

**EMPLOYMENT LAW:
Coverage for Employment Related Issues**

**R. Brent Cooper
Dottie Sheffield
Katherine L. McClelland
COOPER & SCULLY, P.C.
Founders Square
900 Jackson Street
Suite 100
Dallas, Texas 75202
(214) 712-9500
(214) 712-9540 (fax)**

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CGL COVERAGE FOR EMPLOYMENT RELATED CLAIMS

I. INTRODUCTION

Employment litigation is one of the fastest growing areas of litigation in the state of Texas at this time. These claims range from wrongful termination to discrimination, harassment to violations of privacy. While specialty coverage is available for some of these claims, it is often expensive or unavailable. Most companies will turn to the coverage under their general liability or worker's compensation policies as a source of coverage for these types of claims. This paper will focus on the coverage afforded under the general liability policies and worker's compensation policies for these types of claims.

In determining whether a CGL policy provides coverage for employment-related claims, a threshold inquiry is whether the complaint filed against the insured alleges damages for the types of injury covered under that policy. To find coverage for any such claim under the CGL, one must establish three things: (1) that the employment-related injury was caused by an "occurrence"; (2) that the injury meets the policy definition of "bodily injury," "property damage," or "personal injury"; and (3) that no policy exclusion is applicable to the injury.

A. What constitutes an Occurrence?

Under the Coverage A insuring agreement of the CGL policy, the insurer agrees to pay those sums that the insured becomes legally obligated to pay as damages because of "bodily injury" or "property damage" to which this insurance applies. This insurance applies to bodily injury or property damage only if (1) the bodily injury or property damage is caused by an occurrence. An "occurrence" is defined in the policy as an accident, including continuous or repeated exposure to substantially the same general harmful conditions. Whether the bodily injury or property damage is caused by an occurrence hinges on fortuity. What really matters is whether the bodily injury or property damage results without the insured's foresight or anticipation.

There are two lines of Texas cases construing the definition of "occurrence" for the purpose of liability insurance coverage. The first pertains to coverage of claims against an insured for damage caused by its alleged intentional torts. According to this body of law, damage that is the natural result of voluntary and intentional acts is deemed *not* to have been caused by

an occurrence, no matter how unexpected, unforeseen, and unintended that damage may be. *Argonaut Southwest Ins. Co. v. Maupin*, 500 S.W.2d 633, 635 (Tex.1973) (citing *Thomason v. United States Fidelity & Guar. Co.*, 248 F.2d 417, 419 (5th Cir.1957)).

The Supreme Court of Texas defined the extent to which an occurrence may be found where an insured's intentional act leads to unintended consequences. *Trinity Universal Ins. Co. v. Cowan*, 945 S.W.2d 819 (Tex. 1997). Gregory Gage, the insured, was working as a grocery store photo lab clerk when a roll of film containing somewhat revealing pictures of Nicole Cowan was delivered for developing. Gage made extra prints of four of these pictures and later showed them to some friends. Eventually the photos were shown to an acquaintance of Cowan who advised Cowan that the pictures had been distributed. Cowan sued Gage and Gage sought coverage from his homeowner's policy issued by Trinity Universal Insurance Company. Ultimately Trinity denied coverage because Trinity argued that the facts of the case were not an "accident" such as to invoke an "occurrence." It was undisputed that Gage intentionally made copies of Cowan's photographs and showed them to his friends. However, Gage testified that he did not intend for Cowan to learn of his actions. Therefore, Gage argued, he accidentally caused Cowan to suffer severe mental anguish, among other damages. In response, Trinity argued that no "accident" could arise where an actor intends to engage in the conduct which gave rise to the injury. The court, citing *Maupin*, took an approach that was somewhere in the middle of these two extremes that resulted in precluding coverage for Gage based on the lack of an occurrence. The court reaffirmed that the actor's subjective intent or awareness of the potential for resulting injury was not the test in determining an "accident." Rather, Gage's conduct was not an "accident" because the damages naturally flow from Gage's intentional acts.

Because the injury to Cowan was the type of injury that "ordinarily follows" from Gage's conduct and the injuries could be "reasonably anticipated from the use of the means or an effect" that Gage can "be charged with . . . producing," the court held that there was no occurrence. *Id.* at 828 citing *State Farm Fire & Cas. Co. v. S.S.*, 858 S.W.2d 374, 377 (Tex. 1993) (no occurrence where intentional transmission of genital herpes). Further, the court rejected Trinity's argument that there is never an occurrence when the insured's acts are intentional, finding that Trinity's approach would render coverage illusory for many of the things for which insureds commonly purchase insurance. Specifically, the Court held that Trinity's approach would directly conflict with their earlier holdings that

an "accident" includes the "negligent" acts of the insured causing damage which is undesigned and unexpected. *Id.* at 828 citing *Massachusetts Bonding & Ins. Co. v. Orkin Exterminating Co.*, 416 S.W.2d 396 (Tex. 1967). At least one court has seized on this comment by the Supreme Court in *Cowan* to note that the mere fact that the insured intended to engage in the act or conduct that gave rise to the alleged damage does not mean that there can be no accident or occurrence. See *E&L Chipping v. Hanover Ins. Co.*, 962 S.W.2d 272, 276 (Tex. App.–Beaumont 1998, no writ)(Holding that the intentional spraying of contaminated water to put out a fire resulting in damage to adjacent property was an accident or occurrence and was not excluded by the "expected and intended" exclusion.).

In cases involving claims against an insured for damage arising out of his alleged negligence, however, a second line of cases has developed, following *Massachusetts Bonding & Ins. Co. v. Orkin Exterminating Co.*, 416 S.W.2d 396 (Tex.1967). "Accident" in the context of general liability insurance includes negligent acts of the insured causing damage which is undesigned and unexpected. See *Mid-Continent Cas. Co. v. Camaley Energy Co., Inc.*, 364 F.Supp.2d 600 (N.D.Tex. 2005) (insureds' well boring deviation that caused damage to other property was accidental and not intentional as the insured was sued for negligence and trespass based on their loss of control of well boring and accidental deviation); *CU Lloyd's of Texas v. Main Street Homes*, 79 S.W.3d 687 (Tex. App. – Austin 2002, no pet.) (homeowner's allegations that general contractor built homes after learning that foundation designs were inadequate for soil conditions and failed to disclose that knowledge to purchasers stated an accident and thus an occurrence within the meaning of the general liability policy where the homeowners alleged negligence and did not limit their claims to intentional tort or shoddy workmanship, but claimed loss from erroneous soil surveys and faulty or inadequate design by the engineering firm); *Decorative Center of Houston v. Employers Cas. Co.*, 833 S.W.2d 257 (Tex.App.-Corpus Christi 1992, writ denied) (Liability policy issued to owner and general contractor of construction project clearly covered nuisance and trespass against adjoining property owners only if those acts were committed negligently and not intentionally, and, thus, coverage for suit by adjacent property owner against project owner and contractor was precluded).

