

# **DECLARATORY JUDGMENTS**

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## I. INTRODUCTION

This paper will address the ever-increasing use of declaratory judgments to determine insurance coverage and, in particular, the issues of who is a proper party to a declaratory judgment action and the proper scope of a court's inquiry.

## II. PROPER PARTIES TO DECLARATORY JUDGMENT ACTIONS

A declaratory judgment is a judicial determination of the rights of respective parties, as opposed to coercive relief or damages. The purpose of declaratory judgments is to settle and afford relief from uncertainty and insecurity with respect to rights, status, and other legal relations. Declaratory judgments can be brought in federal court pursuant to 28 U.S.C. § 2201 or in state court under Chapter 37 of the Civil Practice and Remedies Code.

Declaratory judgments play a big role in determining the duty to defend in that insurers frequently initiate declaratory judgments to resolve duty to defend disputes. Because the duty to defend is a question of law, declaratory judgments are typically disposed of by summary judgment.

Although Texas courts have had no problem entertaining a declaratory judgment on the duty to defend issue, the traditional rule—until fairly recently—was that the duty to indemnify issue had to await resolution of the underlying lawsuit. *See Firemen's Ins. Co. v. Burch*, 442 S.W.2d 331 (Tex. 1968). In 1997, however, the Supreme Court of Texas held that “the duty to indemnify is justiciable before the insured'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.” *See Farmers Tex. County Mut. Ins. Co. v. Griffin*, 955 S.W.2d 81, 84 (Tex. 1997). Thus, *if and only if* the court declares that there is no duty to defend, the court may also rule (prior to resolution of the underlying litigation) that no duty to indemnify exists. *See Foust v. Ranger Ins. Co.*, 975 S.W.2d 329, 332 n.1 (Tex. App.—San Antonio 1998, writ denied) (noting that the duty to indemnify is not justiciable prior to resolution of the underlying litigation where the insurer's duty to defend is triggered). If a court rules that a duty to defend exists, however, it must await the resolution of the underlying lawsuit before ruling on the duty to indemnify. *See Northfield Ins. Co. v. Loving Home Care, Inc.*, 363 F.3d 523, 537 (5<sup>th</sup> Cir. 2004); *Mt. Hawley Ins. Co. v. Steve Roberts Custom Builders, Inc.*, 215 F. Supp. 2d 783, 793 (E.D. Tex. 2002); *Gehan Homes, Ltd. v. Employers Mut. Cas. Co.*, 146 S.W.3d 833, 846 (Tex. App.—Dallas 2004, pet. filed).

Both Texas and federal courts have held that a lawsuit filed against an insured creates a justiciable controversy so as to afford jurisdiction. *See Griffin*, 955 S.W.2d at 82; *American States Ins. Co. v. Bailey*, 133 F.3d 363, 368 (5<sup>th</sup> Cir. 1998). Some differences between the Federal Declaratory Judgment Act and the Texas Declaratory Judgment Act exist, however, that are worthy of discussion. First, whereas attorneys' fees can be awarded to the prevailing party under the Texas statute, the federal statute does not provide for such an award. *See Utica Lloyd's of Tex. v. Mitchell*, 138 F.3d 208, 210 (5<sup>th</sup> Cir. 1998).<sup>1</sup> Second, in federal

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<sup>1</sup> While the Federal Declaratory Judgment Act does not provide for attorneys' fees, an insured in a federal declaratory judgment still can recover attorneys' fees to the extent the insured establishes a breach of contract. TEX. CIV. PRAC. & REM. CODE § 38.001.

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court, third-party claimants in pending litigation may intervene or be joined in the declaratory judgment action. *See Nat'l Am. Ins. Co. v. Breaux*, 368 F.Supp.2d 604, 621 (E.D. Tex. 2005) (holding that injured third parties were proper parties to a declaratory judgment action and that the court was entitled to declare the insurer's legal rights and relations with respect to both its insured and the injured third party); *Century Sur. Co. v. Hardscape Constr. Specialties*, 2006 WL 1948063 (N.D. Tex. July 13, 2006) (denying third-party claimant's motion for judgment asserting that it was not a proper party in the declaratory judgment action); *Bituminous Cas. Corp. v. Garcia*, 223 F.R.D. 308, 311 (N.D. Tex. 2004) (holding that third-party claimant had right to intervene in declaratory judgment action to protect its interest); *Ohio Cas. Ins. Co. v. Cooper Mach. Corp.*, 817 F. Supp. 45 (N.D. Tex. 1993). *But see Standard Fire Ins. v. Sassin*, 894 F. Supp. 1023 (N.D. Tex. 1995) (dismissing the injured third party as an improper party). In state courts, however, a third-party claimant has not been considered a proper party until final resolution of the liability issues. *See Feria v. CU Lloyd's of Texas*, 2001 WL 1263666 (Tex. App.—Dallas Oct. 23, 2001, no pet.); *Safeway Managing Gen. Agency for State & County Mut. Fire Ins. Co. v. Cooper*, 952 S.W.2d 861, 868–69 (Tex. App.—Amarillo 1997, no writ); *Gracida v. Tagle*, 946 S.W.2d 504, 506–07 (Tex. App.—Corpus Christi 1997, orig. proceeding); *Providence Lloyds v. Blevins*, 741 S.W.2d 604, 606 (Tex. App.—Austin 1987, no writ). *But see Richardson v. State Farm Lloyds Ins.*, 2007 WL 1018651 (Tex. App.—Ft. Worth April 5, 2007, pet. filed).

The fact that third-party claimants, at least traditionally, could not be added to declaratory judgment proceedings in state court has had the potential for creating

duplicative litigation. Technically, the non-party, third-party claimant cannot be bound by any issues resolved in the declaratory judgment proceeding and thus is free to relitigate the insurance issues. *See Dairlyland County Mut. Ins. Co. v. Childress*, 650 S.W.2d 770, 773–74 (Tex. 1983); *State & County Mut. Fire Ins. Co. v. Walker*, 228 S.W.3d 404, 411 (Tex. App.—Ft. Worth 2007, no pet.); *El Nagggar Fine Arts Furniture, Inc. v. Indian Harbor Ins. Co.*, 2007 WL 624535 (Tex. App.—Houston [1<sup>st</sup> Dist] March 1, 2007, pet. denied); *S. County Mut. Ins. Co. v. Ochoa*, 19 S.W.3d 452, 465 (Tex. App.—Corpus Christi 2000, no pet.); *Nat'l Sav. Ins. Co. v. Gaskins*, 572 S.W.2d 573 (Tex. Civ. App.—Ft. Worth 1978, no writ). Thus, federal courts may provide for more finality since a properly joined third-party claimant will be bound by the coverage court's determination as to coverage. *See State Farm Fire & Cas. Co. v. Fullerton*, 118 F.3d 374, 384 (5<sup>th</sup> Cir. 1997).

