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The "Eight Corners Rule": Texas Appellate Court Recognizes a "Coverage Only" Exception.

Federal courts in Texas long have been inconsistent about the existence (or lack thereof) of an exception to Texas' strict "eight corners" rule, which governs an insurer's duty to defend its insured under a commercial general liability insurance policy. *Compare Ooida Risk Retention Group, Inc. v. Williams*, 579 F.3d 469, 476 (5th Cir. 2009) (adopting a limited exception under *Northfield Ins. Co. v. Loving Home Care, Inc.*, 363 F.3d 523, 528 (5th Cir. 2004)), *with Mary Kay Holding Corp. v. Fed. Ins. Co.*, 309 F. App'x 843, 848 (5th Cir. 2009) ("While appreciating the arguments for a limited 'coverage' exception to the 'eight-corners rule,' we recognize that Texas has yet to adopt such an exception."). Yet, Texas state appellate courts have remained consistent in refusing to acknowledge any such exception. *See, e.g.*, *AccuFleet, Inc. v. Hartford Fire Ins. Co.*, 322 S.W.3d 264, 273 (Tex. App.—Houston [1st Dist.] 2009, no pet.) ("We decline to create an exception to the eight corners rule under the facts of this case and consider this extrinsic evidence to determine the existence of a duty to defend."). After all, the Supreme Court consistently has refused to adopt any exception when faced with that option. *See, e.g.*, *Pine Oak Bldrs., Inc. v. Great Am. Lloyds Ins. Co.*, 279 S.W.3d 650, 654 (Tex. 2009). Nevertheless, on May 26, 2011, the Fourteenth District Houston Court of Appeals followed the lead of some federal courts and recognized an exception to Texas' stringent "eight corners" rule. *See Weingarten Realty Mgmt. Co. v. Liberty Mut. Ins. Co.*, 2011 WL 2043027 (Tex. App.—Houston [14th Dist.] May 26, 2011, no pet. h.).

A. Background Facts

Connie Johnson was assaulted by an unknown assailant who entered a store she managed called Fashion Cents. She sued her employer (Norstan Apparel Stores) and Weingarten Realty Management Company ("Weingarten Management"), which she alleged leased the retail space occupied by the store. The actual lessor was Weingarten Realty Investors ("Weingarten Investors"). The entities were separate and distinct, and Weingarten Management merely managed the property. *Id.* at *1.

Norstan had procured a CGL policy from Liberty Mutual Insurance Company, which contained an endorsement naming "all lessors of the premises leased to [Norstan] as additional insureds under the policy." Thus, Weingarten Investors was an additional insured under the Liberty Mutual Policy. Weingarten Management had its own CGL coverage with Scottsdale Insurance Company.

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Shortly before trial, Weingarten Management demanded additional insured coverage from Liberty Mutual, but the insurer refused. Although found not liable, Weingarten Management and Scottsdale filed the instant suit against Liberty Mutual, seeking recovery of defense costs under the theory that Weingarten Management had been named as the lessor in Johnson's lawsuit. They conceded the company was not a lessor of the property, but argued that the allegation gave rise to a duty to defend under the "eight corners" rule. Disagreeing, the trial court examined extrinsic evidence and found that Weingarten Management was not entitled to a defense.

B. Majority Opinion On Appeal

Weingarten Management and Scottsdale (the "Appellants") argued six points of error, but the court only addressed the first three, overruling Appellants on each: (1) the trial court erred in looking at extrinsic evidence; (2) in looking at extrinsic evidence, the trial court erred in finding as a matter of law that Weingarten Management was not a lessor because the lease required Norstan to name the company as an additional insured; and (3) a fact issue existed as to whether Liberty Mutual was estopped from contesting that Weingarten Management was a lessor. (This piece focuses only on the first issue.)

Justice Brown explained the "eight corners" rule, acknowledging that "[t]he Supreme Court of Texas has never expressly recognized an exception" to the rule, although it has acknowledged other courts have drawn a "very narrow exception" where extrinsic evidence is "relevant to an independent and discrete coverage issue, not touching on the merits of the underlying third-party claim." *Id.* at *3 (citing *GuideOne Elite Ins. Co. v. Fielder Rd. Baptist Church*, 197 S.W.3d 305 (Tex. 2006) (acknowledging the exception, but not approving it because it was not satisfied in that case).

