Bloomberg BNA

Daily Labor Report®

Given Proliferating Wage & Hour Claims, Specialized Insurance an Important Consideration for Employers

WAGE & HOUR

Given a dramatic increase in both the number of wage and hour lawsuits and the average cost to employers to resolve one—$4.5 million—a little prevention could be worth at least a pound of cure in this area, Kami Quinn and Jason Rubinstein say in this BNA Insights article. They note that filings of collective wage and hour claims in federal court have more than tripled since 2000.

While the first line of defense is for businesses to review their employment practices, an employer must also consider how its current insurance portfolio would respond to such a claim and whether that likely response can be improved in a cost-effective manner, the attorneys say. The coverage provided by insurance policies for wage and hour class actions can be an extremely valuable corporate asset—even when they provide coverage only for the associated defense costs, Quinn and Rubinstein say.

BY KAMI QUINN AND JASON RUBINSTEIN

Wage and hour lawsuits—claims in which employees and companies dispute the amount owed to an employee or class of employees for work performed—have surged a dramatic 432 percent over the past two decades. J. Berman, *Wage-And-Hour Lawsuits Jumped 432 Percent In The Last 20 Years*, HUFFINGTON POST (May 14, 2013).

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Wage and hour suits generally encompass three categories of claims: (1) hourly employees asserting that they were not compensated for all hours worked; (2) salaried employees claiming they are owed overtime wages; and (3) employees who work for the tipped minimum wage who claim they did not earn enough tips to bring their total compensation to the minimum wage. B. Covert, *Wage And Hour Lawsuits Against Employers Rise For The Fifth Year In A Row*, THINKPROGRESS (May 13, 2013). Notably, these suits are not limited to a particular industry or type of business; any business with employees must consider the possibility that it will be the target of a wage and hour claim in a comprehensive assessment of its business risks.

Indeed, noting that federal court filings of collective wage and hour actions have increased more than 300 percent since 2000, Seyfarth Shaw LLP has called these actions ''the greatest employment threat to American business.'' *See*, *Multi-plaintiff Wage and Hour Lawsuits Pose the Greatest Employment Litigation Threat to*

 ISSN 0418-2693

American Businesses Today (available at http://www.seyfarth.com/Wage-Hour-Litigation).

In addition to the increasing numbers of claims, the cost for employers of defending and settling these claims is significant. According to a report by NERA Economic Consulting, the average cost to resolve a case in 2013 was approximately $4.5 million, but one case in 2013 was resolved for as high as $35 million. D. Martin, S. Plancich and J. McIntosh, *Trends in Wage and Hour Settlements: 2013 Update* (available at http://www.nera.com/67_8329.htm).

California and New York remained the most active jurisdictions for wage and hour lawsuits, comprising 48.5 percent and 17.2 percent of overall settlement dollars, respectively.

Commentators have attributed the surge in wage and hour claims to several factors, including (1) the great recession, which some believe has put pressure on companies to achieve greater productivity with smaller workforces, thus leading to longer hours for current employees; (2) technological advancements allowing work from remote locations unbounded by time of day; (3) the continued potential for large recoveries and attorneys' fees; (4) a relatively easy class certification process as compared to discrimination cases; (5) divergent state and federal labor laws that permit plaintiffs to pursue claims on a variety of theories; and (6) increased awareness of wage and hour issues by employees because of ''social media.'' *See, e.g.*, P. Davidson, *Overworked and Underpaid?* USA TODAY (Apr. 16, 2012) (discussing impact of proliferation of mobile devices).

The first line of defense to avoid a costly wage and hour class action is for companies to review their employment practices carefully with a qualified attorney. But to fully protect the business from the financial consequences of potential wage and hour claims, an employer must also consider how its current insurance portfolio will respond to such a claim and whether that likely response can be improved in a cost-effective manner.

Coverage Analysis

Although coverage for wage and hour claims can exist under a variety of insurance policy types, it is most often found in Employment Practices Liability (EPL) insurance coverage. Employers routinely purchase EPL insurance either separately, or particularly in the case of private companies, in conjunction with their Directors and Officers (D&O) policies.

EPL coverage provisions typically contain broad definitions of ''loss,'' and the companies that purchase them usually expect coverage for wage and hour claims. Nevertheless insurance carriers regularly deny coverage for these claims citing one or more of: (1) an exclusion or public policy prohibiting recovery for the costs of restitution or (2) FLSA exclusions that typically bar coverage for ''alleged violations of the Fair Labor Standards Act . . . or any similar federal, state or local statute.''

EPL coverage provisions typically contain broad definitions of ''loss,'' and the companies that purchase them usually expect coverage for wage and hour claims.

When these denials are closely examined, however, it often becomes apparent that some or all of the claim at issue does not fall squarely and unambiguously within the scope of these exclusions and thus, the policyholder is entitled to some coverage. Several policyholders that have not taken no for an answer in these cases have found their position vindicated in court in decisions that have cast significant doubt on insurers' efforts to apply their two principal arguments on a wholesale basis.

For example, in *SWH Corp. v. Select Insurance Co.*, No. G036145, 2006 BL 165200 (Cal. Ct. App. Oct. 19, 2006) (unpublished), the court denied the insurers' request for summary judgment on the issue of whether the amounts sought in a wage and hour case were ''restitution,'' or not ''loss,'' under the policy. In reaching this conclusion, the court acknowledged that ''[t]he line between damages and restitution is often fine or invisible . . . . [The only 'restitution' relief that is not insurable is] restitution of property or money obtained by criminal, willful, or fraudulent conduct, and/or restitution that is punitive in nature.''