While the traditional rule in state court has been that a third-party claimant is not a proper party to a declaratory judgment action (at least until such time as the third-party claimant becomes a judgment creditor), the Supreme Court of Texas has implied that third-party claimants may have an interest in declaratory judgment actions. *See State Farm & Cas. Co. v. Gandy*, 925 S.W.2d 696, 714 (Tex. 1996) (stating that “[a] plaintiff who thinks a defendant should be covered by insurance may be willing to . . . assist in obtaining an adjudication of the insurer's responsibility”); *Griffin*, 955 S.W.2d at 84 (stating that “*Gandy* requires an insurer to either accept coverage or make a good faith effort to resolve coverage before adjudication of the plaintiff's claim, and *also suggests that the plaintiff may wish to participate in that litigation*”) (emphasis added); *see also Spruiell v. Lincoln Ins. Co.*, No. 07-97-0336-CV, 1998 WL 174722

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(Tex. App.—Amarillo Apr. 13, 1998) (unpublished) (resolving standing question in favor of injured third party and noting that “the Supreme Court has suggested that third parties may wish to participate in declaratory judgment actions involving the insured’s duty to defend”). And, like most courts, the Supreme Court of Texas has expressed its concern with duplicative litigation. Accordingly, if squarely presented with the issue, the Supreme Court may reassess whether a third-party claimant can be a proper party to a declaratory judgment action and, if so, in what circumstances.

The Supreme Court may get that chance in the *Richardson* case. In *Richardson*, the court of appeals held that a third-party claimant can bring a declaratory judgment action against a liability insurer to determine whether the insurer has a duty to defend and/or indemnify its insured. The facts are as follows.

Eunice and Bobby Richardson (the “Richardsons”) filed suit against Robert F. Kays (“Kays”) and State Farm Lloyds Insurance (“State Farm”). The Richardsons alleged that Kays killed their son by rolling over him with Kays’ vehicle. In the same lawsuit, the Richardsons sought a declaratory judgment action against Kays’ insurer, State Farm. In particular, the Richardsons sought a ruling that State Farm had a duty to defend and indemnify Kays.

State Farm, in response, filed a plea to the jurisdiction. In the plea to the jurisdiction, State Farm alleged that the trial court did not have subject matter jurisdiction because the Richardsons have no standing to litigate whether State Farm has a duty to defend or indemnify Kays under the condominium policy because (i) the Richardsons have suffered no injury by State Farm’s decision

not to defend Kays; (ii) no relationship exists between State Farm and the Richardsons under the policy; and (iii) State Farm’s duty to indemnify Kays is not ripe for adjudication because no judgment has been entered demonstrating Kays is legally liable to the Richardsons.

The trial court granted State Farm’s plea to the jurisdiction. Surprisingly, the court of appeals disagreed. In doing so, the court of appeals looked to the Supreme Court of Texas’ opinion in *Farmers Texas County Mutual Insurance Company v. Griffin*, 955 S.W.2d 81 (Tex. 1997). In *Griffin*, the Supreme Court s approved of the use of declaratory judgment actions to resolve insurance coverage issues. Even so, the *Richardson* court took the *Griffin* holding one step further by concluding that “a declaratory judgment action is permissible when brought by a third party seeking to have the insurance company defend or indemnify for the conduct of its insured.” *Richardson*, 2007 WL 1018651, at \*5.

It is common practice for insurers to include third-party claimants as parties to declaratory judgment actions. Oftentimes, insurers add third-party claimants as defendants in declaratory judgment actions against insureds so as to bind the third-party claimant to any ruling on coverage made in the declaratory judgment action.<sup>2</sup> It appears the Ft. Worth Court of Appeals believed that it should be a two-way street.

It is questionable, however, whether a third-party claimant is a proper party to a declaratory judgment action on coverage, regardless of whether the third-party claimant initiates the declaratory judgment

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<sup>2</sup> As noted previously, a third-party claimant is not bound by a coverage determination made in a declaratory judgment action in which it is not a party.

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action, intervenes in an ongoing declaratory judgment action between an insurer and its insured, or is made a defendant in the declaratory judgment action by the insurer. Simply put, Texas is **not** a direct action state and the third-party claimant is a stranger to the policy until such time as the third-party claimant becomes a judgment creditor.

Accordingly, at least historically, most Texas state courts have concluded that a third-party claimant is neither a necessary party nor an indispensable party to a declaratory judgment action—at least prior to the point at which the third-party claimant becomes a judgment creditor. As noted above, however, federal courts have taken a more liberal view and, for the most part, have allowed third-party claimants to be joined or to intervene into declaratory judgment actions.

The Ft. Worth Court of Appeals believed that the *Griffin* case changed the law in Texas. It is questionable whether the Supreme Court of Texas will see it that way. Notably, in *Griffin*, the Supreme Court of Texas did not address whether a third-party claimant should be made a party to a declaratory judgment action. Rather, the Supreme Court simply noted that a declaratory judgment action is an appropriate mechanism for the insurance company to utilize in seeking a declaration that it is not obligated to defend or indemnify its insured in a suit brought by a third party. While it is true that the *Griffin* court suggested that the third-party claimant “may wish to participate in [the declaratory judgment],” the court’s comment in this regard arguably was dicta. *Griffin*, 955 S.W.2d at 84. When directly presented with the issue, it is more likely that the Supreme Court of Texas will adhere to the longstanding principle that a third-party claimant has no standing to initiate a

declaratory judgment action against a liability insurer until such time as the third-party claimant becomes a judgment creditor. Even so, given the court’s dislike for duplicative litigation, it will be interesting to see whether the court allows a third-party claimant to be joined as a party to a declaratory judgment action initiated by an insurer against its insured. Likewise, it will be interesting to see whether the court will allow a third-party claimant to intervene into an existing declaratory judgment action between an insurer and its insured.

