SECREST WARDLE

A Small Business Needs Employment Practices Liability Insurance

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A SMALL BUSINESS NEEDS EMPLOYMENT PRACTICES LIABILITY INSURANCE

I. WHAT IS EPL INSURANCE?

Employment Practices Liability (EPL) Insurance provides insurance coverage to pay sums a company may be obligated to pay because of wrongful acts or omissions or personal injury due to the employment relationship between the insured company and an employee, former employee, or applicant for employment.

A. Covered Parties

New EPL policies protect individuals as well as the company.

B. Litigants

Individuals most likely to assert an employment claim against your company are:

(1) Former employees, especially those who were fired;
(2) Current employees, especially disgruntled employees who did not get a raise or promotion they believed was deserved; and
(3) Employees who claim harassment, discrimination or mistreatment.
(4) The EEOC is always a potential litigant since it can investigate and give employees a "right to sue" letter.

C. Common Claims

Claims commonly covered under an EPL policy include:

(1) Wrongful termination;
(2) Sexual harassment;
(3) Hostile work environment;
(4) Discrimination based on race, color, creed, national origin, marital status, medical condition, physical appearance, age, mental impairment, pregnancy, sexual orientation or preference;
(5) Retaliation;
(6) Wrongful failure to hire or promote;
(7) Wrongful discipline;
(8) Negligent evaluations; and
(9) Violation of an employee's civil rights.

D. Statutes

The federal and state statutes under which an employee can sue your firm are dizzying and include:

1. Federal Statutes

Title VII of the Civil Rights Act of 1964
Age Discrimination & Employment Act
Americans with Disabilities Act
Family & Medical Leave Act
Electronic Communications Privacy Act
Omnibus Control & Safe Streets Act
Fair Labor Standards Act
False Claims Act

2. Michigan Statutes

Eliot Larsen Civil Rights Act
Michigan Persons with Disabilities Civil Rights Act
Michigan Bullard-Plawecki Employee Right to Know Act
Michigan Minimum Wage Law
Michigan Polygraph Protection Act
Michigan Wage & Fringe Benefits Act
Michigan Whistleblower's Protection Act

This presentation will focus narrowly on wrongful employment practices in relation to EPL insurance. It will not discuss labor management issues that may arise in the context of collective bargaining agreements and laws related to those agreements.

II. EVOLUTION OF EPL INSURANCE

Historically, employment law was essentially contract law that enforced a personal agreement between the employer and employee. In contrast, modern employment law is essentially tort law which compensates an employee for injury sustained as a result of the employer's wrongful acts or omissions and in certain circumstances permits punitive damages to punish an employer for its wrongful acts. Today, employment law reflects society's belief that all employees should have an equal chance to compete in the workplace based on their ability to perform the required work. Through employment discrimination laws, the legislature and the courts have decreed that employers shall not act wrongfully toward employees who fall within certain protected classes.

Most employment law is based on either vicarious liability or strict liability. Consequently, the employer may be liable for the acts and omissions of its managers and other employees, even if the employer itself had no specific intent to discriminate.

Following the enactment of the Civil Rights Act 1964, employment practice liability insurance developed as a byproduct of commercial general liability (CGL) and directors and officers (D&O) insurance. CGL and D&O insurance policies generally exclude most employment lawsuits. Insurers initially designed EPL insurance to be a gap filler that would specifically cover employment claims.

EPL insurance dates from the early 1980's when NAS Insurance Services, through Lloyd's of London, introduced an employer's legal expense reimbursement policy. In the early 1990's, carriers began introducing their own EPL insurance products in increasing numbers.

Coverage was limited and in short supply, however, until 1991. That year, the EPL market received a "kick start" due to several events that focused the nation's attention on the liabilities associated with employment practices. First, the Civil Rights Act of 1991 was enacted. This Act contained two provisions that drastically changed the employment practices' environment. The first allowed plaintiffs to recover punitive damages, thereby raising the potential stakes for employee-plaintiffs and their attorneys. The second permitted jury trials for these cases, displacing more conservative federal judges who commentators have long argued favored employers in the Title VII cases. In a jury trial, employers' actions are judged by a panel of individuals in the mainstream workforce. Most of the members of the jury are themselves employees who may have had a bad work-related experience. The introduction of juries into the decision-making process produced a marked difference in the outcome of these cases.

The Clarence Thomas confirmation hearing was another event in 1991 that focused the nation's attention on employment practices. For the first time in our nation's history, "sexual harassment" was being discussed in our Congress, places of business, coffee shops and in our homes. The allegations made by Anita Hill both shocked our conscience and stimulated our discussion of the appropriateness of this type of conduct in the workplace. Shortly after these hearings, the nation was again forced to confront the reality of sexual harassment when news of the Navy's "Tail hook" scandal was released. After the media attention generated by these two events, sexual harassment has never left the front pages of America's newspapers.