Based on this line of cases, it is obvious that where unintended or unexpected damages result from the negligence of the insured, an occurrence may have resulted. If there are sufficient allegations supporting

the unintended or unexpected damages, the insurer may not deny coverage based upon the lack of fortuity or an occurrence until an insurer can demonstrate that the damages resulting from the policyholder's act are calculated or expected damages.

In further defining this concept, the Federal Court of Appeals for the Fifth Circuit has particularly focused its attention on whether the insured's injury was the natural and probable consequence of intentional conduct. In pertinent part, the Fifth Circuit stated in *Meridian Oil Production Co. v. Hartford Accident & Indemnity Co.*, 27 F.3d 150 (5th Cir. 1994):

Texas courts afford coverage for fortuitous damages but deny coverage when damages are the natural and probable consequence of intentional conduct. Regardless of whether the policies involved are worded to cover "accidents" or "occurrence," all offer minor variations of the same, essential concept; coverage does not exist for inevitable results which predictably and necessarily emanate from deliberate actions.

Id. at 152 (footnote omitted).

Thus, at the heart of the accident/fortuity analysis, the focus is not on whether the policyholder's acts were intentional, but instead on whether the resulting injury or damage was expected or intentional. See *Hartford Casualty Co. v. Cruse*, 938 F.2d 601, 604-05 (5th Cir. 1991); *Bituminous Cas. Corp. v. Vacuum Tanks, Inc.*, 75 F.3d 1048 (5th Cir. 1996). Therefore, to determine whether an occurrence has taken place, it is imperative to analyze the acts of the insured that lie beneath the particular injury at issue.

In the context of employment related disputes, as with other claims, the bodily injury must be caused by an occurrence. In *Western Heritage Ins. Co. v. Magic Years Learning Centers and Child Care, Inc.*, 45 F.3d 85, (5th Cir.1995), the court stated that the pleadings must allege bodily injury caused by an occurrence for coverage to be triggered under the CGL policy. In *Magic Years*, the insured day care center sought coverage for a suit filed by a former employee for allegations against the day care center on the theory of respondeat superior and gross negligence.

The state court suit filed by the former employee alleged that the president of the day care center, Charles Wilson, sexually harassed her at work and under other circumstances, that such harassment led to

her constructive discharge, that he invaded her right to privacy by asking probing questions about her personal life and sexual activities, that he unlawfully imprisoned her, that the harassment and her constructive discharge violated her federal and state civil rights, that he committed assault and battery by touching her in an offensive, unwelcome manner, and that he acted with such want of care and conscious indifference as to warrant punitive damages. The Plaintiff claimed that Mr. Wilson and Magic Years were responsible under the doctrine of respondeat superior for Mr. Wilson's conduct and that they were grossly negligent in entrusting him with supervisory responsibility, in not providing a workplace free of sexual harassment, and in not providing an adequate avenue for redress. They also alleged that Magic Years and Mr. Wilson intentionally inflicted severe emotional distress upon the plaintiff.

Reviewing the commercial general liability policy of the insurer, Western Heritage, the court stated that the pleadings must allege bodily injury caused by an occurrence. The insurance policy defined an occurrence as "an accident, including continuous or repeated exposure to conditions, which results in bodily injury or property damage neither expected nor intended from the standpoint of the insured." Western Heritage contended that the definition of occurrence excluded intentionally inflicted injuries and therefore excluded the allegations which arose out of sexual harassment because Mr. Wilson intended or expected to injure Mrs. Alexander when he harassed her and touched her in an offensive, unwelcome manner. The court held that the general definition of occurrence would normally exclude allegations of sexual harassment by the insured, but the Western Heritage policy included an endorsement that expressly provided for coverage for any act which may be considered sexual in nature. The court held that this endorsement trumped the definition of "occurrence" and the assault and battery exclusion, but not the employer's liability exclusion. The court ultimately held that there was no coverage due to an employer's liability exclusion which the court determined only applied against the named insured, Magic Years. With respect to the Mr. Wilson, an employee of the day care center, the court found that the allegations alleged bodily injury which may not have been expected or intended from the standpoint of those employees, so there was coverage for Mr. Wilson under the policy.

B. Is the Injury Covered?

1. Bodily Injury

Even if the employment practices that give rise to discrimination or wrongful termination suits are regarded as "occurrences" (i.e., accidents), does the resulting injury—humiliation, mental anguish, loss of self-esteem, depression, etc.—qualify as "bodily injury" so as to bring Coverage A of the CGL policy to bear on the claim?

A CGL policy typically covers "all sums which the insured shall become legally obligated to pay as damages because of ..."bodily injury." "Bodily injury" usually is defined as "bodily injury, sickness, [or] disease. . . ." Traditionally, coverage for "bodily injury" required allegations of physical symptoms resulting from tortious conduct. Most employment-related claims, however, do not allege classic bodily injury. Instead, plaintiffs frequently allege emotional distress, including mental anguish and suffering, sometimes coupled with the physical symptoms of such suffering. Thus, the issue arises as to whether emotional distress constitutes a covered "bodily injury."

The Texas Supreme Court has explained that the "commonly understood meaning of 'bodily' ... implies a physical, and not purely mental, emotional, or spiritual harm." *Trinity Univ. Ins. Co. v. Cowan*, 945 S.W.2d 819, 823 (Tex.1997). In *Cowan*, the supreme court held that purely emotional injuries do not constitute bodily injury within the terms of insurance contracts. *Id.* at 823. The supreme court further held that the term bodily injury requires "an injury to the physical structure of the human body." *Id.* Moreover, the supreme court stated "[t]hat Texas tort law allows for recovery of mental anguish damages unaccompanied by physical manifestations in some circumstances ... does not mean that insurance coverage for bodily injury necessarily encompasses purely emotional injuries." *Id.* In *Miller v. Windsor Insurance Co.*, 923 S.W.2d 91 (Tex.App.Fort Worth 1996, writ denied), the court of appeals stated that mental anguish suffered by one not involved in an actual accident is not a bodily injury. *See* 923 S.W.2d at 97. Likewise, in *Eshtary v. Allstate Insurance Co.*, 767 S.W.2d 291 (Tex.App.Fort Worth 1989, writ denied), the court of appeals held that "the term "bodily injury" cannot reasonably be construed to incorporate mental pain and anguish if the claim being asserted is a derivative claim arising only as the consequence of injuries to another person." *See* 767 S.W.2d at 293.

The majority of jurisdictions operate under the same doctrine as Texas in requiring that mental anguish or other emotional distress produce some physical manifestation to be considered "bodily injury" as that term is used in liability insurance policies. See *Rolette County v. Western Cas. & Surety Co.*, 452 F Supp 125 (D. ND 1978); *American & Foreign Ins. Co. v. Church Schools*, 645 F Supp 628 (E.D. Va 1986); *St. Paul Fire & Marine Ins. Co. v. Campbell County School Dist. No. 1*, 612 F Supp 285 (D. Wyo 1985) (emotional suffering incurred in violation of First Amendment rights); *Mellow v. Medical Malpractice Joint Underwriting Assn.*, 567 A2d 367 (RI 1989) (damages incurred in invasion of privacy leading to emotional harm); *Allstate Insurance Co. v. Diamant*, 401 Mass 654, 518 NE2d 1154 (1988) (damages arising out of defamation and intentional infliction of emotional distress); *E-Z Loader Boat Trailers, Inc. v. Travelers Indemnity Co.*, 106 Wash2d 901, 726 P2d 439 (1986) (alleged illegal discharge due to sex and age discrimination leading to emotional distress); *West American Ins. Co. v. Bank of Isle of Wright*, 673 F Supp 760 (E.D. Va 1987).

