AN OVERVIEW OF EMPLOYMENT PRACTICES LIABILITY INSURANCE AND PRACTICAL CONSIDERATIONS FROM A PLAINTIFF'S PERSPECTIVE

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Employment Practices Liability Insurance (EPLI) covers companies against claims or lawsuits filed by employees, former employees and employment candidates regarding their employment relationship with an employer. EPLI policies may cover seasonal employees, leased employees and independent contractors.[1] This type of coverage protects the company, its directors, officers, current and former employees. A company can use this type of insurance to cover expenses involved in defending against claims or lawsuits related to employment (regardless of the outcome) and EPLI provides for indemnification of the employer if the case is settled or a verdict is obtained against the employer.

EPLI insures against claims of discrimination (based on age, sex, race, religion, color and national origin), sexual harassment claims, wrongful termination (including constructive discharge and retaliatory discharge), infliction of emotional distress and breach of contract, violation of the Family Medical Leave Act or other leave laws. In addition, some policies contain a catch-all category to provide coverage for claims of discrimination based on protected categories (e.g., sexual orientation) that are not covered under federal discrimination statutes, but may be covered by state or local law.[2] For example, in a typical EPLI policy of this type, a carrier may list a number of categories of protected classes covered by its insurance and then add that it covers those "and other protected classes." Coverage for suits brought by third parties, such as customers, continues to increase in modern policies. However, some carriers restrict the coverage to sexual harassment and some to business relationships.[3]

[1] Richard S. Betterley, The Betterley Report, Employment Practices Liability Insurance Market Survey 2012: Rates Continue to Firm, But Not For All Carriers, December 2012 at 7, 10.
[2] Id at Page 4.
[3] Id. at Page 10.

EPLI policies typically exclude coverage for claims involving wage and hour laws, ERISA, WARN acts, unemployment benefits, COBRA, breach of contract and claims pursuant to the National Labor Relations Act. EPLI policies do not usually cover criminal fines, civil fines, penalties or punitive damages. They also generally exclude claims for bodily injury and property damage, because there are other types of policies which an employer can purchase which cover those claims. Liability for acts involving intentional wrongdoing is also generally excluded by many EPLI policies. However, most policies cover claims for emotional distress or mental anguish associated with covered losses.

There is currently much talk in the industry about whether and how to cover issues arising from social media and bullying in the workplace. At this point, no insurance products have been introduced to specifically insure either.

EPLI Compared To Other Insurance Policy Types

Insurers offer employers a variety of insurance options, so it is important to understand the differences between the types of coverage. Directors and Officers Insurance (D&O), Errors and Admissions Insurance (E&O) and EPLI each protect employers, and/or the managers who work for them, in different ways. D&O insurance liability policies provide insurance for negligent acts, omissions or misleading statements committed by directors and officers of a company that result in lawsuits being filed against the company. D&O coverage can be purchased to reimburse the company when it indemnifies directors or officers, to specifically cover directors or officers when the company doesn't indemnify them or provide entity coverage for claims made specifically against the company. E & O insurance coverage protects those people that give advice, make educated recommendations, design solutions or represent the needs of others. As the name suggests, it protects these people when they've done something they shouldn't have (error) or when they neglected to do something they should have (omission). It is also referred to as Professional Liability or Malpractice Insurance. EPLI covers employers against claims made by workers who have sued the company for violating their legal rights as employees. [4]

[4] Darin J. McMullen, The ABC's of Employment Practices Liability Insurance Coverage, Risk Management Magazine, 2013.

EPLI Costs and Triggering of Claims and Other Coverage Issues

EPLI costs are affected by factors such as the size of the company, the type of business, the number of employees, where the business is located, the number of claims and lawsuits previously filed and the length of time the company has been in business. Insurance companies may also take other factors into consideration when deciding the cost of the premium and structuring a policy best suited for the company. [5]

There are two different types of EPLI policies: occurrence and claims-made: An occurrence policy obligates the insurance company to pay for claims arising out of occurrences during the policy period, regardless of when the claim is reported. The policyholder is covered for any incident that occurs during the term of the policy, regardless of when the claim arising from the incident is reported to the company. In some situations the claim might be made many years after the incident occurred. This type of policy is less common than is a claims-made policy.

