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Insurance Coverage for Wage and Hour Class Action Litigation: Rethinking the Common Wisdom

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INTRODUCTION

While a great deal of commentary exists regarding the impact of the Great Recession on many types of litigation, only recently has the surge in wage and hour class action litigation come into focus. In fact, numerous recent articles have documented the proliferation of high-stakes wage and hour class action litigation.[1]

In addition to the recession, the increase in such lawsuits is primarily driven by: (1) technological advancements allowing work from remote locations; (2) the continued potential for large recoveries and attorneys' fees[2]; (3) a relatively easy class certification process as compared to discrimination cases; and (4) divergent state and federal labor laws that permit plaintiffs to pursue claims on a variety of theories.[3]

While the best strategy to avoid a devastating wage and hour class action is to carefully review your employment practices with a qualified attorney, an often overlooked component of a company's protection from the financial consequences of such a claim is its insurance policies. To ensure

[1] *See, e.g.*, Paul Davidson, *Overworked and Underpaid*, USA TODAY, April 16, 2012 (documenting the recent rise in wage and hour litigation); *Wage-And-Hour Litigation Outpacing All Other Workplace Class Actions*, BUSINESS INSURANCE, April 2, 2012 (discussing that wage and hour litigation outpaced all other types of workplace class actions in recent years); Shannon Green, *Wage and Hour Litigation is Big – and Getting Bigger*, N.J. LAW JOURNAL, Mar. 19, 2012 (noting that the number of Fair Labor Standards Act cases filed in federal court between 2010 and 2011 increased more than 15 percent; there has been more than a 325 percent increase in wage and hour lawsuits filed over approximately the past ten years; and wage and hour lawsuits now exceed the number of all discrimination actions combined in the United States).

[2] Class action settlements in the wage and hour context include: Farmers Insurance Group -- $210 million, State Farm Insurance Companies -- $135 million, Novartis Pharmaceuticals Corporation -- $99 million, Smith Barney -- $98 million, International Business Machines Corporation -- $65 million, Staples Incorporated -- $42 million, Oracle Corporation -- $35 million, Rite Aid Corporation -- $25 million, Starbucks Coffee Company -- $18 million, Taco Bell Corporation -- $13 million, and Radio Shack Corporation-- $8.8 million.

[3] *See, e.g.*, Paul Davidson, *Overworked and Underpaid*, USA TODAY, April 16, 2012 (discussing impact of proliferation of mobile devices).

the best protection, any employer should consider carefully, with the help of a professional if necessary, review of the specifics of its insurance policies and how they are likely to respond in the event of such claims.

COVERAGE ANALYSIS

Most employers routinely purchase Employment Practices Liability ("EPL") insurance policies or, particularly with private companies, Directors and Officers Liability ("D&O") insurance policies that include EPL coverages. Although both of these types of policies typically contain broad definitions of "loss," and the companies that purchase them likely expect coverage for wage and hour claims, insurance carriers both historically and presently assert that the policies do not provide coverage for defense costs or any judgments or settlements incurred in connection with these claims.

Insurers typically rely on two principal arguments. First, insurers assert that the underlying claims do not constitute "loss," or seek only uninsurable restitution. Second, insurers typically contend that coverage is barred by the Fair Labor Standards Act ("FLSA") exclusion, which bars coverage for "alleged violations of the Fair Labor Standards Act . . . or any similar federal, state or local statute."

Companies, however, should not accept these insurer contentions without a careful evaluation of the specifics.

First, as with all insurance coverage issues, the specific language of the policy matters. As stated above, insuring agreements of EPL policies are typically broad in scope and plaintiff lawyers usually assert multiple claims and broad allegations. If even a single such claim or theory is within the scope of coverage, the employer may be entitled to partial or complete coverage of the lawsuit.