In *SL Industries, Inc. v. American Motorists Insurance Co.*, 607 A2d 1266 (NJ 1992), the New Jersey Supreme Court considered the issue of CGL coverage for an employer sued by one of its retired executives. The executive had been encouraged to take an early retirement offer on the grounds that his position was being eliminated. After his retirement, another person was hired as his replacement. The retired executive sued his former employer, alleging age discrimination under federal law and asserting that the employer's actions had caused him "physical and mental pain and suffering, including humiliation, loss of self-esteem, irritability and sleeplessness." The employer submitted the claim to its general liability insurer, which denied the claim on the basis that no "bodily injury" was being alleged.

The court determined that the only element of the employee's complaint against the employer that had any potentiality of triggering "bodily injury" coverage under the CGL was the assertion of "sleeplessness." Ultimately, the court rejected even this possibility, finding that the employee's sleeplessness was 'at base, emotional in nature.' It went on to concur with precedents from other jurisdictions that purely emotional injuries—without accompanying physical symptoms—did not constitute "bodily injury" for the purposes of CGL coverage:

We hold that in the context of purely emotional distress, without physical

manifestations, the phrase 'bodily injury' is not ambiguous. Its ordinary meaning connotes some sort of physical problem.

A comparable ruling was handed down by the Minnesota Court of Appeals in *Hamlin v. Western National Mutual Insurance Co.*, 461 NW 2d 395 (1990), a case that involved sexual harassment charges. The Minnesota court, like the New Jersey court in *SL Industries*, found that the employee's allegations of mental suffering caused by her employer's sexual harassment did not constitute "bodily injury" absent any accompanying physical problems.

The same conclusion was reached by the Colorado Supreme Court in *National Casualty Co. v. Great Southwest Fire Insurance Co.*, 833 P2d 741 (1992). A wrongful termination suit against an employer included allegations of emotional distress but not physical injury or pain. The court reviewed decisions from a number of jurisdictions and concluded that only a few courts, *which we decline to follow*, have determined that bodily injury includes emotional distress when there is no physical impact, fear of physical harm, or physical manifestation of emotional distress (emphasis added).

2. Personal Injury Coverage

Coverage B of the CGL policy provides personal and advertising injury liability coverage. Coverage for "personal injury" arises out of certain listed offenses, including: 1) false arrest, detention or imprisonment; 2) malicious prosecution; 3) wrongful eviction from, wrongful entry into, or invasion of the right of private occupancy; 4) oral or written publication of material that slanders or libels a person or organization or disparages a person's or organization's goods, products, or services; and 5) oral or written publication of material that violates a person's right of privacy. Many older policy forms expanded the coverage for personal injuries by specifically adding "discrimination" to the list of covered torts, thereby providing an obvious trigger of coverage. However, newer policies are either unlikely to contain this express coverage of discrimination or to include the coverage only with explicit and substantial limitations. *Transport Ins. Co. v. Lee Way Motor Freight, Inc.*, 487 F. Supp. 1325, 1327 (N.D. Tex. 1980) (describing the carrier's change in umbrella policy forms between 1972 and 1973, which stopped including discrimination in the definition of personal injury).

Unlike Coverage A, Coverage B has no "occurrence" requirement. As such, there may be

coverage for employment-related claims but only when the complaint asserts a claim for one of the specifically enumerated offenses in the definitions of "personal and advertising injury." *Atlantic Mutual Ins. Co. v. J. Lamb, Inc.*, 100 Cal.App.4th 1017, 1032, 123 Cal.Rptr.2d 256, 267 (Cal.App. 2 Dist., 2002) ("advertising injury" and "personal injury" are terms of art that describe coverage for certain enumerated offenses that are spelled out in the policy); *State Bancorp, Inc. v. U.S. Fidelity and Guar. Ins. Co.*, 199 W.Va. 99, 107, 483 S.E.2d 228, 236 (W.Va., 1997) (under the provisions of coverage B, the "personal injury" or "advertising injury" must arise out of certain enumerated offenses committed by the insured).

Plaintiff employees often include allegations of false imprisonment in their sexual harassment complaints, another enumerated intentional tort under the definition of "personal injury" in Coverage B. However, not every unwelcome physical encounter amounts to a false imprisonment, and so the facts, as pleaded in the complaint, will trigger coverage only if they constitute the tort of false imprisonment. *See Cornhill Ins. PLC v. Valsamis, Inc.*, 106 F.3d 80, 85 (5th Cir. 1997) (finding that allegations that a supervisor attempted to force himself on plaintiff employee in a supply room did not trigger coverage because there was no allegation that the door was locked or that the supervisor detained her in the room for any period of time by use of physical force or threats).

Most courts have refused to extend coverage to personal injury resulting from non-enumerated offenses. *Lindsey v. Admiral Ins. Co.*, 804 F.Supp. 47, 50-52 (N.D. Cal. 1992) (personal injury coverage did not cover claims of employment-related sexual harassment); *United Pacific Ins. Co. v. First Interstate Bancsystems of Montana, Inc.*, 690 F.Supp. 917 (D. Mont. 1988) (wrongful termination suit did not specifically allege tort of defamation; court held personal injury coverage applies only to claims actually arising out of torts enumerated in policy).

Personal injury coverage generally is written as a "self-contained" coverage with its own set of exclusions. Those exclusions should be considered in determining whether coverage exists. *See Old Republic Ins. Co. v. Comprehensive Health Care Assoc., Inc.*, 2 F.3d 105, 109-10 (5th Cir. 1993) (applying Texas law) (exclusion in umbrella policy for bodily injury, property damage, or personal injury "otherwise arising out of employment" precluded coverage or duty to defend for claims against insured company stemming from employees' allegations of sexual harassment). The most noted of these exclusions are the exclusions

for knowing violations of rights of another and material published with knowledge of its falsity. *See Travelers Indem. Co. of Connecticut v. Presbyterian Healthcare Resources*, 2004 WL 389090, *7 (N.D.Tex. 2004) (nonreported) (because the defamation claims in the underlying suit also allege that the defamatory publications were made recklessly, court held that it was not necessary to prove knowledge of falsity in order to prevail and found coverage was excluded by the "Knowledge of Falsity" provision).