With sexual harassment employment practices continually in the newspapers and on television, the number of these claims rose steadily. The first insurance markets to be hit with these types of employment-related claims were the general liability (GL) carriers. Claims were submitted under the theory that this type of harm was somewhat "bodily" in nature, and therefore, mental anguish and emotional distress, for example, should be covered under the GL policy. In fact, a general liability policy may provide a defense against employment claims if the claims pled

involve negligence as well as intentional misconduct. Indemnity will be excluded, however, for all intentional act claims. Other GL provisions typically exclude coverage for emotional distress, as well as non-monetary workplace remedies. The GL markets quickly realized that they were paying claims that they originally had no intention of covering. Consequently, they began using "employment-related claims exclusions" in their policy forms. Some GL carriers were quicker to respond than others, but this position is fairly standard in the GL arena today.

With exposure growing, some professional liability carriers began endorsing their directors and officers (D&O) and errors & omissions (E&O) policies to cover non-entity employment practices liability coverage. This endorsement provided coverage for named insureds in their individual capacity for employment claims. The inadequacies of this coverage soon became apparent. First, employment liability claims tended to be brought not against individuals but against the corporation itself. Without entity coverage, EPL insurance is virtually worthless. Second, protecting only the named insured was very limiting because the individual offender being sued tended not to be a director or officer of the company. While later EPL endorsements expanded the named insured for purposes of an employment liability suit to include all employees of the organization, the lack of entity coverage defeated the likelihood of any realistic protection from these claims.

Even when it was possible to secure limited protection against employment claims under GL or D&O and E&O traditional policies, obtaining coverage generally involved a coverage fight with the insurance carrier. If the carrier provided a defense, it would typically be provided under a reservation of rights, reserving all of its policy defenses. Resolution of the coverage issues would typically be resolved in a declaratory action in which the insured and the insurance company requested a court to declare the rights of each of the parties under the insurance policy. The declaratory action was generally litigated at the same time the insured company was defending the employment claims in the underlying action. A defense under a reservation of rights often provided the defendant with little peace of mind. Until the declaratory action was resolved, the company was uncertain whether the carrier would continue to pay the defense costs and whether the carrier would pay any final settlement or judgment. As a consequence, the company often had to contribute to a settlement of the case.

Today, employment practice liability insurance has become one of the hottest selling and most talked about insurance products in the market. With the insurance industry experiencing an undisputed "soft market" condition, premiums from EPL insurance represents a much-needed growing source of revenue for insurance companies.

A. Three Types of EPL Policies

Three basic types of policies have developed since the inception of EPL insurance.

1. Defense Costs Only Policy

EPL insurance, as originally offered in 1987, offered coverage for defense costs in a limited number of employment practices situations but did not afford coverage for "indemnity" exposures (i.e., any amount paid in settlement or in satisfaction of a judgment). The policy was further limited by a type of "sunset" provision, which extinguished coverage after four years if the limits were not already exhausted by defense costs resulting from claims submitted under the policy. Although this policy form is reportedly still available, it is obviously of limited value.

2. Wrongful Termination Coverage: Defense and Indemnity

In 1991, the first EPL policy offering both defense and indemnity coverage was introduced. The form was limited to wrongful termination claims only, including both constructive and retaliatory discharge. Although the product generated considerably more interest than the earlier defense costs only product, the events of the time led to the development of a more advanced EPL coverage.

3. Triple Perils Coverage: Wrongful Termination, Discrimination or Harassment

In the aftermath of the Clarence Thomas hearings and passage of the 1991 Act, insurance was introduced that has evolved into the EPL form known today. Currently, EPL insurance provides coverage for three named perils of wrongful termination, discrimination and sexual harassment, which constitute the vast majority of employment practice claims. With reference to the latter two, the policies do not require an actual employment termination event. Thus, under most forms, a claim brought by an individual who alleges he or she was demoted for discriminatory reasons or forced to work in a hostile work environment would be covered.

III. THE PURCHASE OF EPL INSURANCE IS ON THE RISE

It is unlikely that your present standard insurance policy, such as a general commercial liability policy, will cover the cost of settlements and judgments for employment discrimination suits and claims.

There has been a substantial increase in employers purchasing employment practices liability insurance. To avoid the impact of significant defense costs and of large damage awards, many companies have begun to look to their insurance carriers for relief from the growing waive of lawsuits. In this regard, employers have been purchasing employment practices liability insurance policies that are designed specifically to cover claims related to employment practices.

In 1999, according to the 2000 RIMS benchmark survey, produced by Risk and Insurance Management Society, Inc. and Ernst and Young, LLP, most companies surveyed purchased EPL coverage. That is up from only 29% of respondents in 1998. And although the smaller companies – most out of the range of such studies – are not as likely to purchase the coverage, they are beginning to see the light.

