DEFINING TERMS IN AN INSURANCE POLICY EXCLUSION: WHAT THE "EIGHT CORNERS" RULE DOES NOT REQUIRE

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In *Carlyle Investment Management, LLC v. Ace American Ins. Co.*,[1] the District of Columbia Superior Court held that when an insurance contract's definitions of relevant terms brings a claim within the scope of an exclusion within the policies, it does not matter whether those same terms might mean something else in the context of a different case or a different contract. The contract definitions of the terms control.

Background

The plaintiffs were three limited liability companies operating under the banner of the Carlyle Group. In 2006, the plaintiffs organized a company called Carlyle Capital Corporation ("CCC"). The primary purpose of CCC was to invest in residential mortgage-backed securities in heavily leveraged transactions financed by repurchase loan agreements. In the spring of 2008, after the market for these investments collapsed, CCC could not meet its margin calls. As a result, CCC defaulted on its repurchase agreements and eventually went into bankruptcy. A number of individual and institutional investors in CCC and the CCC liquidators in bankruptcy filed lawsuits against the plaintiffs, alleging various forms of misrepresentation and mismanagement. The plaintiffs notified the defendant insurers of these claims and asked for "defense costs" under the policies. The defendant insurers denied coverage.

The Policy Language

The plaintiffs sought a declaration that the claims against which they were required to defend in actions relating to CCC were covered losses under their insurance contracts for which the defendant insurers were liable for settlements or judgments and "defense costs." The defendants moved to dismiss, arguing that all of the claims against the plaintiffs in the CCC-related litigation fell within an exclusion of coverage in the insurance contracts. The relevant Exclusion provided:

> [T]he **Insurer** shall not be liable to make any payment for **Loss** in connection with any **Professional Services Claim** arising from **Professional Services** provided to Carlyle Capital Corp.

The dispute between the parties was over the meaning of the Exclusion. The defendants argued that the plaintiffs were stuck with the contract definitions of the terms as they applied to the Exclusion. The plaintiff countered that the Exclusion was narrower than the coverage and was intended to exclude only claims arising from professional services in the nature of those provided by lawyers and accountants ("E&O" claims), not "management-liability claims," such as those alleging acts, errors, or omissions in corporate governance (often referred to as "directors & officers claims"). The plaintiffs argued that if one analyzed the underlying complaints count by count, it was clear that some of the claims were arguably within the Exclusion while the majority of the claims were not.

Since the bolded terms were defined in the policies, the court held that those definitions control the analysis. The policies defined

> "**Loss**" as "damages, settlement, judgments…and **Defense Costs**."

> A "**Claim**" expressly includes any "**Professional Services Claim**,"

which was defined as

"a **Claim** made against any **Insured** arising out of, based upon or attributable to **Professional Services** provided by an **Insured**."

The court concluded that the allegations in the underlying complaints arose out of "professional services" as that term is defined by the policies. The court held that the terms "professional services" and "professional services claim" were not ambiguous because they were specifically defined.

"Professional services" under the policies was broadly defined. Although overly broad exclusions can be invalidated for essentially swallowing up the coverage grant, the court noted that the policies at issue posed no such risk. The policies extended coverage for claims arising out of "professional services" provided by the "insured" to any "fund, organization or portfolio entity." The Exclusion was limited to loss arising from "professional services" provide to a single entity, CCC. Since the Exclusion only applied when professional services activities related to CCC, the court found that Exclusion was narrow.

The "Eight Corners" Rule

The plaintiffs' asked the court to look at each individual count in the multiple-count complaints to see if there may be a clever interpretation of the language in any one count that could take the count outside of the language of the Exclusion. The court stated that although the plaintiffs were correct that the court was required to consider each claim in each complaint in deciding the coverage issue presented, the "eight corners rule" neither required nor permitted the court to scrutinize each count in each complaint "with a dictionary in one hand and The Chicago Manual of Style in the other" to see if there was an allegation that could be contorted so as to bear an interpretation that would take it out of the Exclusion.

The Court's Decision

Rather, the contract definitions of the terms controlled the court's analysis. The court held that the Exclusion was not ambiguous—it excluded Professional Services Claims (a defined term) arising from Professional Services (a defined term) provided to CCC. The contract defined the terms broadly enough to include virtually all of the conduct alleged against the plaintiffs in the underlying lawsuits, whether or not such conduct would be characterized as professional services or corporate management in the industry generally or in some other insurance contract. The court held that if the contract definitions of the relevant terms brought the case within the scope of the Exclusion, it did not matter whether those same terms might mean something else in the context of a different case or a different contract.

Endnote

[1] *Carlyle Investment Management, LLC v. Ace American Ins. Co., et al.,* No. 2013 CA 003190 B (D.C. Super. Ct. May 15, 2014).

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