State Farm Lloyds Ins. Co. v. Maldonado, 963 S.W.2d 38, (Tex. 1998), involved an insured seeking coverage under their personal injury coverage for allegedly slanderous statements made by the employer about a former employee. In *Maldonado*, Adelfa Maldonado worked for Curtis Robert, Sr., as a bookkeeper for nearly twenty years. In 1990, Maldonado resigned her position with Robert and went to work for the Brooks County Auditor. Shortly thereafter, Robert began to circulate stories that Maldonado was a thief and a prostitute. Because of Robert's statements, a district court judge passed over Maldonado for a promotion to County Auditor. There was also evidence that Robert's statements seriously damaged Maldonado's reputation in the community. Maldonado sued Robert for defamation. Robert was insured by State Farm under a policy covering up to \$300,000 in personal injury damages caused by an offense arising out of his business as a certified public accountant. State Farm agreed to defend the action against Robert under a reservation of rights.

The State Farm policy definition of "personal injury" included injury arising out of slander. The policy excludes coverage for personal injury arising from slanderous statements made with knowledge of their falsity and personal injury. The reservation of rights was issued due to some question about whether Robert made the statements with knowledge of their falsity and whether the statements arose from his business. The case went to trial and judgment was rendered for Maldonado in the amount of \$2,000,000. State Farm appealed asserting several no evidence points of error. State Farm asserted that there was no policy coverage because (1) Robert's statements that Maldonado was a thief and a prostitute did not arise out of his business as a CPA; (2) Robert made the statements with knowledge of their falsity.

The appellate court held that there was evidence that Maldonado worked for Robert as a bookkeeper. The allegation that Maldonado was a thief was directly related to her position as a bookkeeper. Robert accused her of taking money from a safety deposit box to which she had access solely because of her position as

bookkeeper. Robert's allegation that Maldonado was a prostitute did not appear to have any factual basis in her employment as a bookkeeper. But, this did not negate coverage for the allegations of theft. The court stated that the jury could have concluded that the "prostitute" allegation also arose from Robert's business because the only evidence of any relationship between Robert and Maldonado was as employer and employee. Therefore, the court concluded that the jury could have inferred that both of Robert's statements about Maldonado arose from that business relationship.

In regards to Robert's knowledge that he knew at the time he made the statements about Maldonado that they were not true, the court stated that there was evidence in the record from which the jury could have found that Robert knew what he was saying was false. But the court said that the mere existence of evidence supporting State Farm's position, however, was not sufficient to entitle State Farm to relief. The evidence in support of the jury's finding of coverage was that, at the time of the statements, Robert was suffering from a terminal illness and was taking excessive doses of a prescription drug. His behavior and appearance at that time were not normal. There was evidence from which the jury could have inferred that Robert's perception and judgment were distorted by the medication, thus preventing him from realizing the falsity of his statements. Also, there was evidence that the trial court in the defamation suit found that Robert did not have knowledge of the falsity of his statements. Therefore the implied finding that Robert was not aware of the falsity of his statements was supported by legally sufficient evidence. Because the trial court had found coverage, the appellate court upheld that finding, and held that Maldonado was entitled to recover the policy limits of \$300,000.

C. Property Damage

Under most CGL policies, "property damage" is defined to include "physical injury to or destruction of tangible property which occurs during the policy period, including the loss of use thereof at any time resulting therefrom"

Employment claims based upon discrimination or wrongful discharge generally seek damages for lost wages and loss of benefits, such as retirement, sick and vacation pay, and health and life insurance benefits. Courts typically conclude that these are economic losses that do not constitute the "tangible" property required under the policy definition of "property damage." Rather, a policy's "property damage" provision contemplates physical damage or destruction

to tangible objects such as buildings, automobiles, and business equipment. *Lamar Truck Plaza, Inc. v. Sentry Ins.*, 757 P.2d 1143, 1144 (Colo. Ct. App. 1988) (tangible property is property "which is capable of being handled, touched, or physically possessed," and "[p]urely economic losses are not included in this definition").

Texas courts hold that economic loss is not property damage under a liability policy. *Houston Petroleum Co. v. Highlands Ins. Co.*, 830 S.W.2d 153,156 (Tex. App.—Houston [1st Dist.] 1991, writ denied); *Terra Int'l, Inc. v. Commonwealth Lloyd's Ins. Co.*, 829 S.W.2d 270, 272 (Tex. App.—Dallas 1992, writ denied); see also *Gibson & Assoc., Inc. v. Home Ins. Co.*, 966 F.Supp. 468 (N.D.Tex. 1997) (As the City's breach of contract claim involves only economic loss and not property damage and does not subject the insurer to any defense obligation); *Nutmeg Ins. Co. v. Pro-Line Corp.*, 836 F.Supp. 385, 388-89 (N.D. Tex. 1993) (finding that, pursuant to the interpretation of general liability policies employed by Texas courts, lost product sales, like lost investments and profits, do not constitute "property damage").

Therefore, employment claims based upon discrimination or wrongful discharge where the plaintiff's generally seek damages for lost wages and loss of benefits, would not be considered "property damages" as defined under the general liability policy.

D. What policy exclusions are applicable?

Even if the hurdles placed by the terms of the CGL coverage grant are met in a particular case, the single strongest bar to coverage for an employment related claim under a CGL policy relates to exclusions under coverage. The standard form CGL coverage agreement contains an intentional acts exclusion as well as the employers' liability exclusion.

1. Intentional Acts Exclusion

The standard CGL policy contains an exclusion which bars coverage for injuries or damage that is either expected or intended from the standpoint of the insured. Since employment-related complaints often allege that the policyholder intentionally caused the plaintiff's injuries, e.g., that the policyholder intentionally inflicted emotional distress, the operation of the expected or intended proviso may be a crucial issue in any employment-related coverage dispute.

Texas courts have held that in determining whether this exclusion applies, focus is on whether the wrongdoer had an intent to injure the plaintiffs, rather than focusing on whether the conduct was voluntary

and intentional. *See State Farm Fire & Casualty Co. v. S.S. & G.W.*, 858 S.W.2d 374, 378 (Tex. 1993). Ordinarily, whether the insured intended harm or injury to result from an intentional act within the meaning of this policy exclusion is a question of fact. *Id.* Under the definition of intent stated in the Restatement (Second) of Torts, an insured intends to harm another if he intends the consequences of his act, or believes that they are substantially certain to follow. *Id.* citing Restatement (Second) of Torts §8A (1965).

Perhaps the most critical issue arising in connection with the expected or intended defense is whose intentions or expectations are relevant in determining whether the expected or intended bars a claim from coverage. Circumstances can be readily imagined in which a complaint alleging discrimination, for example, has been filed against a large corporate policyholder in connection with the acts of a low-level employee far removed from any policy-making or administrative responsibilities. The issue is whether, if the offending employee acted with the intent to cause injury to the plaintiff, the policyholder-corporation should be barred from coverage for that reason alone.