Why all the EPL converts? After a decade of believing "it can't happen to me," risk managers have realized the EPL numbers are adding up.

IV. THE IMPORTANCE OF EPL INSURANCE AS THE COMPANY'S SAFETY NET IN AN EVER-CHANGING LEGAL ENVIRONMENT

Small and large employers in Michigan are subject to an ever-changing and complex body of state and federal employment laws and regulations. Employers must be sure that all key employment decisions, such as hiring, promotion, transfer, demotion, discipline, termination and layoffs do not impose financial obligations on the company to pay large attorney fees or damages to satisfy employee claims, settlements or judgments. There are two basic solutions to the problems: Prevention and Insurance.

Prevention makes good business sense and will help you defend an employment claim, but insurance is the safety net that will catch you when all else fails.

A. The Prevention Strategy

As an employer, you should adopt a preventative strategy to reduce your employment liability exposure. In developing a strategy that best suits your company's needs, you should consider:

1. Employment Audit

A review of your company's employment policies should be performed periodically to ensure compliance with current state and federal laws and regulations. A complete review of the company's (1) employment recruiting advertisements, (2) employment application, (3) investigative

practices, (4) interview practices, (5) personnel handbook, (6) employment contracts, (7) employment policies and procedures, and (8) termination practices can economically identify areas that need correction and thereby dramatically reduce your liability exposure.

Problem: While necessary and beneficial, a legal audit of your company's employment practices will be costly. Additionally, even the best-qualified lawyer is not equipped to predict changes in the law and the retroactive application of those changes. Once an employment practice law is enacted, it is subject to interpretation by the courts. Hungry plaintiff lawyers are always attempting to devise arguments which will serve to expand the application of the laws.

You sell automobile insurance to some customers based upon the argument that their safety record as a driver is no protection against the other drivers on the road. The same analysis applies to an employment audit: the best audit today is no protection against the change in the law tomorrow.

2. <u>Release and Covenant Not to Sue</u>

Whenever a departing employee is given any compensation or benefits to which he or she was not previously entitled, a Release and Covenant Not to Sue should be signed by the employee. The Release should be prepared by counsel or, if prepared by the company, reviewed by legal counsel to ensure it complies with current employment laws. For example, the Older Workers Benefit Protection Act contains a number of technical requirements which must be included in the Release to avoid an age discrimination claim. A properly prepared Release and Covenant Not to Sue can eliminate future liability exposure and prevent future lawsuits.

Problem: Even if you obtain an employee's signature on a Release and Covenant Not to Sue, the attorney drafting that document cannot anticipate the ever-developing case law that is continually broadening the meaning of employer fault. Today's Release may not protect you from tomorrow's claim.

3. <u>Education and Training</u>

Human resource employees responsible for hiring, firing and managing the company's employment policies should receive regular education and training to ensure they are knowledgeable about the current changes in

the laws and are informed about the best methods of preventing future employment claims. Training should focus on the particular issues and problems unique to your business. It should also include receipt of employment newsletters and periodicals and attendance at seminars and formal courses.

Problem: Materials quickly become out-of-date and must be constantly updated to comply with changing legal requirements. It is difficult to schedule training and seminar attendance while you are operating a demanding business. Additionally, education and training are only as effective as the person who is educated and trained. The person you designate to become trained may not have the time, interest or ability to put into practice the training he or she receives. In theory, all things are possible. In practice, all business people know that it is impossible to fit into each day everything that needs to be done that day.

4. Out-Placement

If you are faced with terminating or laying off long-term employees, hiring an out-placement company to assist your employees to find new jobs may greatly reduce your employment liability exposure at a moderate cost. Since an employee who finds a new job is less likely to file a lawsuit, out-placement may reduce your liability exposure. In addition, by facilitating your employee's transfers to new jobs, you are being fair, which improves morale among the remaining employees.

Problem: For a smaller company, out-placement may prove to be cost prohibitive. Additionally, the fact that a terminated employee finds a new job does not constitute a bar to his or her claim against you for discriminatory practices. Additionally, even if your employee is a leased employee, you usually remain liable for employment-related claims under the doctrine of "Dual Employer."

5. Arbitration

A binding arbitration provision in an employment agreement may provide a faster and less expensive alternative to traditional jury trials. A special panel of the Michigan Court of Appeals has held that pre-dispute agreements requiring mandatory arbitration of statutory claims are enforceable if certain requirements are met. Legal counsel should be consulted about the terms of the arbitration provision before the employment agreement is signed by the employee.

Problem: Your ability to compel arbitration depends upon an enforceable arbitration agreement. Specific statutes require that certain provisions are included in an employment agreement in order for an employee to be compelled to waive his or her right to a trial in the state or federal courts.

