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Coverage shrinks for wage lawsuits

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As layoffs drive wage-and-hour claims, middle-market employers may find defense coverage more difficult to find and more costly when they do, particularly in California, insurers and brokers say.

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The market firming for wage-and-hour defense coverage comes after a rise in claims by laid-off workers who allege violations of the Fair Labor Standards Act and other laws, according to brokers and insurers.

Laid-off workers can, for example, allege that they were not paid for all hours worked, misclassified or not properly paid overtime, experts say.

"It's a reflection of how difficult it is for employees to find another job," said Christian Hamlin, a professional lines producer in the Los Angeles office of wholesaler Burns & Wilcox Ltd.

The U.S. unemployment rate remains high, but has improved from the decade's peak unemployment rate of 10.1% in October 2009, according to the U.S. Department of Labor's Bureau of Labor Statistics. In February, the U.S. unemployment rate was 8.9%, a 0.1% decline from January, according to BLS.

At the same time, industry experts say they have seen an increase in wage-

and-hour claims, which has led some insurers to stop writing such defense coverage, which most typically is provided for as a sublimit under employment practices liability insurance policies.

Coverage remains available as some insurers continue to provide it, said Michael Mahoney, senior vp at Willis Insurance Services of California Inc. in San Francisco.

But new or additional insurers have not replaced those that have left the market, and underwriters still in the market have increased their prices for the wage-and-hour coverage or, in certain cases, simply declined certain accounts, other sources said.

"People are leaving, but no one is coming in," said Peter Taffae, a professional lines expert at Los Angeles-based wholesale brokerage Executive Perils Insurance Services. "So from a supply-and-demand factor, it's getting harder and more expensive."

Increasingly, insureds who have experienced even a single claim are unable to renew the coverage, Mr. Taffae said.

"We wouldn't have had this conversation three months ago," Mr. Taffae said. "Now we are starting to see insurers who have been writing it taking a step back and saying, 'We don't want to do it anymore.'"

Limits for the defense of wage-and-hour claims typically have been modest, especially in contrast with a multimillion-dollar loss that wage-and-hour claims can produce when litigation costs are included, sources said. The coverage often is offered with sublimits of about \$100,000 to \$250,000 under an EPL policy, sources said.

Despite the low limits typically available, brokers say they have negotiated additional coverage on larger policies. Willis' Mr. Mahoney, for instance, said he negotiated \$1 million in wage-and-hour sublimits for a middle-market private employer that purchased \$10 million in total EPL limits.

Mr. Taffae said on one account he placed in December, an excess insurer dropped down to provide \$1 million in wage-and-hour defense coverage just above the \$1 million in sublimits provided by the primary insurer. The primary

and excess insurers provided \$5 million each in overall EPL limits, Mr. Taffae said.

Larger employers with sizable deductibles won't be affected because they generally are not buying wage-and-hour sublimits that low, said Mark Knepshield, senior vp at Arthur J. Gallagher & Co. in Los Angeles.

"Middle-market companies, companies with below \$100 million in revenue, those are the ones that are going to feel that coverage tightening more than anyone else," as they are the most likely buyers of such coverage, he said.

Wage-and-hour issues are difficult to underwrite because they are more of a business risk than a traditional employment risk, Mr. Mahoney said.

Underwriters can easily evaluate an employer's controls for preventing harassment or discrimination, he said. But he said it is difficult for an underwriter to scrutinize an employer's determinations that one employee is exempt from overtime and another is not.

Among insurers that have offered a wage-and-hour product, market firming gradually has occurred during the past two or three years or so, coinciding with the weak economy, several sources said. But they added that the firming has accelerated recently.

Purchasers who have not followed the market may be surprised to find fewer options at renewal, or they may find some insurers provide smaller limits than they made available in the past, Mr. Knepshield said.

"It is relatively recent that people are feeling the effects," he added. "But I can tell you we could see that train coming a year and a half ago based on the sheer volume of claims."

Ronna Green, director of professional liability at Scottsdale Insurance Co. said the losses in California and adverse court decisions in the state have increasingly caught the attention of underwriters.

She said she thinks the market is turning, particularly in California, which is known as a "pro workers state" and a hot spot for EPL claims.

"Because of the legal climate there, if you generate a claim, the likelihood that it will be larger than average is pretty good," Ms. Green said. Scottsdale has

been raising its EPL pricing in California during past year because of losses in the state, she said.

Increasingly, wage-and-hour claims in California have become an "add-on" to lawsuits alleging wrongful termination as the lead allegation, said Burns & Wilcox's Mr. Hamlin.

Given that, whether an employer is likely to see a lawsuit with multiple allegations should be weighed when determining whether to purchase wage-and-hour sublimits, brokers said.

The sublimits could be a smarter purchase if employers feel they are likely to see only a wage-and-hour claim. But if they anticipate seeing a complaint that includes a wage-and-hour claim plus other major allegations, such as wrongful termination or discrimination, a duty-to-defend policy would provide coverage up to the full limits of the EPL policy for all of allegations.

Using a sublimit endorsement for wage-and-hour claims allows insurers to limit their exposure. Without the endorsement, insurers could be on the hook for the entire limits of an EPL policy due to a wage-and-hour claim, brokers said.



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