Prior Texas law supported the argument that when the conduct that caused the injury was intentional, even though the named insured did not commit the intentional act, there was no coverage. The courts simply imputed the actor's intent to that of the insured, arguing that but for the actor's excluded conduct, there would be no claim against the insured. *See Am. States Ins. Co. v. Bailey*, 133 F.3d 363 (5th Cir.1998)(sexual act exclusion applied to anything "arising out of" a sexual act was excluded under the specific policy language and therefore applied to specific claims against the church and the associate ministers including allegations of negligence, negligent hiring and supervision of Bailey); *New York Life Ins. Co. v. Travelers Ins. Co.*, 92 F.3d 336, 339-40 (5th Cir.1996) ("A claim against a principal is 'related' to and 'interdependent' on a claim against an agent if the claim against the principal would not exist absent the claim against the agent"; with respect to claims in an underlying state court suit filed by New York Life Insurance Company alleging fraud, negligent hiring, training, and supervision of employees that defrauded New York Life Insurance Company's employees, holding that the employee's underlying acts were not an "occurrence" under the policy issued by Travelers Insurance Company because they were intentional and fraudulent, and that the negligence claims were not covered because they were related to, interdependent on, and inseparable from the insured's fraudulent conduct); *Columbia Mut. Ins. Co. v. Fiesta Mart, Inc.*, 987 F.2d 1124 (5th Cir.1993); *see also Folsom Inv.*

Inc. v. Am. Motorists Ins. Co. 26 S.W.3d 556 (Tex.App.-Dallas 2000, no pet.).

However, in 2002, a decision from the Texas Supreme Court changed this view and now requires that the "occurrence" requirement be determined from standpoint of the entity seeking coverage. *See King v. Dallas Fire Ins. Co.*, 85 S.W.3d 185 (Tex.2002). In *King*, the Texas Supreme Court held that allegations against an employer of negligent hiring, training and supervision constituted an occurrence under the terms of a general liability policy even though the injury was directly caused by the employee's intentional conduct. One of King's employees intentionally attacked a person who subsequently sued King, the employer, on a theory of respondeat superior liability and for negligent hiring, training and supervision of the employee. King sought to enforce the duty to defend in a commercial liability policy issued by Dallas Fire Insurance Company. In *King*, the Dallas Fire Insurance Company's policy contained a separation-of-insureds provision that explicitly established separate policies for King and its employee, but each policy stated that the insureds were to be treated "[a]s if each Named Insured [King] were the only Named Insured," i.e., as if King were the only insured. *Id.* At issue before the high court was "whether an employer's alleged negligent hiring, training and supervision constitute an 'occurrence' under the terms of the policy even though the injury was directly caused by the employee's intentional act." *Id.* The Texas Supreme Court rejected the Fifth Circuit's application of the "related to and interdependent rule" to deny the existence of duty to defend because the negligence claims against the employer derived from the intentional tortious acts of the employee and therefore there was no "occurrence." *Id.* Instead, the Texas Supreme Court held that the district court must examine the plaintiff's pleadings' allegations and the policy's language from the insured's standpoint and not attribute to the insured the employee-assaulter's intent. *Id.* The court expressly stated that:

[T]he Fifth Circuit's rule improperly imputes the actor's intent to the insured. That is to say, whether one who contributes to an injury is negligent is an inquiry independent from whether another who directly causes the injury acted intentionally. Essentially the actor's intent is not imputed to the insured in determining whether there was an occurrence. *Id.*

Based on the separation of insureds provision, the court determined whether there was an occurrence by

reviewing the coverage as if King, the employer, were the only insured. In doing so, the court gave meaning to the other provisions such as the intentional injury exclusion and the assault and battery or sexual misconduct exclusions that would otherwise be surplusage if the actor's intentional conduct was sufficient to exclude claims brought against another responsible party. The Texas Supreme Court concluded there was an "occurrence," invoking the insurer's duty to defend. *See also Nutmeg Ins. Co. v. Clear Lake City Water Authority*, 229 F.Supp.2d 668, 684 -685 (S.D.Tex. 2002) (The holding in *King* was not applicable because Claimants' causes of action were solely against the insured. However, the court rejected the insurer's global argument of no coverage for any claim that is "connected with," "related to," "interdependent with" or "arising from" an excluded act that existed only because of the excluded act based upon the existence of the separation of insureds clause); *Roman Catholic Diocese of Dallas v. Grahmann*, 133 S.W.3d 887 (Tex. App. – Dallas 2004 no pet.); *Acceptance Ins. Co. v. Life Care Corp.*, 89 S.W.3d 773 (Tex. App. – Corpus Christi 2002, no pet.) (there were no factual allegations of intent against the insured and no agency interdependency links between the conduct of Lifecare and its ex-employee; court held coverage where there are allegations of independent negligence on part of insured).

2. Employer's Liability Exclusion

Even if an employer satisfies the requirements of the insuring agreement by demonstrating that it is subject to a suit seeking damages for bodily injury caused by an occurrence, Coverage A contains an exclusion of coverage for suits seeking damages for bodily injury to an employee arising out of, and in the course of, employment.

This exclusion was intended to prevent an insurer from having to cover the liability of any insured because of injury sustained by its employee that would or should be covered by employer's liability insurance. This exclusion is not limited to employees of the named insuree; it applies to employees of any party that qualifies as an insured under the policy, including an additional insured. Donald S. Malecki and Arthur L. Flitner, *CGL Commercial General Liability* (8th Ed., p.37).

Insurers have consistently maintained that employment-related claims such as wrongful termination or sexual harassment fall within the scope of the employer's liability exclusion. The employers' liability exclusion was intended to exclude any and all injuries to an employee during the course of

employment. *See National Union Fire Ins. Co. of Pittsburgh, Pa. v. National Convenience Stores, Inc.*, 891 S.W.2d 20,21-22 (Tex. App.—San Antonio 1994, no writ)(employee's bodily injury allegedly resulting from supervisor's grabbing, embracing, or striking employee on employer's premises during office hours or office party fell under the employer's liability exclusion for bodily injury to an employee arising out and in the course of employment).

Texas courts have held that bodily injury caused by discrimination "[arises] out of and in the course of employment by the insured" by definition, reasoning that the harm cannot occur without the existence of an employment relationship. *Old Republic Ins. Co. v. Comprehensive Health Care Assocs., Inc.*, 2 F.3d 105, 109 (5th Cir. 1993). In *Comprehensive Health Care*, Steve Tarris, as administrator of the Henrietta Care Center operated by CHCA, subjected the plaintiff-employees "to sexual advancements, sexual innuendoes, harassing remarks and demands for sexual favors". When plaintiffs responded negatively to his advances, Tarris allegedly "insinuated that plaintiffs would not get pay raises; that he would not sign their paychecks or possibly not release their check to them; threatened to tamper with personal property belonging to them; that they would not be able to continue as employees ...; that working conditions and scheduling might be changed to a less than desirable atmosphere; and threatened that they would be unemployable in their chosen field either in this area or another." Plaintiffs also alleged that these events resulted in gender-based discrimination and subjected them to a "working environment where sexual compliance was made a condition of employment." They sought relief based upon sex discrimination, sex harassment, assault and slander by Tarris. The court held that because all of the causes of action alleged arose out of their plaintiffs' employment by CHCA, all of the alleged claims could not survive the employer's liability exclusion. *See also Aberdeen Ins. Co. v. Bovee*, 777 S.W.2d 442 (Tex.Ct.App.-El Paso, 1989, no writ) (construing a similar type exclusion to eliminate duty to defend).