If your arbitration clause is not enforceable, your exposure for attorney fees and the potential recovery by your former employee has just risen dramatically. Even if your arbitration clause is enforceable, the defense costs associated with defending a client in arbitration can readily approach the defense costs generated by defending a client in the state or federal courts. Also, depending upon the facts of the claim, an arbitration award can equal or exceed the jury verdict award for the same claim.

B. EPL Insurance – Your Safety Net

As an employer, you may feel as though you are walking an employment high wire. If prevention fails, insurance is the safety net that catches you as you fall. Insurance will protect you from the claims all of your effort could not prevent and from the claims which have become viable since your preventative measures were undertaken. Employment law has made employers more and more liable for acts that are less and less within their direct control. Insurance solves the problem by shifting the risk of the employer's liability to the EPL carrier.

Insurance covering employment claims is currently available to protect your company from monetary damages due to discrimination or a violation of state or federal employment laws. Your insurance policies should be reviewed annually to determine if you have the appropriate coverage with the appropriate policy limits to cover your potential exposure.

1. Example

My law firm has 70 + attorneys; a human resources director; written employment policies and an employee handbook; a PEO providing employment and human resources services; and a practice group of attorneys who specialize in employment law. I have written a book titled "*Michigan Employers Guide: Hiring, Managing and Terminating Employees*." But, we also have a multi-million dollar EPL policy.

Why? Because we know that despite all of our knowledge in this area, despite our training and education and policies and procedures, despite a human resources manager and a PEO—you can never prevent a lawsuit from being filed. It may be a meritless lawsuit but it will still cost my firm time and money to analyze, defend and have it dismissed. Even under the best case scenario, employment practices litigation is time-consuming and costly.

V. WHY A SMALL BUSINESS SHOULD PURCHASE EPL INSURANCE

A. Questions For A Small Business

As insurance agents, you are no doubt aware of the risk/benefit analysis which applies to the purchase of every insurance policy. With respect to EPL coverage, there is a tendency among employers with fewer than ten employees to discount the need for such insurance because of the belief that there would be no basis for an employment practices claim against such a small employer. Before you jump to that conclusion, ask yourselves the following questions:

1. How many full-time/part-time employees do I have?

2. What are my turnover and termination statistics for the previous five years?

3. What are the details of my management and ownership history?

4. Have I had any mergers, acquisitions, or downsizing in the previous five years?

5. Do I have a full or part-time human resources person?

6. Do I have a written employee handbook or human resources policy manual?

7. Has an attorney reviewed my policies or my handbooks?

8. What does my employment application look like?

9. Do I have an employment "at will" statement?

10. Are job applicants required to sign and verify that all representations are true and that there are no material omissions?

11. Do I have a formal employee orientation program?

12. Do I require that applicants or employees submit to drug tests?

13. Do I have written policies regarding discrimination, harassment, progressive discipline, termination, etc.?

If you cannot affirmatively answer every question I just asked you, chances are there is the hidden potential for litigation lurking somewhere in your office. Even if you can answer every question I just asked, you need to know that the changing and ever-broadening nature of employment law makes it impossible for even the most astute attorney to give you advice that is guaranteed to keep you out of litigation. The law changes and it sometimes changes retroactively. The policies and procedures you implement today may not insulate you from a claim next week.

B. No Employer is Immune From Suit

No employer is immune from employment claims, regardless of company size, industry, or workplace demographics. Surveys by the Society of Human Resources Management report that a majority of employers have been sued by employees. Another source reported in 1995 that 90% of Fortune 500 companies had faced sexual harassment claims. According to the LRP Jury Verdict Research database, 41% of claims are against small employers (15 to 100 employees).

As insurance agents, you know that the number of lawsuits is on the rise. Just as the best driver on the road cannot stop someone else from running into him, the best employer in the workplace cannot prevent a lawsuit from being filed against his or her business.

C. Why Small Businesses Need EPL Insurance

1. Expanded Array of Employment Claims

EEOC statistics reveal that sexual harassment claims have doubled between 1991 and 1997, and retaliation claims rose steadily and now make up 24% of EEOC claims. The EEOC received almost 20,000 documented claims during fiscal year 1999 – a 77% increase over the number of claims filed in 1992. Approximately 37% of documented claims involved racial grounds; 31% gender; 9% national origin; and 23% a mixture of religion, age, disability and other factors.

The expanded array of workplace claims falls into three general categories: statutory, tort and contract-based.

A) **Statutory**: A variety of comprehensive federal and Michigan anti-discrimination statutes protect Michigan employees against discrimination in the workplace. These statutes are considered comprehensive because they encompass all aspects of employment, including discrimination in hiring, training, demotion, transfer, promotion, discipline, compensation and discharge.