### **III. THE GENERAL CONTOURS OF THE DUTY TO DEFEND**

Since most declaratory judgments involve the issue of whether an insurer has a duty to defend, it is essential to focus on how courts determine the duty to defend and what evidence is admissible, if any, to determine the duty to defend. Texas courts apply the “eight corners” rule to determine whether an insurer has a duty to defend its insured. See *GuideOne Elite Ins. Co. v. Fielder Road Baptist Church*, 197 S.W.3d 305, 308 (Tex. 2006); *Nat’l Union Fire Ins. Co. v. Merchants Fast Motor Lines, Inc.*, 939 S.W.2d 139, 141 (Tex. 1997); *Northfield Ins. Co. v. Loving Home Care, Inc.*, 363 F.3d 523, 528–35 (5<sup>th</sup> Cir. 2004). In undertaking the “eight corners” analysis, a court must compare the allegations in the live pleading to the insurance policy without regard to the truth, falsity, or veracity of the allegations. See *King v. Dallas Fire Ins. Co.*, 85 S.W.3d 185, 191 (Tex. 2002); *Northfield*, 363 F.3d at 528. Thus, at least in most circumstances, only two documents are relevant to the duty to defend analysis: (i) the insurance policy; and (ii) the pleading of the third-party claimant. See *King*, 85 S.W.3d at 187. Facts ascertained before suit, developed in the process of litigation, or determined by the ultimate outcome of the

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suit do not affect the duty to defend. *See Trinity Universal Ins. Co. v. Cowan*, 945 S.W.2d 819, 829 (Tex. 1997); *Northfield*, 363 F.3d at 528. Accordingly, except in very limited circumstances, the duty to defend is a question of law. *See State Farm Gen. Ins. Co. v. White*, 955 S.W.2d 474, 475 (Tex. App.—Austin 1997, no writ); *State Farm Lloyds v. Kessler*, 932 S.W.2d 732, 736 (Tex. App.—Ft. Worth 1996, writ denied).

The Supreme Court of Texas has explained the “eight corners” rule in the following way:

Where the [complaint] does not state facts sufficient to clearly bring the case within or without the 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. Stated differently, in case of doubt as to whether or not the allegations of a complaint against the insured state a cause of action within the coverage of a liability policy sufficient to compel the insurer to defend the action, such doubt will be resolved in the insured’s favor.

*Merchants*, 939 S.W.2d at 141 (quoting *Heyden Newport Chem. Corp. v. Southern Gen. Ins. Co.*, 387 S.W.2d 22, 26 (Tex. 1965)). The above quote from the Supreme Court of Texas and the case law (both state and federal) that has followed reveals the following important contours of the duty to defend:

- An insurer is required to defend its insured if the allegations state a *potential* claim for coverage under the policy.
- The truth or veracity of the allegations is irrelevant—all factual allegations must be taken as true.
- The allegations should be interpreted liberally with any doubts being resolved in favor of the duty to defend.
- Insurers are not, however, required to read facts into the pleadings and/or imagine factual scenarios that might trigger coverage.
- When a petition alleges multiple or alternative causes of action, the insurer must examine each separate allegation to determine whether it has a duty to defend. If one alternative cause of action or allegation is within the terms of the policy, the insurer has a duty to defend the entire lawsuit.
- The proper focus is on the factual allegations that establish the origin of the damages alleged in the petition rather than on the legal theories asserted in the petition.

In short, an insurer has a duty to defend a lawsuit against its insured *unless* it can establish that a comparison of the policy with the complaint or petition shows on its face that no potential for coverage exists. Stated otherwise, an insurer can refuse to provide a defense only when the facts as alleged fall outside of the coverage grant or when an exclusion applies that negates any potential for coverage.

While it sounds simple enough, an issue exists as to how far an insurer needs to go in liberally construing a pleading in favor of the duty to defend. On the one hand, courts have continuously held that pleadings should be liberally construed with all doubts and reasonable inferences resolved in favor

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of a duty to defend. On the other hand, courts also have continuously held that the liberal standards of the “eight corners” rule do not mandate that courts imagine factual scenarios that might trigger coverage. Adding to the confusion is a steady stream of inconsistent applications of the so-called “eight corners” rule. For example, when it comes to determining trigger, what do you do if the petition or complaint is completely date-deprived? Likewise, when applying the “subcontractor exception” to the “your work” exclusion or in determining additional insured status for a general contractor on a construction project, what do you do if the petition or complaint is silent as to the use of subcontractors? Recently, the trend seems to be that courts appear willing to make logical inferences from pleaded facts while, at the same time, courts will refuse to completely fill in gaps in pleadings. Oftentimes, the debate centers on whether it is even appropriate to use extrinsic evidence.

### **IV. THE EXTRINSIC EVIDENCE DEBATE**

The role of extrinsic evidence in the duty to defend analysis continues to be an area of confusion and debate. As a general rule, the use of extrinsic evidence to either create or defeat a duty to defend violates a strict “eight corners” rule. Most jurisdictions, however, recognize an exception to the “eight corners” rule when the insurer knows or reasonably should know facts that would establish coverage. *See* ROBERT H. JERRY, II, UNDERSTANDING INSURANCE LAW § 111[c][2] (2d ed. 1996). A leading insurance treatise concurs with this approach:

The existence of the duty to defend is normally determined by an analysis of the pleadings. Extrinsic evidence can, however, serve to

create a duty to defend when such a duty would not exist based solely on the allegations in the complaint.

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An insurer should not be able to escape its defense obligation by ignoring the true facts and relying on either erroneous allegations in the complaint or the absence of certain material allegations in the complaint. The insurer’s sole concern should be with whether the judgment that may ultimately be entered against the insured might, either in whole or in part, be encompassed by the policy. There is authority to the contrary, holding that the insurer’s defense obligation should be determined solely from the complaint, but such authority is unreasoned and consists merely of a blind adherence to the general rule in a situation in which the general rule was never intended to apply.

ALLAN D. WINDT, INSURANCE CLAIMS & DISPUTES: REPRESENTATION OF INSURANCE COMPANIES AND INSURED § 4:3 (4th ed. 2001); *see also* Ellen S. Pryor, *Mapping the Changing Boundaries of the Duty to Defend in Texas*, 31 TEX. TECH L. REV. 869, 890–98 (2000).