Some jurisdictions have held that even conduct that occurs outside the scope of employment can be found to arise out of the course and scope of a plaintiff's employment. For example, in *Meadowbrook, Inc. v. Tower Ins. Co., Inc.*, 559 N.W.2d 411 (Minn. 1997), plaintiff employees brought claims of sexual harassment against their employer, alleging a "hostile work environment." The court held that the "course of employment" exclusion in the policy at issue applied to bar coverage, even though the complaint alleged instances of conduct outside "the

course and scope of employment." The alleged outside conduct included a remark during a pre-employment interview; a "pinch" at a company volleyball game; and telephone calls from the employer to an employee's home. Noting the claim asserted "that the environment in which the plaintiffs worked had become hostile," the court opined that it would be "incongruous to hold that such a claim can arise anywhere but in the course and scope of a plaintiff's employment." *Id.* at 420.

With the 1993 revision of the CGL policy, the terms "employee" and "leased worker" were defined in order to provide coverage for employee leasing arrangements. However, not within the scope of this exclusion are the "temporary worker," whose employment is on a day-to-day or short-term basis, and "volunteer workers," a newly defined term of the 2001 edition meaning in part a person who is not an employee of the named insured. Donald S. Malecki and Arthur L. Flitner, *CGL Commercial General Liability* (8th Ed., p.37-38).

3. Temporary Worker Exception

Texas courts have not interpreted the "temporary worker" exception. The majority of jurisdictions have adopted the interpretation that a person is a "temporary worker" only if he/she is furnished to the insured through some type of temporary agency. In *Nationwide Mut. Ins. Co. v. Allen*, 83 Conn.App. 526, 530, 850 A.2d 1047, 1052 (Conn.App.,2004) the court concluded that Nationwide did not have a duty to defend or to indemnify the insured, Allen, because the claimant, Shaw, was an employee and not an independent contractor or a temporary worker. Allen was a sole proprietor doing business as Allen Landscaping, which, for a fee, provides landscaping services to customers. Shaw performed landscaping work for Allen in exchange for pay. Shaw was injured in an accident while he operated a commercial riding mower that had been purchased by Allen. On June 16, 1999, Shaw filed a claim for workers' compensation benefits for his injuries. In a notice of claim signed by Shaw's attorney, those injuries were described as having arisen from an accident that occurred in the course of Shaw's employment by Allen.

Nationwide provided commercial general liability coverage to Allen for a policy period of June 1, 1998, to June 1, 1999 that excluded coverage for bodily injury to his employees arising out of and in the course of their employment with Allen or performing duties related to the conduct of Allen's business. One of the issues was whether Shaw was a temporary worker as defined by the policy. The defendants argue that the "temporary worker" definition is ambiguous because

their interpretation differs from that of the plaintiff. The defendants in their brief construed the "temporary worker" definition to mean "a person (1) who is furnished to you to substitute for a permanent employee on leave or (2) who is furnished to you to meet seasonal workload conditions or (3) who is furnished to you to meet short-term workload conditions." The plaintiff, however, construes "temporary worker" to mean "a person who is furnished to you to substitute for a permanent 'employee' on leave or [a person who is furnished to you] to meet seasonal or short-term workload conditions." *Id.* at 540.

The court concluded that the temporary worker language is clear and unambiguous. The court interpreted the terms such that a temporary worker is a person who must be "furnished" to the insured to substitute for a permanent employee on leave or to meet seasonal or short-term workload conditions. A plain reading of the relevant provisions of the insurance policy and an examination of the facts lead the court to the conclusion that Shaw was not a temporary worker as defined by the policy, because he was not "furnished" to Allen. The court found that Allen did not go to an employment agency, manpower service provider or any similar service to employ or to utilize Shaw's services. Shaw was not employed by anyone who lent or furnished him to Allen as an employee. Thus, the court concluded that Shaw was not furnished to Allen within the definition of "temporary worker" and could not be a temporary worker under the insurance policy. Additionally, the court observed that the temporary worker definition makes no grammatical sense without the "furnished by" language. *Id.* at 541.

Similarly, in *Miller v. Quincy Mut. Fire Ins. Co.*, 2003 WL 23469293, *9 (E.D.Pa.) (E.D.Pa.,2003) the insured argued that employer's liability policy exclusion did not apply because she was a temporary worker. Under the policy, "temporary worker" means "a person who is furnished to you [the insured] to substitute for a permanent 'employee' on leave or to meet seasonal or short-term workload conditions." The court held that initially, Miller's contention failed because she herself alleged in the underlying complaint that she was an employee. Moreover, the court held that the second problem with Miller's argument is that the definition of a temporary worker limits that designation to an employee who is "furnished" to the employer, which Miller was not. Miller argued that the word furnished applies only to substitute employees and not to seasonal employees. However, the court held that the structure of the sentence mandates a different interpretation. The court reasoned:

If the term "furnished" applies only to substitute employees, the sentence would read as to seasonal employees as follows: "Temporary worker means a person who is ... to meet seasonal or short-term workload conditions." Obviously this construction makes no sense and, therefore, "furnished" applies to both types of temporary workers.

Because Miller presented no evidence that she was "furnished" to her employer, Dollar Emporium, the court held she was not a temporary worker as defined by the policy.

4. Independent Contractor Exception

Independent contractors are not considered an "employee" as defined by the policy. There is specific case law that determines whether someone is acting as an independent contractor or as an employee. An employee is an agent of the employer. An agent is one who is authorized by the principal to transact business or manage some affair on the principal's behalf. *See Grace Cmty. Church v. Gonzales*, 853 S.W.2d 678, 680 (Tex. App.—Houston [14th Dist.] 1993, no writ). Under the general agency theory of liability, an employer is vicariously liable for the negligence of an agent or employee, even though the principal employer has not committed a wrong. *See e.g., Baptist Memorial Hospital System v. Sampson*, 969 S.W.2d 945, 947 (Tex. 1998). However "(a)n agency relationship cannot be presumed to exist." *See Royal Mortg. Corp. v. Montague*, 41 S.W.3d 721, 733 (Tex. App.—Fort Worth 2001, no pet.). Further, the party asserting that an agency relationship exists has the burden of proving it. *See Spangler v. Jones*, 861 S.W.2d 392, 396–97 (Tex. App.—Dallas 1993, writ denied). Although the question of agency is generally one of fact, whether it exists under established facts is a question of law. *See Ross v. Texas One Partnership*, 796 S.W.2d 206, 210 (Tex.App.—Dallas 1990).