Justice Brown then explained that the exception at issue was first articulated in *International Service Insurance Co. v. Boll*, 392 S.W.2d 158 (Tex. Civ. App.—Houston 1965, writ ref'd n.r.e.). In *Boll*, the individual allegedly liable for an auto accident was excluded from coverage under his father's policy. Thus, the insurer did not argue the son was not liable, but that, even if he were liable, no facts existed under which his liability could be covered. So, the court allowed the insurer to introduce evidence that the excluded son was the son referred to in the underlying lawsuit. *Boll* was later acknowledged (and sometimes followed) by the Texarkana, and Corpus Christi courts of appeals. *See Cook v. Ohio Cas. Ins. Co.*, 418 S.W.2d 712 (Tex. Civ. App.—Texarkana 1967, no writ); *Gonzales v. Am. States Ins. Co. of Tex.*, 628 S.W.2d 184, 186 (Tex. App.—Corpus Christi 1982, no writ) (acknowledging but not utilizing the exception); *State Farm Fire & Cas. Co. v. Wade*, 827 S.W.2d 448, 452–53 (Tex. App.—Corpus Christi 1992, writ denied).

In *Boll*, *Cook* and *Wade*, the terms of a policy exclusion dictated that no potential for coverage existed under the facts alleged. "The merits of the underlying claim did not come into play because even if the allegations were true, a policy exclusion made coverage impossible." Here, in comparison, Liberty Mutual argued that even if the facts alleged are true, no coverage

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exists because Weingarten Management is a stranger to the insurance policy. Thus, while the circumstances were different, Justice Brown found "the ultimate position is the same—an insurer should not be required to defend when extrinsic evidence can easily establish that the policy does not provide coverage even if all of the allegations in the plaintiff's petition are true." *Weingarten*, 2011 WL 2043027 at *5.

In explaining the rationale of the "eight corners" rule, Justice Brown noted that it is to defend insureds against all claims, including meritless ones, because—to the insured—a meritless claim still requires a defense. But, that benefit exists only for an insured and "[a] a stranger to the policy neither needs nor should expect this benefit." Accordingly, enforcing the strict "eight corners" rule in the instant case does not further the underlying policy of the doctrine. "This is a 'pure coverage' question in which Liberty Mutual does not question the merits of the underlying third-party claim." *Id.* As such, the need for a very narrow exception existed, but under the exception the extrinsic evidence must apply strictly to an issue of coverage without contradicting an allegation in the third-party claimant's pleadings that is material to their underlying claims.

Justice Brown distinguished *GuideOne* on the grounds that, in that case, the insurer had a policy with the church and was obligated to defend the church against some claims. The insurer there argued that the underlying claims were meritless and could easily be disproved by showing the offending minister was not employed by the church when the policy incepted. Weingarten Management, on the other hand, was not an insured as to any claim because it was a total stranger to the policy. Thus, the instant case was more like *Blue Ridge Insurance Co. v. Hanover Insurance Co.*, 748 F. Supp. 470 (N.D. Tex. 1990), where the court allowed extrinsic evidence to show that one could not be considered an insured based on false, fraudulent or otherwise incorrect facts that might be alleged. *See Weingarten*, 2011 WL 2043027 at *7.

Justice Brown rejected Appellants' reliance on *AccuFleet*, 322 S.W.3d 264, and *Liberty Mutual Insurance Co. v. Graham*, 473 F.3d 596 (5th Cir. 2006). In *AccuFleet*, the court found that Continental Airlines could not satisfy the definition of "insured" under the facts alleged and the terms of the policy. That case only would further Appellants' position "if the court held that, based on the information available in the pleadings and policy, the insurer owed Continental a defense even though extrinsic evidence could show that (1) there was no potential for coverage even if the pleaded facts were true, or (2) Continental was actually a total stranger to the policy." *Weingarten*, 2011 WL 2043027 at *8. And, in *Graham*, the court ultimately adhered to the "eight corners" rule because coverage potentially existed under the facts alleged by the underlying plaintiff. That is, Graham was not a stranger to the policy because, at least in some circumstances (i.e., when he was not intoxicated while driving a company vehicle), he was a permissive user of his company truck. *Id.* at *9.

Justice Brown also rejected the Appellants' claim that the extrinsic evidence touched the merits of the underlying case because Weingarten Management's alleged status as a lessor was necessary to show Johnson

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was an invitee and entitled to a duty of care. Because Liberty Mutual's desire to contradict that allegation was confined to disputing Weingarten Management's status as an "insured," the court disagreed with Appellants.

