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In Determining Duty To Defend, Wisconsin Supreme Court Clarifies Four-Corners Rule

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Christopher L. Lynch
Partner

In coverage actions, policyholders (and their attorneys) frequently rely on the well-accepted principle that an insurer's duty to defend is broader than its duty to indemnify. Indeed, given the ever-escalating costs of litigation, obtaining coverage for a policyholder's defense can be just as, if not more, important than obtaining coverage for the resulting settlement or judgment. Recently, however, the Wisconsin Supreme Court issued two opinions that serve as reminders that an insurer's duty to defend, while broad, is not unlimited. The cases provide insight into how courts evaluate an insurer's duty to defend and reveal some factors policyholders should consider when confronted with an insurer that denies such coverage. ***Marks v. Houston Casualty Company*** In *Marks v. Houston Casualty Company,* No. 2013AP2756 (Wis. June 30, 2016), the court confirmed that, under Wisconsin law, a court evaluating whether an insurer has a duty to defend can consider policy exclusions as well as the policy's coverage granting provisions. The court first confirmed that in Wisconsin, as in many jurisdictions, an insurer's duty to defend is determined by applying a "four corners" analysis – *i.e.,* by determining whether the allegations contained within the four corners of the complaint would, if proven, constitute a claim potentially covered by the policy. The policyholder argued that, because the insurer had unilaterally disclaimed coverage and refused to provide a defense, the insurer should be estopped from relying on policy exclusions to support its denial of a duty to defend. The court disagreed. (Some jurisdictions refer to this as an "eight-corners" analysis because the court must look at two documents – the complaint and the insurance policy.) The *Marks* court reasoned that "a rule that an insurer who declines to provide a defense may not rely on policy exclusions to protect itself against allegations of breach of the duty to defend makes no sense." The court offered the following hypothetical: "If A demands that B perform an action under a contract, B relies on a particular clause in the contract in refusing to perform that action, and A sues B for breach of contract, a court of necessity must interpret that clause in order to determine whether B in fact breached the contract." Accordingly, the court also determined that when an insurer denies a duty to defend based on a policy exclusion, a court should consider that exclusion in applying the four-corners rule to determine whether the insurer breached its duty to defend. ***Water Well Solutions Service Group, Inc. v. Consolidated Ins. Co.*** On the same day it issued its *Marks* opinion, the Wisconsin Supreme Court also issued another opinion that addressed the four-corners rule, *Water Well Solutions Service Group, Inc. v. Consolidated Ins. Co.,* No 2014AP2484 (Wis. June 30, 2016). In *Water Well,* the court was asked to determine whether a court could consider extrinsic evidence outside the complaint in determining

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whether an insurer breached its duty to defend. Resolving some conflicting precedent among Wisconsin courts, the *Wells* court held that evidence outside the four corners of the complaint cannot be considered when determining an insurer's duty to defend. The court went so far as to state, "[w]e now unequivocally hold that there is no exception to the four-corners rule in duty to defend cases in Wisconsin." In support of its holding, the court reasoned, "[w]e have applied the four-corners rule, without exception, in duty to defend cases for so long because it generally favors Wisconsin insureds." In a corresponding footnote, the court also stated: Recognizing exceptions to the four-corners rule would require the insurer to not only draw reasonable inferences from the language of the complaint in evaluating its contractual duty to defend, but to imagine claims the plaintiff might have made. Imposing this judicially-created burden on insurers would, in practical application, rewrite the contractual duty to defend to be triggered whenever any claim is made rather than only those claims covered under the actual policy terms. However, in a separate footnote, the court also conceded: we recognize there may be isolated instances in which an insurer has no duty to defend based on the complaint's allegations, but nevertheless owes a duty to indemnify based on extrinsic evidence considered later during a coverage determination. Our decision in this case is not influenced by hypothetical possibilities. Regardless, in such situations the insured will obtain its bargained-for coverage. **Lessons for Policyholders** For policyholders outside of Wisconsin, the *Marks* and *Well Water* opinions will have little direct impact. But the cases nevertheless serve as useful reminders of some factors that all policyholders should keep in mind when confronted with an insurer that refuses to defend a claim.

- While most jurisdictions apply some variation of the four-corners rule, the scope of that analysis and the recognized exceptions to that analysis vary among jurisdictions. Unlike Wisconsin, some jurisdictions recognize that insureds can rely on extrinsic evidence outside the complaint to establish a duty to defend. In those jurisdictions, the insured is not completely at the mercy of the underlying plaintiff's complaint, and extrinsic evidence may help show that a complaint that is in-artfully or incompletely pled nevertheless asserts causes of action that are potentially within the policy's coverage. Thus, it's important to know and consider the status of the law(s) that govern(s) the policy at issue.

- Even where consideration of extrinsic evidence is not allowed, courts may be permitted, or even required, to make reasonable inferences from the facts alleged in the complaint. Those inferences must be made in favor of the insured. Thus, even where a fact is not specifically alleged in a complaint, its existence or non-existence may be established by inference.

- In many jurisdictions, including Wisconsin, if even one claim alleged in the complaint is covered, then the insurer has a duty to defend the policyholder against the entire lawsuit. In such jurisdictions, an insurer likely cannot avoid its duty to defend by showing that a policy exclusion applies to one claim, unless it can show that the exclusion applies to all claims asserted against the policyholder.

Making sure that an insurer fulfills its duty to defend can be critical to policyholders dealing with an underlying lawsuit. The recent decisions of the Wisconsin Supreme Court confirm that, when confronted with an insurer that

is refusing to defend, policyholders should consider seeking advice from experienced insurance law practitioners to help guide them through the nuances of the four-corners analysis.