The nature and extent to which the principal can control the agent is the key factor in determining the existence of the agency relationship. A key element of an agency relationship is the principal's right to control the agent in carrying out the assigned task. An agent is subject to the control of the principal except for the agent's physical conduct and is under a contractual obligation with the principal. *See Royal Mortg. Corp.*, at 733. To determine whether one is an independent contractor or employee, the test is whether the employer has the right to control the progress, details, and methods of operation of the employee's work. *See*

Limestone Products Distribution v. McNamara, 71 S.W.3d 308, 312 (Tex. 2002); *Thompson v. Travelers Indem. Co. of R.I.*, 789 S.W.2d 277, 278 (Tex. 1990). The employer must control not only the end result, but also the means and details of the accomplishment of the result. *See Thompson*, 789 S.W.2d at 278. If the employer does not have control over the employee, the employee is an independent contractor and the doctrine of respondeat superior does not apply. *See St. Joseph Hospital v. Wolff*, 94 S.W.3d 513, 542 (Tex. 2002).

The employer's right to control can be proved in two manners: (1) by evidence of a contractual agreement that explicitly gives the employer a right to control the employee, or (2) if there is no agreement, by evidence that the employee was performing services peculiar to the employer's business or that the employer actually had a right to control the employee. *See Newspapers, Inc. v. Love*, 380 S.W.2d 582, 590 (Tex. 1964).

To prove an employer-employee relationship, there must be proof of a written contract establishing that relationship. If the contract expressly gives the employer the right to control the details of and the means for completing the work, the contract is proof of an employer-employee relationship. *Id.* at 589. If the contract provides that the relationship is that of an independent contractor relationship and does not give the employer the right to control the details of the work, the contract is proof of an independent contractor relationship. *See Weidner v. Sanchez*, 14 S.W.3d 353, 373-74 (Tex. App.—Houston [14th Dist.] 2000, no pet.).

If there is no contract executed between the parties, or if the parties do not strictly adhere to contractual terms, the conduct of the parties must be used to establish an employer-employee relationship. To determine whether the employer had a right to control the employee, we must consider the following factors:

- (1) the independent nature of the employee's business. *See Limestone*, 71 S.W.3d at 312; *Pitchfork Land & Cattle, Co. v. King*, 346 S.W.2d 598, 602-04 (Tex. 1961);
- (2) the employee's obligation to furnish tools, supplies, and materials necessary to perform the job; *See Limestone*, 71 S.W.3d at 312; RESTATEMENT (SECOND) OF AGENCY § 220(2)(e), cmt. (k).
- (3) the employee's right to control the progress of the work except the final results; *See Limestone*, 71 S.W.3d at 312.

(4) the length of time of employment; *See Limestone*, 71 S.W.3d at 312, and
(5) the method of payment. *See Dougherty v. Gifford*, 826 S.W.2d 668, 679 (Tex. App.—Amarillo 1992, no writ).

5. Dual Capacity Doctrine

The employers liability exclusion is stated to apply whether the insured is liable as an employer or in any other capacity. The phrase “in any other capacity” is intended to encompass claims or suits against employers under the so-called dual capacity doctrine. The dual capacity doctrine holds that an employer normally shielded by the exclusive remedy of workers compensation laws may still be answerable for additional damages in tort. This type of claim can occur when the employer is judged to occupy a second capacity that constitutes an exposure that is common to the public in general, rather than to one’s employment. In other words, the injury, or the exposure thereto, is not necessarily peculiar to employment. It is an exposure to which the employee would have been equally exposed apart from his or her employment, as a consumer of the product. Donald S. Malecki & Arthur L. Flitner, *CGL Commercial General Liability* 38 (8th ed.).

In *Ramirez v. Pecan Deluxe Candy Co.*, 839 S.W.2d 101, 108 (Tex. App.Dallas 1992), the court of appeals discussed the dual capacity doctrine where a employee can exercise the option to receive workers’ compensation benefits as the exclusive remedy or sue under common law tort. Under this doctrine, an employer may be liable to its employee if it occupies, in addition to its capacity as employer, a second capacity that confers on it obligations independent of those imposed on it as an employer. *Cohn v. Spinks Indus., Inc.*, 602 S.W.2d 102, 103 (Tex. Civ. App.—Dallas 1980, writ ref’d n.r.e.); 2A ARTHUR LARSON, THE LAW OF WORKMAN’S COMPENSATION § 72.81, at 14-112 (1990). The dual capacity doctrine attempts to circumvent the exclusivity provisions of the workers’ compensation laws. *Cohn*, 602 S.W.2d at 103; *see also* TEX.REV. CIV.STAT.ANN. art. 8308-3.08 (Vernon Supp. 1992) (previously TEX.REV.CIV. STAT.ANN. art. 8306, § 3a (Vernon 1989)).

6. Third-Party-Over Actions

The last part of the employers liability exclusion deals with third-party-over actions. Employers can become involved in suits called third-party-over or simply third-party actions. These actions arise when an injured employee sues a negligent third party

(regardless of workers compensation benefits received), and the third party, in turn, impleads the employer. The employer, in such a case, must look to employer’s liability insurance unless the employer assumed the liability of the third party. In that instance, the CGL contractual liability coverage, rather than employer’s liability coverage, is the applicable coverage. Donald S. Malecki and Arthur L. Flitner, *CGL Commercial General Liability* (8th Ed., p.39).

In *U.S. Fire Ins. Co. v. Deering Mgt. Group, et al.* 946 F.Supp. 1271 (Tex. 1996), defendant Mary Ann Ybarra was sexually assaulted on the premises of a Wendy’s restaurant. Ybarra, an employee of Wendy’s, was assaulted as she was entering her automobile after closing the restaurant for the evening. The defendant brought a negligence suit against Wendy’s, Kiest, owner of premises, and Casterline, the franchise operator. U.S. Fire insured Kiest under a CGL policy. U.S. Fire filed declaratory judgment action seeking determination that it had no duty to defend or indemnify Kiest and the lessor due to the employer’s liability exclusion.

US Fire’s CGL policy contained the standard language found in the employer’s liability exclusion which provides that the exclusion does not apply “to liability assumed by the insured under an insured contract.” Under the provisions of the policy, an “insured contract” can be a lease of premises. In the lease of premises entered into between Kiest, Ltd. and Casterline, the lease provided that Casterline was to provide, for the benefit of both Casterline and Kiest, Ltd., a minimum of \$1,000,000 in comprehensive general liability insurance to cover claims for personal injury or death occurring on the leased premises.

Defendants argued that the employer’s liability exclusion did not apply since there was an “insured contract” where the lessee agreed to provide insurance for the benefit of the lessor and himself. The court held that the lease did not give rise to liability under the insured contract provision. While the lease did require the insured restaurant owner to secure insurance for the benefit of both the lessor and lessee, it did not require Casterline to hold Kiest, Ltd. harmless for any negligence on the part of Kiest, Ltd. Accordingly, the court found that the insured contract provision did not apply to this case. *Id.* at 1284.