California, for example, permits both the insured and the insurer to use extrinsic evidence in determining the duty to defend. Texas courts, to put it kindly, have been sporadic in their application of the “eight corners” rule. In June 2006, the Supreme Court of Texas weighed in on the debate. *See GuideOne Elite Ins. Co. v. Fielder Road Baptist Church*, 197 S.W.3d 305 (Tex. 2006). Unfortunately, the opinion has

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provided more questions than it did answers. Prior to discussing *Fielder Road*, a little bit of historical background is in order.

### **A. History of Extrinsic Evidence Prior to 2006**

Prior to 2006, although the Supreme Court had hinted that Texas was a strict “eight corners” state, the Supreme Court had never squarely rejected an exception to the “eight corners” rule. Whether and in what instances an exception existed basically was left to the trial and appellate courts to decide on a case-by-case basis. While a vast majority of the cases declined to recognize or apply any exception to the “eight corners” rule, such was not always the result.

Several state appellate courts have concluded that the so-called “eight corners” rule is not absolute. *See Utica Lloyd’s of Tex. v. Sitech Eng’g Corp.*, 38 S.W.3d 260, 263 (Tex. App.—Texarkana 2001, no pet.) (“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 in making the determination.”); *Mid-Continent Cas. Co. v. Safe Tire Disposal Corp.*, 16 S.W.3d 418, 421 (Tex. App.—Waco 2000, pet. denied) (“The exception to this general rule occurs [w]hen the petition in the Underlying Litigation does not allege facts sufficient for a determination of whether those facts, even if true, are covered by the policy.”); *Providence Wash. Ins. Co. v. A&A Coating, Inc.*, 30 S.W.3d 554, 556 (Tex. App.—Texarkana 2000, pet. denied) (“However, there are certain limited circumstances where extrinsic evidence beyond the ‘eight-corners’ will be allowed to aid in the determination of whether an insurer has a

duty to defend.”); *Tri-Coastal Contractors, Inc. v. Hartford Underwriters Ins. Co.*, 981 S.W.2d 861, 863–64 (Tex. App.—Houston [1<sup>st</sup> Dist.] 1998, pet. denied) (recognizing limited exceptions to the “eight corners” rule); *State Farm Fire & Cas. Co. v. Wade*, 827 S.W.2d 448, 451–52 (Tex. App.—Corpus Christi 1992, writ denied) (allowing extrinsic evidence to be used to fill gaps in a petition or complaint); *Cook v. Ohio Cas. Ins. Co.*, 418 S.W.2d 712, 715–16 (Tex. Civ. App.—Texarkana 1967, no writ.) (holding extrinsic evidence allowed to show automobile involved in accident was excluded from coverage); *Int’l Serv. Ins. Co. v. Boll*, 392 S.W.2d 158, 161 (Tex. Civ. App.—Houston 1965, writ ref’d n.r.e.) (holding extrinsic evidence allowed to show person involved in accident was excluded from policy).

Some federal courts have likewise concluded that the “eight corners” rule may not be absolute. *See Primrose Operating Co. v. Nat’l Am. Ins. Co.*, 382 F.3d 546, 552 (5<sup>th</sup> Cir. 2004) (permitting the review of extrinsic evidence when the underlying complaint did not contain sufficient facts to determine whether a potential for coverage exists); *Mid-Continent Cas. Co. v. Oney*, 2004 WL 1175569 (N.D. Tex. May 27, 2004) (noting that extrinsic evidence can be considered to determine fundamental coverage issues); *Westport Ins. Corp. v. Atchley, Russell, Waldrop & Hlavinka, L.L.P.*, 267 F. Supp. 2d 601, 612–25 (E.D. Tex. 2003) (recognizing that extrinsic evidence may be used to establish fundamental coverage facts, such as whether the party bringing the claim is a named insured under the policy); *John Deere Ins. Co. v. Truckin’ U.S.A.*, 122 F.3d 270, 272 (5<sup>th</sup> Cir. 1997) (holding that extrinsic evidence can be considered where the allegations in the underlying petition are not sufficient to determine whether a potential



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for coverage exists); *Sw. Tank & Treater Mfg. Co. v. Mid-Continent Cas. Co.*, 243 F. Supp. 2d 597, 602 (E.D. Tex. 2003) (holding that the consideration of extrinsic evidence is warranted in certain circumstances); *Matagorda Ventures, Inc. v. Travelers Lloyds Ins. Co.*, 203 F. Supp. 2d 704, 714 (S.D. Tex. 2000) (noting that the “eight corners” rule does not apply rigidly in every case).

The *Wade* decision from the Corpus Christi Court of Appeals, at least traditionally, had been the most widely cited case in connection with the use of extrinsic evidence under Texas law. The facts of *Wade* are as follows. Williamson owned a boat that was insured by State Farm. Williamson and a passenger set off from Port O’Connor, Texas in Williamson’s boat, but subsequently they were found drowned in the Gulf of Mexico. The passenger’s estate brought suit against Williamson. State Farm tendered a defense under a reservation of rights and filed a declaratory judgment action to determine its policy obligations. The applicable policy contained a “business pursuits” exclusion. The problem, according to the court, was that the petition did not contain sufficient factual allegations to determine whether State Farm owed a defense:

Texas courts allow extrinsic evidence to be admitted to show a lack of a duty to defend. We conclude that the underlying petition, read broadly, does not address the issue of how the boat was used, which is an essential fact for determining coverage under this private boatowner’s policy, and whether State Farm has a duty to defend the wrongful death suit. It makes no sense to us, in light of these holdings, to say that extrinsic

evidence should not be admitted to show that an instrumentality (boat) was being used for a purpose explicitly excluded from coverage particularly, when doing so does not question the truth or falsity of any facts alleged in the underlying petition filed against the insured.

*Wade*, 827 S.W.2d at 453. Thus, under the *Wade* exception to the “eight corners” rule, extrinsic evidence may be admitted in a declaratory judgment proceeding when the petition does not set out facts sufficient to allow a determination of whether those facts—even if true—would state a covered claim. Stated differently, under *Wade*, extrinsic evidence can be admitted where a “gap” in the pleadings exists.

