one case, the court may reject a claimant's notion of a "negligent occurrence" where the facts clearly demonstrate intentional conduct and harm (*Griffin*), whereas in other circumstances a court may require coverage based on factual allegations that describe a covered claim for "violation of the right of privacy" even where that cause of action is not actually asserted by the claimant (*Green Tree*).

In all events, the court's ability to impose or reject a Duty to Defend in accordance with the Eight Corners rule depends on whether the pleading alleges facts sufficient to determine that the claim is potentially within the coverage of the policy or not. Under the historical "Fact" pleading regime in which the Eight Corners rule first developed, this would not have presented much of a problem since all facts necessary to support a judgment were required to be pled with specificity.

Under modern "Notice" pleadings, however, few facts need be pled, and the plaintiff has broad latitude to plead or not plead facts relevant to the insurance coverage available to the defendant Policyholder.

The liberality of amendment available under "Notice" pleadings in Texas can result in situations where the Duty to Defend is not owed under one pleading, even though it is owed under a prior or subsequent pleading, all dependent on the facts which the claimant deigns to allege. This changeable coverage regime raises significant questions whether a declaratory judgment favoring an Insurer (or Policyholder) on the Duty to Defend has any finality or preclusive effect, where the Duty may hinge on the variability of each amendment to the pleading. The problem is even more pronounced where courts in some circumstances are authorized under *Griffin* to enter judgment on an Insured's ultimate Duty to Indemnify based on the Insured's lack of a Duty to Defend under a particular pleading, but the supposed finality of such a judgment can be undermined by a simple amendment to that pleading.

Applying the Eight Corners rule is problematic where the pleading fails to provide sufficient facts to determine potential coverage, and the courts must decide whether to consider extrinsic evidence to determine the Duty to Defend. Ostensibly, most courts favor application of extrinsic evidence only as to those issues pertaining to the Policyholder's coverage under the policy, and do not allow extrinsic evidence on issues that affect or involve liability facts pertinent to the underlying suit brought by the claimant against the Policyholder. In practice, some courts seem to ignore the distinction and they may be all too willing to allow the parties to develop evidence that may pertain to liability issues in the underlying suits.

Prior pronouncements of the Texas Supreme Court have supported a strict application of the Eight Corners rule, limited to the pleading and policy, only. There are indications that the Court is concerned about the application of extrinsic evidence to determine the Duty to Defend, and it may well be looking for an opportunity to resolve the issue. Moreover, recent decisions of the Court indicate that it may be loosening its prior rigorous restrictions against using extrinsic evidence of policy draftsmanship to interpret or illuminate the extent of coverage afforded by the insurance. It remains to be seen whether and to what extent the Court clarifies these issues in future cases.