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Virginia Federal Court Rejects Liability Insurer's "Business Pursuits" and "Known Falsity" Exclusions; Owes Defense for Slander Allegations

A federal court in Virginia recently held in *Travelers Casualty and Surety Company v. Schur*, No. 3:15CV60-HEH (E.D.Va., Nov. 24, 2015), that a liability insurer's so-called "business pursuits" and "known falsity" exclusions do not preclude a defense against defamation allegations where the allegations raised at least a potential for coverage under the policy. The decision illustrates the continued application of Virginia's "eight corners" and "potentiality" rules, which mandate a narrow application of the underlying allegations against the language of the policy and require a defense if any allegation raises even a potentiality for coverage.

Background

Schur arose from litigation over Black Water Management ("BWM"), a limited liability company formed between two individuals — Jacob Schur and Mark Sprenkle — for the promotion and management of music artists. During the course of the litigation, Shur was required to produce documents to Sprenkle, which he did at the offices of Black Iris Music, LLC ("Black Iris"), a client of Sprenkle. While producing his documents to Sprenkle, Schur made allegedly false statements about Sprenkle to Black Iris. These statements, according to Sprenkle, damaged Sprenkle's reputation.

Sprenkle brought suit against Schur alleging defamation per se. Schur tendered the suit to Travelers Property and Casualty Company ("Travelers") under two insurance policies — a homeowner's policy (the "Primary Policy") and a personal lines umbrella policy (the "Umbrella Policy"). Travelers denied coverage, contending that coverage was barred by exclusions in both policies.

The policies afford coverage for "personal injury" caused by an "occurrence" that is not otherwise excluded from coverage. The policies define "personal injury" as liability occurring from oral, written or electronic publication of material that slanders or libels another person. The policies contain what is known as a "business pursuits" exclusion. The Primary Policy excluded personal injury "[a]rising out of or in connection with a 'business' ... engaged in by an 'insured.' " "Business" was defined as "[a] trade, profession, or occupation engaged in on a full-time, part-time or occasional basis," as well as "[a]ny other activity engaged in for money or other compensation." The Umbrella Policy also excluded coverage for "personal injury" "arising out of 'business' pursuits or 'business' property of an 'insured.' " The Umbrella Policy stated that " '[b]usiness' includes trade, profession or occupation." The Primary Policy also contained an additional exclusion for personal injury "[a]rising out of oral, written or electronic publication of material, if done by or at the direction of an 'insured' with knowledge of its falsity."

Travelers brought a declaratory judgment action to confirm its coverage position under the language of the policies. The parties cross-moved for summary judgment.

The Court's Decision

The court denied summary judgment for Travelers and awarded it in favor of Schur, finding that the allegations of the underlying complaint failed to implicate either the "business pursuits" or "known falsity" exclusions. The court focused on whether the allegations as stated in the underlying complaint came within

coverage as stated under the insurance policy. This analysis, known as the "eight corners" rule, looks only to the language of the allegations and the policy to determine whether the allegations implicate coverage. Even if the allegations are not clearly within the scope of coverage under the policy, if they create even a potential for coverage — the "potentiality" rule — the insurer must provide a defense.

Travelers argued that the "business pursuits" exclusion barred coverage because Schur's alleged statements involved BWM. Schur responded that the mere formation of BWM fails to meet the definition of a "business" under the policies and that the underlying allegations fail to show that the litigation involving BWM arose from BWM's operation as a "business."

The court agreed with Schur. The court found that the only references to BWM in the underlying complaint concerned its formation by Sprenkle and Schur and that the two engaged in litigation about it. This says nothing about BWM operating as a "business." It likewise does nothing to link Shur to BWM as his "trade, profession or occupation." The court further found that even if BWM were operating as a "business," other than the litigation involving BWM, the underlying complaint alleges nothing showing that the litigation arose from or in connection with BWM as a "business." Based on these allegations, the court concluded that the allegations failed to demonstrate that the "business pursuits" exclusion plainly and unambiguously applies.

Travelers also argued coverage was barred because the underlying complaint alleged that Schur "knew that his defamatory statements were false when he made them." Schur argued, on the other hand, that alternate allegations in the underlying complaint stated that Shur made his statements "with conscious disregard for the truth and the facts available to him." The court found that because the alternate allegations provide potentiality that Schur could be found liable for defamation per se without actual knowledge of falsity, the exclusion could not apply.

Insurance Implications

Schur illustrates the significant breadth of defense coverage owed under common liability policies. The decision also underscores the importance of closely analyzing all allegations against an insured to determine whether any of the allegations state facts that could give rise to liability against the insured. This is particularly important where, as in *Schur*, the court's duty-to-defend analysis is limited to only those facts stated in the complaint and the plain language of the insurance policy. Facts known to the parties or the court, but which are not expressly stated in the complaint, cannot be considered. Thus, where the facts as alleged create even a potential for liability against the insured, the insurer must provide a complete defense against the underlying lawsuit.

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