*Wade* has been cited favorably by numerous federal courts. *See Guar. Nat’l Ins. Co. v. Vic Mfg. Co.*, 143 F.3d 192, 194–95 (5<sup>th</sup> Cir. 1998) (acknowledging a “narrow exception” to the “eight corners” rule when a petition does not contain sufficient facts to enable a court to determine if the duty to defend exists); *W. Heritage Ins. Co. v. River Entm’t*, 998 F.2d 311, 313 (5<sup>th</sup> Cir. 1993) (same); *Acceptance Ins. Co. v. Hood*, 895 F. Supp. 2d. 131, 134 n.1 (E.D. Tex. 1995) (same). In contrast, Texas state courts generally had rejected the *Wade* approach to extrinsic evidence. In *Tri-Coastal*, for example, the court noted that “we are unable to find other Texas appellate courts that have followed the *Wade* rationale.” *Tri-Coastal*, 981 S.W.2d at 863–64.

Although rejecting *Wade*, the *Tri-Coastal* court did recognize certain instances when extrinsic evidence may be permissible:

In Texas, extrinsic evidence is permitted to show no duty to defend only in very limited

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circumstances, for example where the evidence is used to disprove the fundamentals of insurance coverage, such as whether the person sued is excluded from the policy, whether a policy contract exists, or whether the property in question is insured under the policy.

*Id.* at 863 n.1. The *Tri-Coastal* court adopted what can be called a “fundamentals of insurance exception” to the “eight corners” rule. *See, e.g., Landmark Chevrolet Corp. v. Universal Underwriters Ins. Co.*, 121 S.W.3d 886, 890–91 (Tex. App.—Houston [1<sup>st</sup> Dist.] 2003, pet. filed); *Chapman*, 2005 WL 20541, at \*7–\*8. In a treatise-like opinion, District Judge Folsom essentially adopted the *Tri-Coastal* analysis and, in so doing, concluded:

Only in very limited circumstances is extrinsic evidence admissible to rebut [the presumption of coverage]. These instances are ones in which “fundamental” policy coverage questions are resolved by “readily determined facts.”

*Westport*, 267 F. Supp. 2d at 621. The *Westport* opinion is perhaps the most comprehensive discussion of Texas case law on the extrinsic evidence issue.

Both *Westport* and *Tri-Coastal*, at least impliedly, recognized that the extrinsic evidence debate may turn on the *type* of extrinsic evidence being considered. Generally speaking, extrinsic evidence can be broken down into three categories: (i) evidence that relates only to liability; (ii) evidence that relates only to coverage; and (iii) mixed or overlapping evidence that relates to both liability and coverage. *See Pryor, Mapping Changing Boundaries,*

*supra*, at 869; *see also* Randall L. Smith & Fred A. Simpson, *Extrinsic Facts & The Eight Corners Rule Under Texas Law—The World is Not as Flat as Some Would Have You Believe*, 46 S. TEX. L. REV. 463 (2004).

In the past couple of years, the confusion has reached new heights. In *Northfield*, which was issued in March of 2004, the Fifth Circuit reviewed the long and winding road of Texas case law and made an “*Erie* guess that the current Texas Supreme Court would not recognize any exception to the strict eight corners rule.” *Northfield*, 363 F.3d at 531. The *Northfield* court went on to say that:

[I]n the unlikely situation that the Texas Supreme Court were to recognize an exception to the strict eight corners rule, we conclude any exception would only apply in very limited circumstances: 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.

*Id.* (emphasis in original).

Following *Northfield*, one would have expected the extrinsic evidence issue to be settled within the Fifth Circuit (at least until such time as the Supreme Court of Texas weighed in on the issue). Expectations do not always come true. Two months after *Northfield* was issued, a federal district court in Lubbock held that “[t]his court may properly consider extrinsic evidence on the duty to defend only in the very narrow circumstance of ‘where fundamental policy

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coverage questions can be resolved by readily determined facts that do not engage the truth or falsity of the allegations in the underlying suit.” *Oney*, 2004 WL 1175569, at \*5 (citing *Northfield*, 633 F.3d at 530). Given the *Erie* guess made in *Northfield*, the *Oney* analysis appears to be flawed. Or was it? A few months later, in August of 2004, the Fifth Circuit issued another opinion, concluding that “[f]act finders . . . may look to extrinsic evidence if the petition ‘does not contain sufficient facts to enable the court to determine if coverage exists.’” *Primrose*, 382 F.3d at 552 (citing *Western Heritage*, 998 F.2d at 313). Ironically, the judge that authored *Primrose* is the very same judge that authored *Northfield*.

Right about the same time, the Fort Worth Court of Appeals issued its opinion in *Fielder Road Baptist Church v. GuideOne Elite Insurance Co.*, 139 S.W.3d 384, 388–89 (Tex. App.—Ft. Worth 2004), *aff’d*, 197 S.W.3d 305 (Tex. 2006). The facts are as follows: Jane Doe filed a sexual misconduct lawsuit against the Church and Charles Patrick Evans. In her petition, Jane Doe alleged that “[a]t all times material herein from 1992 to 1994, Evans was employed as an associate youth minister and was under Fielder Road’s direct supervision and control when he sexually exploited and abused Plaintiff.” The Church tendered the lawsuit to GuideOne, who undertook the Church’s defense under a reservation of rights. A few months later, GuideOne initiated a declaratory judgment action. In the declaratory judgment action, GuideOne sought discovery of Evans’ employment history with the Church. Ultimately, the Church stipulated that Evans had ceased working at the Church *prior* to the time the GuideOne policy took effect. The trial court relied on the stipulation in granting GuideOne’s summary judgment. The court of appeals, however, reversed by concluding

that it was improper for the trial court to consider extrinsic evidence. In particular, despite recognizing that the allegations in the pleading may not have been truthful, the court of appeals rejected the use of extrinsic evidence in such circumstances because the extrinsic evidence at issue did not fall within the fundamentals of insurance exception. *Id.* In other words, the Fort Worth Court of Appeals essentially adopted the “fundamentals of insurance exception” from *Tri-Coastal*. The Supreme Court accepted the petition for review.