1. **Federal** –

   Title VII of the Civil Rights Act of 1964

   Americans with Disabilities Act

   Age Discrimination & Employment Act

   Family & Medical Leave Act

   Fair Labor Standards Act

   Electronic Communications Privacy Act

   Omnibus Control & Safe Streets Act

   Federal Privacy Protection Act

   False Claims Act

2. **Michigan** –

   Eliot Larsen Civil Rights Act

   Michigan Persons with Disabilities Civil Rights Act *(formerly the Michigan Handicapper's Civil Rights Act)*

   Wage & Fringe Benefits Act

   Bullard-Plawecki Employee Right to Know Act

   Whistleblower's Protection Act

   Polygraph Protection Act

B) **Tort**: Tort theories of liability include:

1. Wrongful discharge.
2. Retaliation.
3. Privacy claims.
4. Intentional and negligent infliction of emotional distress.
5. Interference with contractual and business relationships.

C) **Contract**: Contract claims include breach of express and implied covenants and rights under:

1. Written agreements.
2. Employee handbooks.

D) **<u>Damages</u>**: The Civil Rights Act of 1991 and state and federal statutes enacted during the past decade have greatly expanded the range of remedies available to the plaintiff employee.

Under this expanded framework of claims and remedies, employers may be held directly or vicariously liable for claims brought by employees as a result of negligent or intentional acts.

2. <u>There Has Been An Explosion of Employment Claims</u>

Over the last several years, there has been what is commonly described as an "explosion" in disputes concerning all aspects of the employment relationship. Lawsuits against employers are on the rise. In 1998, employees brought more than 24,000 federal employment discrimination suits against private employers. Employees won 35.5% of the cases that went to trial. The median damage award was $137,500, but in 14.2% of the cases, Plaintiffs were awarded $1,000,000 or more and in 10.6% of the cases, awards exceeded the $10,000,000 mark.

Countless other cases were settled for undisclosed amounts. The types of cases that are filed tend to be affected by news coverage, especially sexual harassment cases; there has been a 2,200% increase in such suits in just the past ten years.

More than half of the HR professionals responding to a *1999 Employment Practices Liability Survey* said their organizations had been named as a Defendant in at least one employment related lawsuit. 91% of those responding said former employees did the suing. A survey conducted by the *Society for Human Resource Management* and the law firm of Jackson Lewis reports:

- 37% of employers were sued by current employees
- 8% were sued by unsuccessful job candidates
- 5% were sued by prospective employees

In a 1992 study by Betterly Risk Consultants, Inc. it was determined that the number of work related claims against corporations was increasing at the rate of 5,000 per year. In many cases, the increase in lawsuits has resulted from changes in state and federal law concerning the rights of employees and job applicants to be free from discriminatory and otherwise hostile work places.

EPL claims will likely continue to be on the rise far into the 21st Century. The medioric rise in the number of employment-related claims is one of the hottest issues facing corporate management today.

In this environment, managers of every kind of organization, from the small, private, not-for-profit corporations to the Fortune 500 corporations should be concerned about protecting their organizations from the cost of settling such suits or paying the verdicts.

3. <u>The Size of Settlements and Verdicts Are Increasing</u>

In 1992 the average employment practices award was $458,997 with the mid-point award being $96,500. A more recent study indicated the average award is now $536,000. If defense costs are added, the amount would be in the $1,000,000 range. Recent cases against Shoney's, Inc., Lucky Stores, Inc. and State Farm Group have resulted in verdicts and settlements, including punitive damages of more than $100,000,000.

Before you discount the significance of these statistics by concluding that such a large award could never happen to you, consider that defense costs alone can be staggering, if not fatal to a small company.

Arguably, it is a smaller employer which has the greater need for EPL coverage. That is because even the filing of a claim of discrimination with a state or federal agency can cost your company a significant amount of money based upon both man hours and defense fees. The premiums you pay for an EPL policy, even after five years, will constitute a small percentage of the total cost of even an unsuccessful employment discrimination claim.

Bad publicity as well as damages from jury trials are dangers you must consider when deciding whether to purchase EPL insurance.

4. <u>The Cost of Employment Claims Is Increasing At An Alarming Rate</u>

Presently, an effective defense to employment claims is costly, disruptive and time-consuming, even if the claim is meritless. Most employment

cases are fact intensive and combine statutory, tort and contract theories, which make them typically difficult to resolve through a summary judgment motion. The cost of defending the claim often constitutes the primary cost associated with employment claims. Defense costs frequently dwarf both total settlements and judgments. Faced with ongoing costs and disruption of business operations, many employers are forced to pay meritless claims just to stop the bleeding. An EPL policy that provides a defense requires the carrier to select an attorney who specializes in the defense of employment claims and pay the attorney fees necessary to defend the claim.

Even though most cases settle, the cost of defending a case can be substantial for even a major corporation. For the small to medium-sized company, defense costs can prove staggering. Sometimes the attorney fees can run into the hundred of thousands of dollars.

It is wise to remember that in February of 1996, umbrella insurance policies sold by State Farm Insurance and Pacific Indemnity paid $900,000 into President Clinton's legal defense fund to cover his costs in defending a sexual harassment action filed against him by Paula Jones.

