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Fifth Circuit Asks Texas Supreme Court to Decide Whether Policy-Language Exception to "Eight-Corners Rule" Is Permissible Under Texas Law

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Many jurisdictions apply some variation of the "eight-corners rule" in assessing an insurance carrier's duty to defend a third-party lawsuit brought against its insured. Under the eight-corners rule, the duty to defend is determined by the claims alleged in the underlying petition and the coverage provided in the policy. The rule takes its name from the fact that only two documents are ordinarily relevant to the determination of the duty to defend: the policy and the pleadings of the third-party claimant. Generally, facts outside the pleadings, even those easily ascertained, are not material to the determination and allegations against the insured are liberally construed in favor of coverage.

While some jurisdictions offer exceptions to the eight-corners rule, Texas state courts have consistently applied the eight-corners rule without any clear exception in determining whether a duty to defend is triggered. Recently, however, the U.S. District Court for the Northern District of Texas relied on extrinsic evidence in relieving an insurer of its duty to defend or indemnify. On the subsequent appeal, the Fifth Circuit Court of Appeals certified a question of law to the Texas Supreme Court seeking clarification of whether a policy-language exception to the eight-corners rule is permissible under Texas law. Some background on the eight-corners rule in Texas and a possible limited exception.

In *State Farm Lloyd's v. Janet Richards et al.*, 2019 WL 4267354 (Sept. 9, 2019), a 10-year-old boy died in an ATV accident at his grandparents' house. The boy's mom sued the grandparents, the Richards, essentially alleging that they were negligent in failing to supervise and instruct the boy. The Richards asked their insurer, State Farm, to defend (and if necessary, indemnify) them. State Farm refused and sought a declaration in federal court that it had no duty to defend or indemnify. In doing so, State Farm argued two exclusions barred coverage and relied on extrinsic evidence. The first exclusion, the "motor-vehicle exclusion," excluded coverage for bodily injury arising from the use of an ATV *while off an insured location*. Although the complaint was silent as to the location of the accident, 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. The other exclusion—the "insured exclusion"—excluded coverage for bodily injury to any insured, which includes "you" and your relatives *if residents of your household*. State Farm attached the Richards' admission that they were the boy's grandparents, as well as an order appointing them as joint-managing conservators in order to show that the boy was a "resident of [the Richards'] household." Again, the complaint was silent as to the boy's residency.

The parties filed cross summary-judgment motions. The Richards argued that under Texas's eight-corners rule State Farm could not rely on extrinsic evidence to prove up a policy exclusion, and because the complaint was silent as to critical facts establishing application of either exclusion State Farm owed a duty to defend. The district court disagreed and, finding that the extrinsic evidence satisfied both exclusions, granted summary judgment for State Farm.

The district court held that 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." According to the district court, the policy at issue in *Richards* did not require the carrier to defend all actions against its insured regardless of whether the allegations of the suit are groundless, false or fraudulent, and therefore, did not define the duty to defend as broadly as those policies typically at issue in cases applying the eight-corners rule. The district court reasoned that those cases in which an insurance policy provides that the insurer must defend any suit brought against its insured "even if the allegations of the suit are groundless, false or fraudulent," rely upon the eight-corners or complaint-allegation rule to determine the duty to defend. As the district court concluded that State Farm's duty to defend arose only if a suit was brought to which the coverage applies, it held that the eight-corners rule was not applicable, and extrinsic evidence was admissible to make that determination.

The Fifth Circuit was not so sure. The Fifth Circuit recognized that federal courts applying Texas law have utilized a limited exception to the eight-corners rule under certain circumstances, although the exception has not been expressly adopted. In *Northfield Ins. Co. v. Loving Home Care, Inc.,* for example, the Fifth Circuit suggested that if the Texas Supreme Court were to recognize an extrinsic-evidence exception to the eight-corners rule, it would do so only 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. Although the Texas Supreme Court has never expressly adopted this two-pronged exception, federal courts (applying Texas law) have assumed its viability because the Texas Supreme Court has cited it with approval. *See e.g., GuideOne Elite Ins. Co. v. Fielder Rd. Baptist Church*; *Pine Oak Builders, Inc. v. Great Am. Lloyds Ins. Co.* Nevertheless, according to the Fifth Circuit the Texas Supreme Court has yet to decide a case that fits within this narrow exception.

In sum, the Fifth Circuit reasoned that there is no controlling Texas Supreme Court case law determining whether there's a policy-language (or other) exception to the eight-corners rule. As such, the Fifth Circuit turned to the Texas Supreme Court to answer a certified question of whether the policy-language exception relied upon by the district court is a permissible exception to the eight-corners rule under Texas law. Although it is unclear whether and how the Texas Supreme Court will answer the certified question, this is an issue that has been, and will likely continue to be, the subject of insurance litigation throughout Texas.