### B. The Supreme Court Weighs In

On June 30, 2006, the Supreme Court of Texas handed down its long-awaited opinion in *Fielder Road*. In so doing, the court agreed with the court of appeals and *declined* to adopt an exception to the “eight corners” rule. Nevertheless, the Supreme Court was careful to limit its decision to situations when the extrinsic evidence is “relevant both to coverage and the merits . . . .” *Fielder Road*, 197 S.W.3d at 310. More specifically, the court refused to adopt any exception to the “eight corners” rule for “liability only” or “overlapping/mixed fact” scenarios:

[W]ere we to recognize the exception urged here, we would by necessity conflate the insurer’s defense and indemnity duties without regard for the policy’s express terms. Although these duties are created by contract, they are rarely coextensive.

*Id.* at 310. Moreover, in reaching its decision, the court did not disapprove of other case law and commentary that discussed a “coverage only” exception to the “eight corners” rule. As noted in the prior section, and as recognized by the Supreme

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Court of Texas, authority exists for admitting extrinsic evidence in “coverage only” situations—at least when the “coverage only” evidence involves fundamental coverage facts that can be readily ascertained and are undisputed. Although allowing extrinsic evidence in such circumstances may technically violate a strict “eight corners” rule, the reality is that considering “coverage only” evidence does not violate the contractual underpinnings of the duty to defend. Moreover, insurers still will have to defend groundless, false, or fraudulent claims that otherwise state a potential for coverage. Under a “coverage only” exception, for example, insurers only will be able to avoid the duty to defend in situations when the insured has not paid premiums for a defense (e.g., when the defendant is not listed as an insured, or where the property is not scheduled on the policy). Unfortunately, the Supreme Court of Texas in *Fielder Road* did not expressly say one way or the other whether it would recognize the exception.

Subsequent to the issuance of *Fielder Road*, one court noted the following:

Although the Texas Supreme Court explicitly rejected the use of extrinsic evidence that was relevant both to coverage and to the merits of the underlying action, it did not rule on the validity of a more narrow exception that would allow extrinsic evidence solely on the issue of coverage. In fact, the language of the opinion hints that the court views the more narrow exception favorably. For example, the court specifically acknowledged that other courts recognized a narrow exception for extrinsic evidence that is relevant to the discrete issue of coverage

and noted that the Fifth Circuit had opined that, were any exception to be recognized by the Texas high court, it would likely be such a narrow exception.

*Bayou Bend Homes v. Scottsdale Ins. Co.*, 2006 WL 2037564 (S.D. Tex. July 18, 2006). And, subsequent to *Bayou Bend Homes*, several courts have applied a “coverage only” exception under Texas law. See, e.g., *B. Hall Contracting, Inc. v. Evanston Ins. Co.*, 447 F. Supp.2d 634, 647 (N.D. Tex. 2006) (holding that “coverage only” extrinsic evidence can be considered in the duty to defend analysis);<sup>3</sup> *Boss Management Services, Inc. v. Acceptance Ins. Co.*, 2007 WL 2752700 (S.D. Tex. Sept. 19, 2007) (recognizing a “coverage only” exception to the “eight corners” rule); *Roberts, Taylor & Sensabaugh, Inc.*, 2007 WL 2592748 (S.D. Tex. 2007) (same). Likewise, although not applying the exception, the Fifth Circuit has interpreted *Fielder Road* as permitting extrinsic evidence in “coverage only” scenarios. See *Liberty Mut. Ins. Co. v. Graham*, 2006 WL 3743108 (5<sup>th</sup> Cir. Dec. 21, 2006). Moreover, subsequent to *Fielder Road*, the Supreme Court has been vague on the issue. See *Lamar Homes, Inc. v. Mid-Continent Cas. Co.*, 2007 WL 2459193 (Tex. Aug. 31, 2007) (holding that the duty to defend must “generally be gleaned from the plaintiff’s complaint.”) (emphasis added).

Even if admission of “coverage only” facts is allowed, an insurer should not be

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<sup>3</sup> Interestingly, the court in *B. Hall* concluded that the “‘eight-corners or complaint-allegation rule’ is not applicable to this case” because the policy in question did not contain language requiring the insurer to defend suits that contain allegations that are “groundless, false, or fraudulent.” *B. Hall*, 447 F. Supp. 2d at 645. In so doing, the court placed too much emphasis on the missing language.

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permitted to use such evidence to contradict allegations in a petition. *See, e.g., Graham*, 473 F.3d at 602–03. Stated simply, while extrinsic evidence may be used in certain limited circumstances in which it is initially impossible to discern whether coverage is potentially implicated and when the extrinsic evidence goes solely to a coverage issue that does not overlap with the merits of the underlying lawsuit, extrinsic evidence cannot be used to contradict allegations—even untrue allegations—in a petition or complaint. *See Valley Forge Ins. Co. v. Shah*, 2007 WL 737490 (S.D. Tex. March 7, 2007) (“Even when the allegations appear to be untrue, the court ordinarily cannot consider extrinsic evidence to defeat an insurer’s duty to defend.”). Likewise, when a potential for coverage can be found from the face of a pleading, an insurer should not be permitted to develop extrinsic evidence through discovery or through the admission of extrinsic evidence in an effort to defeat the duty to defend. *See Fair Operating, Inc. v. Mid-Continent Cas. Co.*, 2006 WL 2242547 (5<sup>th</sup> Cir. Aug. 1, 2006) (affirming district court’s order refusing insurer’s request to undertake discovery of extrinsic evidence);<sup>4</sup> *Graham*, 473 F.3d at 602.

Given the uncertainty surrounding the *Fielder Road* opinion, it appears that the extrinsic evidence debate will continue until the Supreme Court of Texas once again weighs in on the issue. The Supreme Court may get that opportunity very soon. *See D.R. Horton-Texas, Ltd. v. Markel Int’l Ins. Co.*,

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<sup>4</sup> Courts in other jurisdictions have refused to allow an insurer to undertake discovery in a declaratory judgment when the underlying lawsuit remains pending. *See Harleysville Lake States Ins. Co. v. Granite Ridge Builders, Inc.*, 2007 WL 1662676 (N.D. Ind. June 7, 2007); *see also Old Republic Ins. Co. v. Chuhak & Tecson, P.C.*, 84 F.3d 998, 1002 (7<sup>th</sup> Cir. 1996).