Moreover, several judicial decisions in recent years have cast doubt on insurers' efforts to apply their principal arguments on a wholesale basis. For example, in *SWH Corp.*[4] the California Court of Appeals denied the insurers' summary judgment on the issue of whether the amounts sought in a wage and hour case were "restitution," or not "loss" under the policy. The court determined that SWH had suffered a covered "loss" as defined by the policy and that whether SWH's "loss" constituted restitution that is uninsurable under California law is an issue of fact. *Id*. at *10-13. In reaching this conclusion, the court acknowledged that "[t]he line between damages and restitution is often fine or invisible . . . . [The narrow type of uninsurable relief is only] restitution of property or money obtained by criminal, willful, or fraudulent conduct, and/or restitution that is punitive in nature." *Id*. at *11-12.

The SWH court also found that the underlying allegations of wage and hour violations that were the basis of SWH's claim of "loss" did not come within the policy's FLSA exclusion because the FLSA exclusion was ambiguous and, therefore, should be construed in favor of the insured. *Id*. at *12-14.

[4] *SWH Corp. v. Select Ins. Co.*, 2006 WL 2786930 (Cal. Ct. App. Oct. 19, 2006).

More recently, in *California Dairies, Inc. v. RSUI Indemnity Co.*, 617 F. Supp. 2d 1023 (E.D. Cal. 2009), the court found that the policy's FLSA exclusion applied to some, but not all, of the allegations against the company. Specifically, the court found that the FLSA exclusion did not apply to the following claims: (1) failure to reimburse employees for costs related to uniforms; (2) failure to comply with itemized wage statement requirements; and (3) failure to pay wages due at termination. *Id*. at 1044-47.[5]

Finally, it is important for employers to be aware that the insurer's duty to defend it under the policy is broader than its duty to indemnify the company. As such, even if it is determined that an insurer is not ultimately obligated to indemnify its insured for an underlying wage and hour claim settlement or judgment, the insurer may still be obligated to cover defense costs. Given the substantial defense costs associated with class action wage and hour litigation, coverage for defense costs is often a significant recovery and is certainly better than no coverage.

PROACTIVE MEASURES

Regardless of whether a company has been named in a wage and hour lawsuit, there are several steps that all risk management and legal departments can take to put their companies in the best possible position to avoid such claims and potentially secure insurance coverage if and when the need arises.

First, evaluate corporate policies and operations that may impact wage and hour issues in an attempt to prevent claims in the first place. For example, some companies have instituted policies requiring certain employees to leave firm-issued wireless devises at the office so that these employees are unable to work from remote locations when they are not on the clock.

Second, collect, organize, and safeguard all of the company's policies. This process should include an effort to identify, and obtain, if possible, policies issued to other pertinent companies, such as predecessors and current or former affiliates of your company.

Third, consider involving outside coverage counsel to audit the organization's current insurance portfolio to confirm that the company has the most complete and cost-effective coverage available to it for these types of claims.

Fourth, if the company becomes aware of facts or circumstances that may give rise to a wage and hour claim, or is served with a wage and hour lawsuit, the company should give notice promptly to all of its liability insurers, absent any relatively rare, case-specific circumstances that may justify refraining from giving such notice. Because certain actions that the company takes at the outset of litigation and throughout its defense may bear on the ultimate likelihood of recovering insurance proceeds, it may benefit the employer to involve coverage counsel from the outset.

[5] The court found the following claims to be "similar" and subject to the FSLA exclusion: (1) unpaid minimum wage; (2) unpaid overtime wages; and (3) failure to provide meal and rest periods or pay an additional hour of wages.

Finally, in the event that an insurer does deny the company's claim, do not take those denials at face value and seek an independent review of the carrier's position.

CONCLUSION

The coverage provided by insurance policies for wage and hour class action lawsuits can be an extremely valuable corporate asset, even if such policies only provide coverage for defense costs associated with such claims. Companies can maximize the benefits of these assets by acting proactively now, and by being willing to question coverage denials from their insurers.