The following is a quote from a December 1994 Morefar Marketing, Inc. memo concerning the cost involved in defending work-related discrimination claims:

"The rule of thumb was that the value of a Title VII case before the 1991 amendments (to the 1964 Civil Rights Act) was $2,000 – $5,000 for a quick settlement. Now it is more than $20,000. It can cost employers between $5,000 and $20,000 just to defend themselves through the charge filing stage where claims are brought before the EEOC or Michigan Civil Rights Department. That's before a formal lawsuit is filed. To retain a good defense lawyer, it will generally cost about $5,000 just to have a file opened. In all out litigation, defense costs range anywhere from $20,000 to $200,000, depending upon the length and complexity of the case."

5. <u>An Employer Is Not Protected From the Requirements of the Employer Liability Statutes by its Small Size</u>

Federal employment statutes typically require that a company have a minimum number of employees before it is subject to the requirements of the Act. For example, the federal employment statues require the following number of employees:

Title VII of the Civil Rights Act of 1964 – 15 or more employees

Federal Americans with Disabilities Act – 15 or more employees

Federal Age Discrimination Act – 20 or more employees

Federal Family & Medical Leave Act – 50 or more employees

Michigan's employment statutes also require a minimum number of employees for the Act to be applicable to a particular employer. However, Michigan's requirements are far less stringent than the federal requirements. In several cases, only one employee is necessary for the Act to regulate the actions of the employer. Michigan's statutes require the following number of employees:

Michigan Elliot-Larsen Civil Rights Act – 1 or more employees

Michigan Persons with Disabilities Civil Rights Act – 1 or more employees

Michigan Minimum Wage Law – 2 or more employees

Michigan Bullard-Plawecki Employee Right to Know Act – 4 or more employees

Rather than protecting the company, its small size not only fails to exempt it from the requirements of the statutes, but makes it extremely difficult for the company to be fully versed in the ever-changing requirements of the statutes. A small company may be far more likely to be unaware of developments that could impose liability on the company. Consequently, it would be far wiser to rely on EPL insurance to protect the company than relying upon its small size to exempt it from the requirements of the federal and state statutes.

6. <u>Adverse Jury Attitudes</u>

National research conducted by Dan Gallipeau, Ph.D. (New York Employment Law & Practice, May 29, 2001) revealed that 72% of jurors polled believed that sexual harassment is a common occurrence in the workplace. When voting in favor of a plaintiff, jurors were actually motivated to find "against the employer" giving great latitude to issues of notice to the employer and imposing high standards upon them to be proactive, as opposed to reactive, in response to employee complaints.

Jurors usually believed that any discipline they received from their own employers was unjustified and they tended to apply the same rationalization to the plaintiff. Seventy-six percent of jurors felt it was common practice for an employer to retaliate against a complaining employee.

Although Gallipeau's article discusses only sexual harassment, one would expect the same employee mentality in juror response to apply to other employment practices claims, including age, race, sex, and disability discrimination, constructive termination, wrongful demotion, failure to hire, failure to promote and invasion of privacy.

7. <u>Economic Downturn</u>

A reduction in the work force often generates discrimination claims, particularly age discrimination claims, but also claims for other protected classifications that may appear to be disproportionately impacted by the employer's decisions and actions regarding downsizing. In his article, "Juror's Views of Sexual Harassment 2001," Ph.D. Gallipeau cautions that employees have become more aware of their rights and the power they can wield at a time when jurors are holding employers to higher standards of training and investigation. When employees enjoy a sense of security and value of work, employers see few claims. But when the company suffers, profits decline, supervisors become irritable, and well-informed employees view themselves as expendable, the bonds of corporate loyalty are broken and employment claims abound.

8. <u>The Legislature or the Courts Create New Protected Classes</u>

Under federal law, including Title VII of the Civil Rights Act of 1964, individuals cannot be held liable for harassment. But now, in California state court, this has changed. The legislature enacted A.B. 1856 that says employees can be held liable when they harass co-workers. Similarly, the federal Age Discrimination Employment Act protects individuals over the age of 40 from age discrimination. New Jersey's legislature, however, passed a statute that permits individuals under the age of 40 to bring claims of age discrimination against current or prospective employers. (N.J. Stat. Ann. §§10:5-4, 10:5-12)

Unless a small businessman monitors the legislative enactments or the most recent court rulings, he cannot be sure that conduct that was legal today will be legal tomorrow. The legislature can create new classes of

protected individuals through legislative enactments, or the courts can interpret existing laws to broaden those classifications. In either case, the employer may be operating under the erroneous belief that the law has not changed. In such a situation, only an EPL insurance policy will protect the employer.