2006 WL 3040756 (Tex App.—Houston [14<sup>th</sup> Dist.] Oct. 26, 2006, pet. filed).

In *D.R. Horton*, the Houston Court of Appeals addressed the duty to defend and extrinsic evidence issue in the context of an additional insured tender. In 2002, James and Cicely Holmes sued D.R. Horton alleging that their house contained latent defects that led to the propagation of toxic mold. The Holmes’ petition was silent about D.R. Horton’s use of subcontractors to construct the home. In particular, the Holmes’ petition did not name any subcontractors, nor did it make any reference to damage caused by any of D.R. Horton’s subcontractors. D.R. Horton, however, had extrinsic evidence that demonstrated that the alleged damages to the home were caused, at least in part, by work performed on D.R. Horton’s behalf by its masonry subcontractor. Accordingly, since D.R. Horton required its subcontractors to name it as an additional insured, D.R. Horton tendered the Holmes’ lawsuit to the liability carriers for the masonry subcontractor. Those insurers, however, declined to defend D.R. Horton based on the fact that the Holmes’ petition failed to mention the use of or otherwise reference any subcontractors.<sup>5</sup> In the coverage litigation against the additional insured carriers, D.R. Horton sought to introduce extrinsic evidence that the damages to the home were caused by the masonry subcontractor (i.e., the named insured). The trial court refused to permit the use of extrinsic evidence. The court of appeals, while recognizing that D.R. Horton “produced a significant amount of summary judgment evidence that . . . links [the

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<sup>5</sup> The additional insured endorsement limits the insurer’s liability to those claims arising out of the named insured’s (i.e., the masonry subcontractor) work for the additional insured (D.R. Horton).

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masonry subcontractor] to the injuries claimed by the Holmeses,” concluded that the trial court properly excluded the evidence. In particular, without explaining its basis for doing so, the court of appeals side-stepped the debate by classifying the extrinsic evidence before it as relating to *both* coverage and liability. *See D.R. Horton*, 2006 WL 3050756, at \*5 n.11.

D.R. Horton has filed a petition for review with the Supreme Court of Texas. In the petition for review, D.R. Horton refutes the contention that the extrinsic evidence related to both liability and coverage. Rather, D.R. Horton contends that the extrinsic evidence it sought to introduce went solely to coverage (i.e., additional insured status). D.R. Horton then urges the Supreme Court to take *Fielder Road* one step further by expressly adopting a “coverage only” exception to the “eight corners” rule.

Another opportunity will be in the *Pine Oak Builders* case. *See Pine Oak Builders, Inc. v. Great Am. Lloyds Ins. Co.*, 2006 WL 1892669 (Tex. App.—Houston [14<sup>th</sup> Dist.] July 6, 2006, pet. granted). One of the issues in *Pine Oak Builders* was whether the so-called “subcontractor exception” to the “your work” exclusion applied. The *Pine Oak Builders* case involved five underlying lawsuits. In four of the underlying lawsuits, the homeowners specifically alleged that Pine Oak Builders utilized subcontractors to construct the homes—thus falling within the “subcontractor exception” to the “your work” exclusion. In one of the underlying lawsuits, however, the homeowners failed to mention the use of subcontractors. Pine Oak Builders sought to introduce extrinsic evidence that it used subcontractors in all of the underlying lawsuits. The court of appeals refused to consider the extrinsic evidence. *See Pine Oak Builders*, 2006 WL

1892669, at \*5–\*6. In so doing, the court noted:

We recognize that the refusal to consider extrinsic evidence will inevitably result in some inequitable outcomes. Nonetheless, two factors stand at the forefront of our decision and trump any equitable considerations: (i) the Texas Supreme Court has only applied the eight-corners analysis in duty to defend cases and has resisted all opportunities to adopt a permissive extrinsic evidence stance in such cases, and (ii) the clear majority of courts of appeals that have addressed the issue, including most of the recent opinions, have rejected the permissive rule.

*Id.* at \*6. The Supreme Court has granted the petition for review in *Pine Oak Builders*. Accordingly, it will give the court an excellent opportunity to “clarify” the position set forth in *Fielder Road*.

### **V. DOES A FINDING OF NO DUTY TO DEFEND NECESSARILY MEAN NO DUTY TO INDEMNIFY?**

It is uniformly accepted that the duty to defend is broader than the duty to indemnify. *See Burlington Ins. Co. v. Tex. Krishnas, Inc.*, 143 S.W.3d 226, 229 (Tex. App.—Eastland 2004, no pet.); *E&L Chipping Co. v. Hanover Ins. Co.*, 962 S.W.2d 272, 274 (Tex. App.—Beaumont 1998, no writ); *Northfield*, 363 F.3d at 528. Accordingly, an insurer may have a duty to defend even when the adjudicated facts ultimately result in a finding that the insurer has no duty to indemnify. *See Utica Nat’l Ins. Co. v. Am. Indem. Co.*, 141 S.W.3d 198,

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203 (Tex. 2004); *Farmers Tex. County Mut. Ins. Co. v. Griffin*, 955 S.W.2d 81, 82 (Tex. 1997). In other words, it is well-settled that the duty to defend and the duty to indemnify are distinct and separate duties. *See Griffin*, 955 S.W.2d at 82; *Cowan*, 945 S.W.2d at 821–22. In contrast to the duty to defend, the duty to indemnify is not based on the third-party claimant’s allegations, but rather upon the actual facts that comprise the third party’s claim. *See Am. Alliance Ins. Co. v. Frito-Lay, Inc.*, 788 S.W.2d 152, 154 (Tex. App.—Dallas 1990, writ dism’d); *Canutillo Indep. Sch. Dist. v. Nat’l Union Fire Ins. Co.*, 99 F.3d 695, 701 (5<sup>th</sup> Cir. 1996). Simply put, extrinsic evidence is admissible to determine the duty to indemnify. *See Acceptance Indemnity Ins. Co. v. Maltez*, 2007 WL 2471481 (S.D. Tex. Aug. 28, 2007) (noting that the court may consider extrinsic evidence to determine the scope of the duty to indemnify). In fact, “[a]n insurer is not obligated to pay a liability claim until [the] insured has been adjudicated to be legally responsible.” *S. County Mut. Ins. Co. v. Ochoa*, 19 S.W.3d 452, 460 (Tex. App.—Corpus Christi 2000, no pet.). For this reason, the duty to indemnify is not ripe for determination prior to the resolution of the underlying lawsuit *unless* a court first determines, based on the “eight corners” rule, that there is no duty to defend and the same reasons that negate the duty to defend also negate any potential for indemnity. *See Griffin*, 955 S.W.2d at 82.