A claims-made policy protects an insured against claims or incidents that are reported while the policy is in force. Normally, a claims-made policy provides coverage for acts occurring prior to the claims-made policy period. Coverage for acts occurring prior to the policy period is called "prior acts coverage," and the period prior to the policy period for which claims are covered is called the prior acts period. Prior acts coverage is usually only provided when a claims-made policy has been in force immediately prior to the current claims-made policy on a basis consistent with the prior policy. Prior acts coverage is defined as "full prior acts," covering acts occurring at any time prior to the current policy period, or is defined by a "retroactive date." When a retroactive date is used, prior acts coverage is provided from the retroactive date to the current policy period.[6]

Most policies enumerate the ways in which coverage can be triggered. This may include, a demand letter, administrative complaint or a lawsuit. Oral demands are usually insufficient to trigger coverage because of uncertainty as to proof and timing, but are covered by some policies. When a claim is first presented in the form of a lawsuit, the claim is deemed to be made upon the insured's receipt of the summons or similar process. Most carriers require the named insured to

[5] Although in 2012, Aon Insurance began offering EPLI for Wage and Hour Claims, Ibid. at Page 3.

[6] Ibid.

report a claim “as soon as practicable.” However, other carriers provide a specific time period during which if a claim is not reported, they will deny coverage. [7]

A recent case on the definition of a claim under an EPLI policy caused temporary panic among insureds, until it was reversed.[8] Ten Cracker Barrel employees filed discrimination charges with the EEOC, which subsequently filed a class action lawsuit on their behalf, alleging racial and gender discrimination under Title VII.[9] The carrier denied coverage, asserting that the EEOC lawsuit was not a claim under the EPLI policy.[10] The policy defined a claim as “[A] civil, administrative or arbitration proceeding commenced by the service of a complaint or charge, which is brought by any past, present or prospective ‘employee of the insured entity’ against any insured for …[violation] of any federal, state or local law that concerns employment discrimination.”[11] The district court held that the EEOC lawsuit was not a claim under the policy because it had been brought by the EEOC, not an employee.[12] The Sixth Circuit reversed the district court and found that a civil proceeding can be commenced by a charge rather than a complaint, depending on one’s interpretation of the word “commence.”[13] Thus, the employees’ filing of an EEOC charge could be interpreted as commencing a proceeding, because it was the condition precedent necessary for the EEOC to file civil litigation against the insured.[14] The Sixth Circuit held that because the EPLI policy wording was ambiguous, and traditional contract law principles apply to insurance contracts, the policy must be construed in favor of the non-drafting party. Cracker Barrel’s interpretation of the term “claim” was ruled to govern the interpretation of the contract and the insurance company could not disclaim coverage on that basis.[15]

It is important to note that defense expenses count towards the total liability limit on an EPLI insurance policy. Lawyers on both sides of EPLI covered claims should be cognizant that defense expenses eat into the amount available to settle a case. Moreover, expenses incurred in

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[7] Richard S. Betterley, The Betterley Report, Employment Practices Liability Insurance Market Survey 2012: Rates Continue to Firm, But Not For All Carriers, December 2012 at Page 11.
[8] Cracker Barrel Old Country Store, Inc. v. Cincinnati Insurance Co. 2012 U.S. App. LEXIS 19161 (6th Cir. September 10, 2012).
[9] Id.
[10] Id.
[11] Id. at 8.
[12] Id.
[13] Id. at 9.
[14] Id.
[15] Id. at 9-14.

defending a claim under an EPLI policy are usually subject to a self-insured retention (or deductible). Most policies provide that defense expenses are part of the retention, so that they will not have to defend against minimal or nuisance claims.

