



Understanding Employment Practices Liability Insurance

Due to the myriad of labor and employment laws that govern the employer-employee relationship, virtually all businesses face the prospect of being sued by their employees at some point. For many companies, an employee's lawsuit, if successful, could be catastrophic since compensatory and punitive damages, together with attorney fees and costs, can amount to hundreds of thousands of dollars, if not more. In order to minimize this potential risk, insurance companies created Employment Practices Liability Insurance (EPLI). Consequently, understanding EPLI coverage is critical for every business in today's litigious society.

Unfortunately, many business owners, risk managers and human resource managers do not fully understand EPLI and why having it is so important in today's business climate. In particular, many businesses are unaware of the following issues involving EPLI coverage:

1. Who is covered?
2. What types of claims are covered?
3. What is the coverage amount?
4. What are the conditions with which the employer has to comply to receive coverage?
5. Who will defend the lawsuit?

Each of these topics will be discussed.

1. Who Is Covered?

In general, EPLI coverage insures employers, its employees, directors and officers (otherwise known as the "insured"). In limited instances, coverage may be extended to a spouse of an insured for claims made against jointly held property.

2. What Types of Claims Are Covered?

Typically, EPLI coverage insures employers against discrimination, harassment, wrongful termination and employment tort claims that are not covered by other types of business insurance such as comprehensive general liability insurance, directors and officers liability insurance, professional

liability insurance and/or workers' compensation. More specifically, EPLI can be obtained to insure an employer against any actual or alleged wrongful act of an employee, including in most cases, but not limited to:

- (a) Wrongful dismissal, discharge or termination (actual or constructive), including breach of an implied contract;
- (b) Harassment (including quid pro quo, hostile work environment or other sexual harassment);
- (c) Discrimination based on age, gender, race, color, national origin, religion, sexual orientation or preference, pregnancy or disability;
- (d) Retaliation;
- (e) Employment-related misrepresentation(s);
- (f) Wrongful failure to employ or promote;
- (g) Employment-related libel, slander or defamation;
- (h) Wrongful deprivation of a career opportunity, demotion or discipline;
- (i) Negligent hiring, retention, training or supervision;
- (j) Infliction of emotional distress or mental anguish;
- (k) Failure to provide or enforce adequate or consistent policies; and
- (l) Violation of an individual's civil rights.

Moreover, some EPLI policies will cover claims brought by third parties, such as independent contractors or an employer's customers. However, claims made under the Americans with Disabilities Act, Family and Medical Leave Act, federal or state wage and hour laws, benefit laws or Occupational Safety and Health Act are sometimes not covered. As such, in reviewing a potential policy, it is imperative for the employer to determine the specific types of acts that would be covered by the insurance policy to ensure the insurance carrier (the insurer) has a "duty to defend" against a particular claim. Where a policy does not cover all of the types of claims an employer

wants to insure itself against, it can often negotiate for and obtain a rider at an additional expense to expand the basic coverage provided by the insurer.

3. What Is the Coverage Amount?

The coverage amount set forth in an EPLI policy is usually expressed as a policy limit. The policy limit establishes the maximum amount that the insurer will pay for a claim after the retention has been met. The term “retention” is another name for a deductible. As such, an EPLI policy may provide that it will pay up to \$1,000,000 per claim after the \$25,000 retention has been met. This means the insured will be responsible for the first \$25,000 of attorneys’ fees and expenses in defending/settling the claim and that the insurer will be responsible for the remaining attorneys’ fees, expenses and settlement amounts associated with the claim up to a maximum of \$1,000,000. EPLI policy premiums are directly affected by the retention amount (the lower the retention, the higher the premium). An employer that is selecting a retention amount should consider why it is obtaining the EPLI policy as well as how much it can afford to pay in the event it is sued. In particular, the employer should determine whether it is obtaining the policy to reduce the effects of a catastrophic claim or is it merely trying to shift all liability for employment claims to the insurance carrier. Where the employer is seeking to avoid the former, it may be willing to obtain a higher retention amount and pay a lower premium, whereas if it is seeking to accomplish the latter it may want a nominal retention amount at a higher premium cost.