In most cases, the negation of the duty to defend also will negate the duty to indemnify. *See Griffin*, 955 S.W.2d at 84. This fact, however, oftentimes is overstated as an absolute rule. *See, e.g., Am. States Ins. Co. v. Bailey*, 133 F.3d 363 (5<sup>th</sup> Cir. 1998) (“Logic and common sense dictate that if there is no duty to defend then there must be no duty to indemnify.”); *see also Century Sur. Co. v. Hardscape Constr. Specialties*,

2006 WL 1948063 (N.D. Tex. July 13, 2006) (“Of course, when there is no duty to defend, there is also no duty to indemnify.”). Notably, a quick Westlaw or Lexis search will reveal dozens of cases that stand for the proposition that if there is no duty to defend, there can be no duty to indemnify. While oftentimes true, such a conclusion is by no means automatic. Even if an insurer obtains a judgment as to defense and indemnity based on a particular petition or complaint, for example, it is always possible that the petition or complaint can be amended to trigger a duty to defend. For example, in *Nautilus Insurance Co. v. Nevco Waterproofing, Inc.*, 2005 WL 1847094 (S.D. Tex. Aug. 3, 2005), the court noted as follows:

This Court’s ruling [on the duty to indemnify] is issued without prejudice and is based on the petition in the underlying suit at the time the court ruled. The Court does not intend to preclude Nevco from seeking indemnity from Evanston if Nevco is found liable on a theory that was not pleaded in Concierge’s operative petition when construed broadly.

*Id.* at \*3 n.6.<sup>6</sup> Similarly, in *Markel International Insurance Co. v. Campise Homes, Inc.*, 2006 WL 1662604 (S.D. Tex. June 6, 2006), the court concluded that:

The resolution of the duty to defend issue is not automatically dispositive of the issue of indemnity. An insurer’s duty to indemnify is distinct and separate

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<sup>6</sup> This decision was ultimately vacated and remanded by the Fifth Circuit based on mootness after the underlying action against the insured was dismissed after settlement was made with a major contractor.

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from its duty to defend . . . . However, “[l]anguage in some cases can be read to indicate that if the live pleading at the time a determination of the duty to indemnify is sought did not trigger the duty to defend, no duty to indemnify can be found.” For example, if the same basis that negates the duty to defend likewise negates any possible duty to indemnify, then a court may properly consider the issue of indemnity.

In the instant case, the Court cannot find that the same basis that negated the duty to defend negates any possible duty to indemnify. Due to the sloppy pleading in the underlying lawsuit, it remains a fundamental mystery when the alleged property damage occurred. The Wolfes’ did not allege property damage within the policy period, therefore, there is no duty to defend. However, this does not conclusively resolve the issue of indemnification. Presumably, the conclusion of the underlying lawsuit will clarify when the alleged damage occurred—outside or within the policy period. If the alleged damage occurred within the policy period, then there may be a duty to indemnify. It is impossible at this juncture to make a determination as to indemnification.

*Id.* at \*3 (internal citations omitted). Likewise, if a plaintiff brings a lawsuit against the insured alleging only intentional conduct but is granted a trial amendment alleging non-intentional conduct and obtains a judgment on the alternative

ground, the duty to indemnify should be triggered even though the insurer never defended. *See Trinity Universal Ins. Co. v. Cowan*, 945 S.W.2d 819, 825 n.4 (Tex. 1997) (“This holding does not affect a party’s right to introduce evidence of physical manifestations of mental anguish against a tortfeasor under the ‘fair notice’ rule . . . . Our holding extends only to the duty to defend under the complaint allegation rule.”); *see also Pryor, Mapping Changing Boundaries, supra*. Accordingly, the rule is better stated as follows: When no duty to defend exists, and no facts can be developed at the trial of the underlying lawsuit to impose coverage, an insurer’s duty to indemnify may be determined by summary judgment.

The *D.R. Horton* case provides the perfect example of a mistaken application of the “if no duty to defend, then no duty to indemnify” rule. As noted in the previous section, the *D.R. Horton* court concluded that no duty to defend existed because the underlying petition failed to mention the use of subcontractors so as to trigger additional insured status. After reaching this conclusion, the court stated as follows:

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. For this reason, the same arguments that disposed of Markel’s duty to defend also dispose of its duty to indemnify. Because the *Holmes* suit did not allege facts covered by the policy, even proof of those facts would not trigger coverage. We



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therefore affirm the trial court's summary judgment in favor of Markel on the issue of Markel's duty to indemnify.

*D.R. Horton*, 2006 WL 2040756, at \*6 (internal citations omitted). The court clearly was wrong in this regard. In particular, as noted in the opinion, D.R. Horton had produced ample summary judgment evidence demonstrating the requisite causal link between the named insured's work and D.R. Horton's liability. Even if such evidence is not admissible at the duty to defend context, no valid reason exists to ignore the extrinsic evidence at the duty to indemnify stage. In fact, since the duty to indemnify is based on *actual* facts, it is definitely proper for a court to consider extrinsic evidence.<sup>7</sup>

## **VI. CONCLUSION**

Declaratory judgments are a popular tool to determine an insurer's obligations to its insured. Nevertheless, significant issues remain such as whether the third-party claimant is a proper party and, if so, under what circumstances. Another significant issue is the proper scope of the court's inquiry in a declaratory judgment. More specifically, the primary issue is whether extrinsic evidence can be used at the duty to

defend stage. In addition, an issue exists as to whether a ruling that no duty to defend exists necessarily negates a duty to indemnify. The Supreme Court of Texas will soon have the opportunity to address these issues.

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<sup>7</sup> Insurers sometimes attempt an end run around the "eight corners" rule by trying to use extrinsic evidence on the duty to indemnify while the underlying lawsuit is pending. Assuming the extrinsic evidence would defeat the duty to indemnify, insurers then argue that no potential for coverage exists and thus no duty to defend. Such a tactic is wholly improper. When an insurer has a duty to defend, based on the "eight corners" rule, it is wholly improper to use extrinsic evidence during the pendency of the underlying lawsuit. The only exception to this rule is if the extrinsic evidence is wholly unrelated to the merits of the underlying lawsuit (e.g., a late notice defense).