After the retention is exhausted, EPLI covers damages resulting from an insured's employment practices, including settlements, judgments, back pay and front pay awards, pre-judgment and post-judgment interest, attorneys' fees and costs, and as previously stated, defense expenses. EPLI polices typically exclude coverage for wages, salaries, benefits or expenses of the insured; punitive damages (unless coverage is permitted by applicable state law); fines, penalties, or taxes; amounts due under an express employment contract; stock options and deferred compensation; and injunctive relief (e.g., reinstatement, providing ADA accommodations).

Coverage for either Punitive Damages or Intentional Acts can be prohibited by states, either by regulation or on a theory that such coverage is contrary to public policy. Currently, there are approximately sixteen states that prohibit or restrict coverage for either Punitive Damages and/or Intentional Acts, including New York, Ohio, Florida, and California. Almost every carrier offers separate coverage to fill in such potential gaps in coverage, either via most favorable venue wording, or with an off-shore wraparound in a jurisdiction such as Bermuda that does not frown upon such coverage. [16]

Selection of Counsel

Carriers prefer to exercise control over counsel, believing that unqualified legal representation cannot be allowed, and that control over fees is necessary, particularly in EPLI insurance coverage. In fact, some insurance carriers have expressed a reluctance to enter the smaller employer market because they believe that such employers often use improper counsel, and take employment actions without legal advice. [17]

However, although most carriers continue to control the selection of counsel, the trend is for the carrier to be flexible in allowing the insured to select or approve counsel. If the insured requests specific counsel approval at the right time (during proposal negotiations), the carrier is often willing to approve the insured's choice. Some carriers offer the insured a choice of an indemnity policy, which allows the insured full control over selection of counsel. Carriers that

[16] The Betterley Report at 9.
[17] Id. at 12-13.

are primarily interested in larger employers are more likely to give selection of counsel to the insured; carriers that specialize in smaller insureds are less likely to be able to invest the time necessary to approve special counsel requests, since they are charging correspondingly less premium. The modern trend, even by small carriers, is to allow the use of the insured's choice of counsel, as long as they are clearly qualified. [18]

Consent to Settle

Many EPLI policies require that the insured consent to settle any claim. This consent, pursuant to most policies, must not be "unreasonably withheld." Sometimes the insured and the insurer disagree over whether a matter should be settled. An insurer often wishes to settle the matter when it can do so for less than the expected defense costs, or an amount that the insurer views as reasonable, when considering the potential damages that could be awarded and the uncertainty over litigating the claim. The insured often takes a different tact, that it does not want to set a precedent for settlement, which it views as possibly opening the floodgates for employees to attempt litigation against the company. In other cases, insureds, regardless of the validity of the plaintiff's claim, believe the claim is meritless and possibly frivolous and do not want to settle, based on principle.[19]

In cases where the insured and insurer disagree over settlement, "Hammer clauses" often govern the situation. A "Hammer Clause" in an EPLI policy allows a carrier to limit its claim payment to no more than the amount it could have settled for, plus defense costs. This protects the carrier against a "litigate at any cost" insured, while protecting the employer against a "settle it, who cares about the precedent" carrier.[20]

An alternative to the traditional "Hammer Clause," the "soft" hammer clauses allows the carrier and the insured to share the cost incurred beyond the claim. Most carriers will not force an insured to settle, but are free from any additional cost (settlement or defense) obligations. A few policies continue to allow the carrier to settle without the insured's consent. In practice, if the insured has a good reason to continue the defense, carriers will not enforce their hammer clause.[21]

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[18] Id. at 12.
[19] Marshall D. Bilder and Robert McGuire, Consent to Settle, New Jersey Lawyer Magazine, page 17-18 (August 2012).
[20] Id. at 13.
[21] Id.

There are consequences if an attorney appointed as counsel by an insurance company settles a claim at the direction of the insurance company without the consent of the insured. In a New Jersey case, the Court concluded that the attorney could be liable for malpractice, having violated his primary duty to the insured, his client.[22] The Court explained that "In this setting . . . insurance defense counsel routinely and necessarily represent two clients: the insurer and the insured."[23] The Court reasoned that "the intrusion of the insurance contract does not alter the fact that the relationship with the insured is that of attorney and client."[24] "It cannot be overemphasized that the relationship is the same as if the attorney were hired and paid directly by the insured."[25]

EPLI Coverage: Practical Considerations From A Plaintiff's Perspective

Plaintiffs' attorneys will want to maximize the possibility that EPLI will provide coverage for a proffered settlement. This should be considered from the onset of litigation, as it is important to draft a plaintiff's complaint in order to ensure coverage. EPLI must also be considered when determining strategy, with an eye toward both settlement negotiation strategy and litigation.