9. Courts May Make Retroactive Decisions

Under various circumstances, both federal and state appellate courts may render decisions that have retroactive effect. Recently, the Michigan Court of Appeals in *Zanni v Medaphis Physician Services Corp*, 240 Mich App 472 (2000) held that the section of the Civil Rights Act precluding discrimination on the basis of age protects workers who are discriminated against on the basis of their youth, abrogating *Zoppi*, 206 Mich App 172. The court further held that the decision was neither unexpected nor indefensible, and would thus be given full retroactive effect.

In the *Zanni* situation, a small business may have relied on the rule of law established by *Zoppi*, and made its decisions on the basis that a youthful employee could not bring an age discrimination claim. In applying *Zanni* retroactively, the court, after the fact, made the small businessman's employment decisions concerning youthful employees wrongful.

A small business, just like any other business, cannot protect itself from decisions giving retroactive effect other than by purchasing an EPL insurance policy.

10. An Employer Cannot Be Sure Its Employment-Related Decision Will Be Vindicated in Court, No Matter How Reasonable It Appears

The uncertainty of litigation, especially litigation involving a jury trial, can cause an employer to make poor employment decisions for fear that a jury might misinterpret them. Conversely, an employer who makes the right decisions still worries that a jury of six strangers could interpret the facts differently.

In *Reed v Lepage Bakeries Inc*, 102 F2d 33 (D.Me. 2000), Manuella Reed suffered from a bipolar disorder. Upon reporting to work on light duty following a workers' compensation leave, Ms. Reed met with human resources representatives and her supervisor behind closed doors to discuss work restrictions. Ms. Reed was not interested in reviewing her

work restrictions as required by company policy. Instead, she was rather insistent on discussing changing her work schedule. Ms. Reed was told that they were not there to talk about her schedule. She "lost it" and went into a "blind rage" that included shouting "F--- You" at the human resources representative.

Q. If she worked in your organization, would she be terminated? If she was, would the termination violate the Americans with Disabilities Act?

Ms. Reed was terminated following this incident for workplace misconduct. She then sued under the Americans with Disabilities Act. Although Ms. Reed admitted that her conduct was inappropriate, she claimed that her termination was discriminatory because her misconduct was allegedly caused by her disability. This case presents in a nutshell the dilemma presented to many small companies that employ persons with disabilities. The disability may cause the employee to engage in misconduct ranging from violence to unprofessional conduct to absenteeism, which normally would be cause for discipline, often including termination were the misconduct engaged in by a person without a disability. The disabled employee, however, will often argue that because the misconduct was caused by the disability, adverse employment action taken because of the misconduct actually constitutes action taken against the employee "because of" the employee's disability, thereby constituting a violation of the Americans with Disabilities Act.

Here, the court ultimately ruled against Ms. Reed, holding she could not walk away from supervisors simply because they caused her stress. The important point, however, is that the employer was forced to make a difficult decision in a situation where it may not have been certain of all the facts or the current status of the law. That uncertainty, in many cases, results in an employer not taking the appropriate action because they fear a lawsuit, the corresponding legal costs, and the possibility of an adverse verdict. Although EPL insurance does not alter the outcome, it does afford an employer the confidence to make a reasonable decision without fear that the cost of litigation or an adverse judgment would put it in bankruptcy.

11. <u>Current Standard Policies of Insurance Do Not Protect the Employer</u>

Although traditional policies of insurance may afford protection under limited circumstances for employment claims, in general, they do not afford protection for the vast majority of employment practices claims.

D&O – The wrongful act definition in many D&O policies is broad enough to cover many employment claims but many policies, nonetheless, provide only limited protection because they do not insure the company as a separate entity. Although officers and directors require protection, most employment claims are directed against the employer or the employee's supervisor.

In addition, D&O policies do not cover officers and directors for intentional misconduct outside the scope of their responsibilities.

GL – GL policies sometimes provide a limited defense and/or indemnification coverage against employment claims that include negligent conduct or that assert vicarious and direct liability. But the chances of obtaining a complete defense and indemnification coverage without a costly coverage dispute are remote because of the standard limitations and exclusions in GL policies.

Obstacles to coverage include provisions that (1) insure employees only for acts within the scope of employment, (2) exclude coverage for intended acts or injuries, (3) define "bodily injury" as not including emotional distress, and (4) define "property damage" as not including economic losses. In addition, many GL policies now exclude injuries arising out of or in the course of employment.

Workers' Compensation – Workers' compensation policies do not offer reliable protection against most employment claims because they are specifically directed toward benefits under workman's compensation statutes, not civil suits seeking damages.

Homeowners' Policies – Homeowners' policies often have the same obstacles to employment claims as GL policies, including limitations from the definitions of "occurrence," "bodily injury," and "property damage." Exclusions for "intentional acts" and "business pursuits" assure that carriers will deny coverage for employment claims.

12. An Employer Cannot Rely on a Short-Time Employee's Loyalty

An employer cannot rely upon an employee's loyalty to ensure the employee will not file an employment claim. This is especially true for short-term employees who have no real relationship with your company, but may be in a position to recover large sums of money in an employment action.