Finally, EPLI policies often provide that the coverage amount is affected by an insured’s willingness to settle a claim based upon the insurance carrier’s advice. For instance, insurers will often provide a “carrot” or “stick” incentive to obtain an insured’s cooperation in settling a claim. For example, in some instances a policy may provide that an insured’s retention will be reduced retroactively by a specific percentage (i.e., 10%) if it agrees to settle a claim based on the insurer’s advice. In contrast, other policies may provide that the coverage amount will be capped or the employer will have to split the cost of the litigation with the insurer going forward if an employer unreasonably refuses to settle a claim against the carrier’s advice. This is commonly known as the “hammer clause” in a policy.

4. What Conditions Does the Employer Have To Comply With To Receive Coverage?

In order to receive EPLI coverage, employers often have to demonstrate that they have employment policies and procedures that are compliant with all current federal and state laws and regulations. In fact, insurance carriers often will not issue coverage unless these policies and procedures are memorialized in the form of an employee handbook or other

written document and the employer demonstrates that it has distributed the handbook and/or written policies to its employees. Insurance carriers also will require employers to demonstrate that they have provided employment training to their employees and corrected or resolved any previous employment problems it had prior to seeking coverage. Where an employer demonstrates that it has taken these steps, the insurance carrier will be more likely to insure the employer and even may offer the employer discounts on its premiums.

Once a claim has been made against an insured, the insured will have to provide timely notice of the claim to the insurer in order to receive coverage under the policy. As such, employers must carefully review their policies to ensure they understand what is defined as a “claim” under the policy. For example, some policies provide that a “pre-lawsuit” or “demand” letter is a claim that triggers the notice requirements under the policy. Others define a claim as any agency charge (e.g., EEOC charge of discrimination). Where an insured fails to provide timely notice as required by the policy, most insurers will either refuse to provide coverage to or defend the employer under the policy or refuse to apply to the policy retention any attorneys’ fees or costs incurred by the employer in defending the claim prior to the late notice of the claim to the insurer. As such, it is incumbent for employers that have obtained EPLI coverage to understand what constitutes a claim under the policy and then to notify all of its managers that if they receive a “demand” letter or other legal papers, etc., the manager should forward them immediately to the company representative responsible for providing timely notice to the insurance carrier. This step is important to prevent an unintentional waiver of coverage rights and to decrease the likelihood of having a coverage dispute with the insurance carrier.

5. Who Will Defend the Employer Against the Lawsuit?

Lastly, many EPLI policies state that an employer will be defended against a claim by one of the law firms either listed on the insurer’s pre-approved panel of attorneys or, if no panel exists, by a law firm chosen by the insurer. Although it is most common that the attorneys assigned to defend an employer are hand-picked by the insurance carriers, employers can generally negotiate for their own attorneys to be approved as defense counsel for the employer’s claim under the policy and, in some instances, to have their attorneys added to the insurance carrier’s panel of approved counsel. This may be an especially important issue for an employer where it has a law firm that is particularly familiar with its business and the history of its relationship with its employees. Hence, employers should not overlook this issue when choosing EPLI insurance.

In conclusion, EPLI coverage can be a valuable tool in managing a business' risk when sued by one of its employees. However, before obtaining an EPLI policy, an employer must completely understand the terms of the policy in order to ensure it receives the appropriate plan for its particular business needs. As such, it is important for a company to have a good insurance broker to assist it in selecting the appropriate EPLI policy for its particular business. Moreover, once an employer decides to purchase EPLI coverage, it

should review its employment policies and procedures and handbooks to ensure they are in compliance with all current federal and state laws and regulations. In the event a company's owner, human resources manager or risk manager has questions regarding an EPLI policy or needs assistance in reviewing and revising its employment policies and procedures, it should seek guidance from counsel. The attorneys at Fox Rothschild LLP have substantial experience in such matters.



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