

Texas Appellate Court Applies "Eight Corners" Rule

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A Texas appellate court has held that an insurer was not required to defend a policyholder where the factual allegations in the petition did not come within the scope of coverage of an E&O insurance policy. *Landmark Chevrolet Corp. v. Universal Underwriters Ins. Co.*, 2003 WL 22809055 (Tex. Ct. App. Nov. 26, 2003).

The insurer had issued an E&O policy to two car dealerships. The policy provided that the insurer had a duty to defend the dealerships against, among other things, alleged violations of state or federal "truth-in-lending or truth-in-leasing law[s]." Former customers sued the dealerships, alleging that the dealerships had unlawfully charged a "consumer services fee" in exchange for a "worthless" coupon book. The underlying petitions alleged fraud and violations of the Texas Deceptive Trade Practices Act. The insurer declined to defend the dealerships in the litigation on the ground that the plaintiffs had not alleged violations of truth-in-lending laws. The dealerships then brought a declaratory judgment action.

The appellate court held in favor of the insurer. The "eight corners rule," the court noted, requires the court to "compar[e] the factual allegations in the four corners of the pleadings with the language in the four corners of the insurance policy," while focusing on the origin of the damages, as opposed to the legal theories alleged, and giving "a liberal interpretation" to the allegations. Thus, the insurer's duty to defend only arises if "the factual allegations in the pleadings...when fairly and reasonably construed, state a cause of action potentially covered by the policy." The court then explained that "[e]ven giving the pleadings the required liberal construction, they do not allege facts indicating that the...plaintiffs are seeking damages for a violation of federal or state truth-in-lending or truth-in-leasing law." The court found that the plaintiffs had not alleged that the dealerships were "creditors" or that the cars were purchased on credit, as required under the Federal Truth-in-Lending Act, or that the automobiles were to be paid for in deferred installments, as required under Texas' Motor Vehicle Installment Sales Act. The court also refused to permit the consideration of extrinsic evidence, explaining that the Texas Supreme Court has "never recognized an exception to the 'eight corners rule,'" and that the Court of Appeals itself has "specifically considered, and rejected, such an exception."

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