On September 1, 1994, twelve jurors in northern California fired a shot heard, if not around the world at least around the country. On that day, the jury awarded over $7.1 million in punitive damages to a legal secretary, Rena Weeks, for claims of sexual harassment against the law firm of Baker McKenzie and one of its partners. Days earlier, the same jury awarded Ms. Weeks $50,000 in compensatory damages for the same conduct. It is noteworthy that the plaintiff had only worked for Baker McKenzie for approximately 70 days. Even more striking is the fact that she only worked for the harassing partner for 25 days. (Even though the trial judge later cut the verdict in half, plaintiff's attorneys were elated and defense attorneys were not surprised by the jury's willingness to award such astronomical damages.)

At first, Baker McKenzie's case appeared to be an anomaly. Over the next three years, however, the headline cases included Bill Clinton, Texaco, Mitsubishi, Miller Brewing, and most recently, Smith Barney's multi-million dollar settlement with 25 female former and current brokers.

13. Efforts to Avoid Claims through Training May Not Work

In *Burlington Industries Inc v Ellerth*, 118 S Ct 2257 and *Faragher v City of Boca Raton*, 118 S Ct 2275, the Supreme Court offered employers an affirmative defense to sexual harassment claims if the employer used "reasonable care" to prevent harassment through training and also showed that the employer acted promptly to correct any reported harassment. Statistics reviewed a year after the Supreme Court's ruling revealed that the number of sexual harassment claims had not significantly dropped. The training was often found to be inadequate because it was too legalistic for managers and workers to appreciate fully. Other experts felt that some companies simply had not been taking the training seriously, thinking that the mere hiring of legal consultants would help shield them from liability.

In the aftermath of *Faragher* and *Ellerth*, it was generally believed that companies could defend harassment claims by adopting tough policies and aggressively enforcing them. However, the Supreme Court's guidelines also provided plaintiffs' lawyers many chances to prevail in court. A speaker at the Law & Society Association's annual meeting on May 28, 1999, argued that there is growing anecdotal evidence that some discrimination training can polarize employees. "Training may reinforce stereotypes and inspire animosity between employees who are encouraged to share their real feelings." While an employer cannot simply abandon training for fear that it could be construed by the EEOC and the courts as a

sign of "bad faith," the employer cannot blindly rely on training to protect it from employment liability. In addition, it must be remembered that businesses have an ever-changing workforce and the training given must continually undergo changes as well.

A failure to keep the training current may be viewed the same as no training at all. If that should occur, EPL insurance would still provide protection for the employer.

14. <u>Changing Technologies May Cause an Employer to Make the Wrong Employment Decision</u>

Conducting an investigation of an employee's complaint is a necessary step in defending a potential employment claim. Unfortunately, rapidly changing technology may produce errors in the investigation performed by the employer. Those errors not only affect the original employment complaint but could, in fact, produce a new claim of discrimination or invasion of privacy.

As a result of e-mail's informal nature and assumed impermanence, employees often use e-mails to send messages that may be too candid or inappropriate to put in writing. In fact, however, most e-mail systems capture the exact message and create a complete record of that message. It is a mistake to believe that once the "delete" key is hit, the message has been deleted. In fact, information remains on the hard drive until the computer runs out of new (unused) space. This makes it easier to retrieve electronic messages than to retrieve paper. Similar trails are left by computer users who download information from the Internet, including material from pornographic sites.

When investigating a possible violation of a company's electronic media policy, the investigator must recognize "spoofing," creation of an e-mail message that appears to have been created by someone else. In that situation, the actual electronic harasser is not the person who supposedly sent the harassing e-mail. Similarly, pornographic material on an employee's computer may have been downloaded onto the computer by a different employee.

Re-mailers may also be used to hide the culprit's identity. Re-mailers are stations on the Internet that hide the identity of users who send messages through them. This makes it almost impossible to trace the actual author of the message.

Headers may also be used to deceive the recipient and the investigator as to the identity of the author of the e-mail. A header is the message at the beginning of the e-mail that looks like names and codes. It identifies the route the message traveled, other recipients, the time, date and location from which the e-mail was sent, and the time, date and location at which the message was received. Although the header is supposed to identify the name of the sender, the sender may not be the person who wrote the e-mail. If one employee obtains access to another employee's computer or password, he or she may send messages from the other person's computer which appear, because of the header, to have been sent by the other employee.

Changing technology may cause an employer unaware of these technological developments to make an incorrect employment decision. The termination, or discipline, of an innocent employee in itself can lead to a claim for wrongful termination, intentional infliction of emotional distress, defamation, or various other claims. The fact that the employer acted in good faith, although incompetently, will not be a defense. EPL insurance, however, will provide protection for investigative and disciplinary errors.