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.

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.

Accordingly, it is critical for policyholders to examine their coverage and the claims against them closely before accepting a denial of coverage. First, as with all insurance coverage issues, the specific language of the policy matters. Some definitions of ''loss'' are broader than others, and some FLSA exclusions are narrower than others.

Second, the allegations of the particular wage and hour claims are important. Plaintiff lawyers usually assert multiple claims and allege various theories of liability. For example, plaintiffs may pursue common law wage and hour claims as Rule 23 class actions along with FLSA claims in the same lawsuit. If even a single such claim or theory is within the scope of coverage, the employer may be entitled to at least partial coverage for the lawsuit.

Third, an insurance company's duty to pay for its insured's defense is broader than its duty to cover judgments or settlements. So even if it is ultimately deter-

  DLR ISSN 0418-2693

mined that an insurer is not obligated to cover an underlying wage and hour settlement or judgment, the insurer may still be obligated to cover defense costs in the interim. This ''litigation insurance'' can be extremely valuable because wage and hour suits often are pursued as class actions, and the costs of defending such actions can be quite substantial.

Fourth, other types of insurance policies, beyond EPL and D&O policies, may provide at least partial coverage for wage and hour claims. This fact is exemplified by the Fourth Circuit's recent decision in *Republic Franklin Insurance Co. v. Albemarle County School Board*, 670 F.3d 563 (4th Cir. 2012). *Albemarle* addressed whether a ''Commercial Package Insurance Policy'' provided coverage for an underlying wage and hour class action brought against a school board by bus drivers and transportation assistants who worked for the board. The underlying plaintiffs demanded, among other things, unpaid wages and overtime pay, liquidated damages as authorized by the FLSA, and attorneys' fees.

The Fourth Circuit first held that the alleged failure to comply with the FLSA qualified as a ''wrongful act'' under the policy. The court also held that, although any ultimate judgment awarding back wages and overtime pay would not be a covered ''loss'' under the policy because the obligation to pay any such amounts was a pre-existing duty, any obligation to pay either liquidated damages under the FLSA or attorneys' fees would constitute a covered ''loss'' from a ''wrongful act'' within the meaning of the policy.

In reaching this latter holding, the Fourth Circuit expressly rejected the insurer's argument that liquidated damages under the FLSA are ''restitutionary in nature'' and thus not ''damages''—an argument that, as noted, insurers often raise in the context of EPL policies. In addition to noting that such an argument was contrary to U.S. Supreme Court precedent holding that liquidated damages under the FLSA are compensatory damages, the Fourth Circuit noted that if it accepted that argument, it ''would be excluding almost all tort awards from the definition of 'damages' [in commercial insurance policies].''

Significantly, *Albemarle* did not involve a typical EPL policy or a typical D&O policy with an EPL component. Rather, the case involved a ''Commercial Package Insurance Policy'' that included, among other things, a ''School District and Educators Legal Liability Coverage Form.'' Although these other types of insurance policies, in contrast to EPL coverage provisions, may not expressly identify employment-related claims as the type of underlying claims encompassed by the policies, the policies may be a very valuable source of protection if a company satisfies the insuring agreements of the policies, as in *Albemarle*.

Such policies may be a significant source of protection because, as in *Albemarle*, these other policies sometimes do not contain a FLSA exclusion. Thus, employers should analyze their complete roster of insurance policies, including their errors and omissions (E&O) policies, when faced with a wage and hour claim, to ensure that all potentially responsive policies are identified and timely noticed and that rights thereunder are properly preserved.

Emerging Market of Specialty Policies

Employers that find their existing EPL or other coverage does not provide them with the protection from wage and hour claims that they desire should be aware that some insurers do offer specialty policies designed to cover wage and hour claims, particularly for large employers. Apparently recognizing the uncertainty of coverage for wage and hour claims under EPL and D&O policies, Marsh has released the Marsh Wage and Hour Preferred Solution. Marsh asserts that this product is designed for companies with more than 4,000 employees and provides coverage for actual or alleged violation of the FLSA or similar state laws. Similarly, Aon Risk Solutions also now offers wage and hour coverage intended for large employers.

However, in considering such policies, it is important to note that marketing claims by insurers that there is never wage and hour coverage under EPL policies have been shown to be false.

Thus, although employers should consider whether such specialty coverage makes sense for their business, they should still preserve and, when necessary, exercise their right to pursue coverage under their EPL policies, which typically have higher limits. The specialty policies can also differ materially from each other, so a careful review of any proposed policy language is warranted. Finally, because the specialty products are not ''standard form,'' the policy language should be negotiated to ensure appropriate coverage is obtained.

Practice Tips

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 now to put their companies in the best possible position to avoid such claims and potentially secure insurance coverage if and when the need arises.

■ In an attempt to prevent claims in the first place, evaluate corporate policies and operations that may have an impact on wage and hour issues.

■ Collect organize, and safeguard all of the company's policies.

■ Consider involving outside 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. Consider whether specialty coverage for wage and hour claims is appropriate for the company. If specialty coverage is pursued, ensure that the language of the policy is negotiated to provide appropriate scope of coverage.

■ 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 counsel from the outset. It is important to insure that all rel-

evant policies are identified, insurance claims are submitted to carriers appropriately, and that coverage is pursued in a strategic manner.

■ In the event 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 provide coverage only for defense costs associated with such claims. Companies can maximize the benefits of their insurance assets by being proactive, and by being willing to question, and challenge where appropriate, coverage denials from their insurers.

  DLR ISSN 0418-2693