

Fifth Circuit Rejects Exception to Texas's Eight-Corners Rule But Nonetheless Holds No Duty to Defend Fiduciary Liability Claim

April 2009

The United States Court of Appeals for the Fifth Circuit, interpreting a fiduciary liability policy under Texas law, has held that there was no duty to defend claims that involved the benefit plans of a non-insured entity or claims that involved non-fiduciary acts. *Mary Kay Holding Corp. v. Fed. Ins. Co.*, 2009 WL 290485 (5th Cir. Feb. 6, 2009).

The policy provided specified coverage for the insured entity, its subsidiaries and their directors, officers and certain employees, for "all Loss . . . on account of any Claim first made against the Insured during the Policy Period . . . for a Wrongful Act" The policy defined "Wrongful Act" as "any breach of the responsibilities, obligations or duties imposed upon fiduciaries of the Sponsored Plan by [the Employee Retirement Income Security Act of 1974 (ERISA) or] any negligent act, error or omission in the Administration of any Sponsored Plan"

A bankrupt company, which the insured previously had supported financially, sued the insured for alleged violations of ERISA and the Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA). The bankrupt entity asserted that officers of the policyholder, while acting as ERISA fiduciaries with respect to the bankrupt entity's employee benefit plans, misused and diverted plan assets, failed to disclose material information to participants of the benefit plans and misrepresented the plan participants' rights to continue coverage under COBRA after being terminated. The underlying complaint asserted that the policyholder vicariously was liable for these alleged breaches of fiduciary duty to the bankrupt entity's plans. The bankrupt entity further asserted that the insured directly was liable for failing to provide COBRA continuation coverage to the bankrupt entity's plan participants upon the termination of their employment. The alleged basis for this direct claim was that the policyholder was a member of a "control group" that included the bankrupt entity and that this control group relationship exposed the insured to liability.

The insurer denied coverage and, in the coverage litigation that followed, the insurer took the position that: (1) there was no coverage with respect to the alleged breaches of fiduciary duty to the bankrupt entity's plans because the entity was not a subsidiary under the policy, and (2) the direct COBRA claims against the insured

were barred because the claims involved the insured's acts as a plan sponsor, and not as a fiduciary. The court agreed.

The court first concluded that the bankrupt entity was not a "subsidiary" under the policy and, therefore, that there was no coverage for claims involving the entity's benefit plans. In reaching this conclusion, the court declined to adopt, as the district court had, a limited coverage exception to Texas's "eight-corners rule." Nevertheless, the court concluded that it was unnecessary for it to adopt this exception because the district court's findings could be affirmed based on the underlying complaint itself. In this regard, the court pointed out that the complaint failed to allege any facts from which the subsidiary status of the entity during the policy period could be determined. The court also rejected the notion that the policy provided coverage for entities that qualified as subsidiaries at points prior to the policy period, noting that the policy defined "subsidiary" in the "present-tense."

The court further held that there was no coverage under the policy for the direct COBRA claims against the policyholder, which involved the provision of access to plan benefits. The court concluded that these claims implicated the insured's role as a plan sponsor and were not fiduciary in nature. Accordingly, the alleged acts did not constitute wrongful acts as the policy defined that term. The court emphasized that, although some circuits have allowed fiduciary-based relief for failure to advise plan participants of COBRA rights, the Fifth Circuit clearly had distinguished between statutory duties, which included the COBRA notice requirements, and fiduciary duties. The court also rejected the insured's arguments that the underlying complaint asserted allegations involving "non-sponsor" duties sufficient to trigger a duty to defend. In reaching this conclusion, the court found that any non-sponsor allegations were too conclusory in nature to give rise to the duty to defend and that, in any case, any non-sponsor allegations were inapplicable to the direct COBRA claims against the insured.