EPLI coverage varies from policy to policy, making it very important for plaintiffs to know the extent, length, and limitations of coverage before litigation begins. The plaintiff's attorney will generally want the defendant to be covered as broadly as possible for settlement purposes, and since it is difficult to obtain a defendant's policy before litigation commences, the plaintiff will want to determine which claims generally are covered by EPLI insurance issued within the jurisdiction in which the plaintiff is filing suit. In the alternative, and/or in addition, plaintiff's counsel can always simply ask defendant's counsel whether the employer is covered – often times the answer will be provided, although generally not the details of the policy.

Plaintiff's counsel should carefully draft the complaint so that a claim or claim(s) that is covered by EPLI is included therein. This is easy enough advice to follow if a plaintiff has a strong claim which will invariably be covered by insurance, but becomes a more complex analysis if the covered claim is weak. In any jurisdiction where plaintiffs want to litigate in state court, it also becomes more complicated if the covered claim will throw the matter into federal

[22] Lieberman v. Employers Insurance of Wasau, 171 N.J. Super. 39 (1979), *aff'd as modified*, 84 N.J. 325 (1980).
[23] Id. at 244.
[24] Id. at 245.
[25] Id. at 353.

court, while foregoing the claim would keep it in state court. In any situation where plaintiff's counsel is making such decisions, the client should be kept fully informed and understand the reasons for the decision.

As part of the complaint, it is important to include a clause requesting any insurance policies which might provide coverage under any of the plead claims, which would require a defendant to produce any EPLI policy which would apply. Until the plaintiff's attorney reviews the specific EPLI policy of the defendant, he or she may not be able to understand which of his or her claims are covered by the policy. In addition, the amount of coverage, such as the coverage limit, can vary wildly from policy to policy, making it vastly important for both defense and plaintiff's counsel to know the limits before discussing a settlement that may not be entirely covered by the policy.

There are still other issues that plaintiffs' lawyers and their clients should consider during litigation. Assuming that a plaintiff's claims are covered by the insurance carrier and not subject to an exception or exclusion somewhere in the policy, a plaintiff must decide his or her strategy. One such strategy is to burn up the defendant's deductible as quickly as possible, because after the defendant runs through his or her own money, the plaintiff will then have access to a larger pot of money from the carrier. Another strategy is to limit expenses (by trying to limit motion practice, etc.), since as defense costs are part of the total policy limits, a plaintiff would rather see that amount allocated toward settlement than litigation expenses.

Allocation of resources under EPLI policies have been the subject of litigation.[26] In a sexual harassment case, the claims of seven female employees settled at an amount of money exceeding the one million dollar limit in the policy. Not only was the settlement in excess of the one million dollars, but most of the insurance money was used by insurance-appointed counsel, so that only about one-fifth of the settlement was covered by the insurer. The insured sued the insurer for breach of contract, common law bad faith, and unfair trade practices, since the lawyers appointed by the insurer had refused to settle early on in the case and had in the insured's view, wasted money throughout the proceedings, leaving the company holding on to the proverbial bag of over one million dollars in costs and other liability related to the settlement. Although normally courts side with insurance companies in these sorts of suits, CMC was able to withstand summary judgment on all of its claims, because it was able to present triable issues of

[26] Cornett Management Company, LLC v. Lexington Insurance Co., 2007 U.S. Dist. LEXIS 58284 (N.D.W.Va.).

fact that the insurance company and its appointed lawyers mishandled the case from the beginning, made errors in the investigation and attempted settlement of the case, and misrepresented aspects of the policy. However, this is a rare victory for the insured in support of coverage, as opposed to insurance companies' efforts to avoid liability.