Simply put, Justice Brown found that employing the strict "eight corners" rule in the instant case would not advance the policy of preventing an insurer from refusing to defend an insured simply because the plaintiff's case lacks merit. *Id.* at *10. Rather, it would impose on insurers a duty to defend anyone who—by accident or otherwise—is pleaded into coverage under a policy to which it previously was a complete stranger. "If a contract does not exist, a duty to defend should not be allowed to spring into existence based on artful or inartful pleading." *Id.*

C. Dissenting Opinion

Justice Frost issued a dissenting opinion in which she focused on the fact that the Supreme Court never has adopted an exception and, that if it ever were to adopt an exception, it would do so in limited circumstances. Thus, the Fourteenth Court was not permitted to adopt an exception outside the context specified by the Supreme Court, and the instant case falls outside that context.

In her opinion, Justice Frost emphasized the Supreme Court's recent emphasis on the importance of adhering to the "eight corners" rule. *See id.* at *12 (citing *Burlington Northern and Santa Fe Ry. Co. v. Nat'l Union Fire Ins. Co. of Pittsburgh*, 334 S.W.3d 217, 219 (Tex. 2011); *D.R. Horton–Texas Ltd. v. Markel Int'l Ins. Co.*, 300 S.W.3d 740, 744 (Tex. 2009); *Nokia, Inc.*, 268 S.W.3d at 497; *GuideOne Elite Ins. Co.*, 197 S.W.3d at 308–11; *King v. Dallas Fire Ins. Co.*, 85 S.W.3d 185, 187 (Tex. 2002). Justice Frost also noted that the Supreme Court's guiding statements in *GuideOne* are "judicial dicta binding on this court." Such language not only required that the evidence be "coverage only" evidence, but that it also be "initially impossible to discern whether coverage is potentially implicated." *Id.* at *13 (citation omitted). Simply put, Supreme Court cases clarify that the situation in which the Court may recognize an exception are narrower than recognized by the majority.

According to Justice Frost, it was not initially impossible to discern whether coverage was potentially implicated because the allegations stated that Weingarten Management was a lessor and had control over the property. Thus, "[o]n this basis, alone, the situation in the case under review does not fit within the circumstances under which the Supreme Court of Texas might consider an exception to the eight-corners rule." *Id.* at *14. Further, the extrinsic evidence contradicted the allegation in the underlying pleading that Weingarten Management was the lessor in contravention of the Supreme Court's decision in *Pine Oak*. And, finally, the company's status as a lessor went to the merits of the claim because it governed the scope of the company's duty to its lessee's employees. Accordingly, it was not "coverage only" extrinsic evidence at issue. *Id.* Justice Frost also rejected the majority's reliance on *Blue Ridge*. She noted that the Fifth Circuit in *Graham* impliedly disapproved of the *Blue Ridge* legal standard in favor of the standard adopted in *GuideOne*. *Id.* at *15.

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Commentary:

A pure "coverage only" exception to the "eight corners" rule is not a terrifying proposition by any stretch of the imagination. In fact, it could benefit insurers and insureds alike. Nevertheless, as the Supreme Court recently recognized in *Pine Oak*, contradicting the allegations of the underlying lawsuit has never been permissible. As such, while the opinion only recognizes a limited exception, it may have gone too far in permitting the extrinsic evidence to contradict allegations. This case, if appealed, will present the Supreme Court with an opportunity to clarify the standard.

GETTING TO KNOW LEE H. SHIDLOFSKY AND THE INSURANCE LAW PRACTICE GROUP . . .

Lee H. Shidlofsky is a founding partner of Shidlofsky Law Firm PLLC. His practice is devoted to representing and counseling corporate policyholders in the area of insurance law, risk management, contractual risk transfer, and extra-contractual issues. He is Chair of the Insurance Law Section and a former council member of the Construction Law Section of the State Bar of Texas. He is the author of numerous articles and seminar papers and is a frequent speaker at continuing legal education seminars in Texas and across the country. Lee has been named a "Super Lawyer" by Texas Monthly Magazine each year since 2004, including a ranking as a Top 50 attorney in the Central and West Texas Region since 2007, and is ranked as a top insurance coverage lawyer by Chambers USA and Who's Who Legal. Lee also is a Fellow of the Texas Bar Foundation.

Douglas P. Skelley is a senior associate at Shidlofsky Law Firm PLLC. He represents and counsels corporate policyholders in numerous insurance law matters. He is a member of both the Insurance Law Section and the Construction Law Section of the State Bar of Texas. Doug was named a Texas "Rising Star" by Texas Monthly Magazine in 2010 and 2011.

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