7. Employment Related Practices Endorsement

In 1988, Insurance Services Office (“ISO”) proposed a new exclusion in CGL coverage forms relating to employment discrimination and similar

offenses. Following public hearings, ISO agreed not to add this exclusion to the coverage forms but, instead, to make the exclusion available by endorsement. The "Employment-Related Practices Exclusion" endorsement can be viewed as an extension of employer's liability exclusion e. because it appears to be an insurer's defense against attempts by insureds to secure coverage under their CGL policies for damages arising from wrongful terminations and other employment-related practices that have proliferated over the past several years.

The employment related practices endorsement excludes coverage for all "bodily injury" or "personal injury" arising out of employment-related practices, acts, or omissions, including coercion, demotion, defamation, harassment, humiliation, and/or discrimination. See *Potomac Ins. Co. of Illinois v. Peppers*, 890 F.Supp. 634 (S.D. Tex. 1995)(the court applied such an exclusion to claims of defamation alleged by one partner against another in the insured entity).

The violating conduct that gives rise to the alleged injury must be clearly employment-related to fall within this exclusion. See *Acceptance Ins. Co. v. Lifecare Corp.*, 89 S.W.3d 773, 784 -785 (Tex.App.-Corpus Christi 2002, pet. denied) (Lifecare, negligently gave information to Thomas Care about its former employee, however, court noted there was no allegation against Lifecare that it gave an employment-related evaluation and nor would the court extend the exclusion to Lifecare's non-employment or post-employment activities as described); *Adams v. Pro Sources, Inc. and North River Ins. Co.*, 231 F.Supp.2d 499 (M.D. La. 2002) (alleged defamation was made in the context and course of employee's employment sufficient to fall within employment related practices exclusion where statement concerned employee's performance as employee on last day of employment); *Berman v. Gen. Accident Ins. Co. of Am.*, 176 Misc.2d 13, 671 N.Y.S.2d 619, 622-23 (1998) (held that statements made about a former employee that assessed her performance and provided an explanation of why she was fired fell squarely within the employment-related practices exclusion for specified employment related practices such as evaluation and defamation); *Frank and Freedus v. Allstate Ins. Co.*, 45 Cal.App.4th 461, 52 Cal.Rptr.2d 678, 683-84 (Cal. Ct. App. 1996), (held that post-employment remarks made about an employee who was suing his former employer on wrongful termination, federal and state anti-discrimination, and state law defamation grounds were clearly "employment-related," and thus excluded under the employment practices exclusion); *HS Servs. v. Nationwide Mut. Ins. Co.*, 109 F.3d 642, 644 (9th Cir.1997) (held that the defamation was not "clearly

employment-related" because, although its content was directed to the employee's employment, the statements were not made in the context of employee's employment, but instead in the context of competition created between former employee and employer).

There are several Texas cases that have analyzed what activities are considered employment-related as to be excluded by this employment-related practices exclusion. *Travelers Indem. Co. of Connecticut v. Presbyterian Healthcare Resources*, 2004 WL 389090, *5 (N.D. Tex. 2004). In *Presbyterian Healthcare*, the court held that peer review activities are not employment related activities within the meaning of the exclusion in the insurance policy. The insured sought coverage for the claims of business disparagement, slander, and libel that are alleged to have occurred within the policy period in the underlying lawsuit. Travelers argued that the policy specifically excluded coverage for claims of business disparagement and defamation under the "Employment-Related Practices Exclusion," which was applicable to Personal and Advertising Injury Liability coverage. This exclusion stated that coverage does not apply to personal injury to a person arising out of any "employment-related practices, policies, acts, or omissions, such as coercion, demotion, evaluation, reassignment, discipline, defamation, harassment, humiliation, or discrimination directed at that person." The insured replied by arguing that the employment-related practices exclusion can only apply if the injured party is an employee. The court concluded that use of the word "person" in the exclusion provides for exclusion from coverage persons who applied for employment with the insured, but were not hired, as well as former employees who allege injury during employment related activities. Thus, the court ruled that the exclusion applies to persons who apply for employment with the insured, current employees, and former employees of the insured who allege defamation occurring during employment related practices.

In *Waffle House, Inc. v. Travelers Indem. Co. of Illinois*, 114 S.W.3d 601, 607-608 (Tex.App.-Fort Worth 2003, pet. denied) the Texas court interpreted another employment related exclusion in a Travelers' policy. In *Waffle House*, a former employee, Scribner, and her personnel recruiting company, Resources Recruiters, Inc., sued Waffle House, Inc., for defamation. The suit alleged that Waffle House defamed the employee by telling a competitor that she was discharged for poor performance, was vindictive, had tried to entice people to leave with her, and had a personal vendetta against Waffle House.

The exclusion in Travelers' policy provided that the policy "does not apply to ... 'personal injury' *arising out of* any ... termination of employment ... [c]oercion, demotion, evaluation, reassignment, discipline, defamation, harassment, humiliation, discrimination, or other employment-related practices, policies, acts or omissions." The court stated that the phrase "arise out of" in the employment-related acts exclusion required a "but for" causal relationship. Travelers argued that the allegations of post-employment defamation in the underlying complaint clearly arose out of employment-related acts and therefore there was no coverage under the policy. The court held that the defamatory statements were made over 2 years after the employee's termination to prevent Waffle House's competitor from acquiring Waffle House employees and were thus not causally related to Scribner's employment.

The court reviewed precedence finding that the terms "arise out of" requires a causal connection between the injury and the events excluded by the policy. The court reviewed the evidence and found that no causal connection existed between the defamatory statements made by Waffle House executives and the employee's injury. The statements made by the executives were lies intended to prevent the exodus of employees from Waffle House to Grandy's. Waffle House stated in its pleadings in the underlying suit that the purpose of the calls was "to inform Grandy's of the situation in an attempt to halt the apparent pirating of their employees." Travelers even conceded in its brief on page twenty-three that the "defamatory statements were made to Grandy's to avoid the loss of Waffle House employees." The court concluded that when statements such as these are coupled with the fact that the defamatory statements were made over two years after the employee's termination, the *context* of the statements clearly shows that they arose out of Waffle House's attempt to prevent its employees from leaving the company and not out of the employee's termination. In other words, no causal relationship existed between the defamation and the injured employee's employment. *Id.* at 608-09.

Waffle House addresses another issue that arises under the Employment-Related Practice Exclusion Endorsement, whether the exclusion applies to post-employment conduct. Several courts have addressed this issue throughout the nation. In *Frank and Freedus v. Allstate Ins. Co.*, 45 Cal.App.4th 461, 52 Cal.Rptr.2d 678, 683-84 (Cal.Ct.App.1996) a California state appeals court determined that post-employment remarks made about an employee who was suing his former employer on wrongful termination, federal and state anti-discrimination, and state law defamation grounds were clearly "employment-related," and thus

excluded under the employment practices exclusion. 52 Cal.Rptr.2d at 685. Crucial to this determination was the court's finding that the term "employment-related," was not ambiguous even though it was not specifically defined by the policy. *See id.* (stating that "[t]he term is not technical....[i]t is used in its ordinary sense, i.e., related to employment....[and] it modifies the specified acts (including defamation) [and its] clear meaning is coverage for... employment-related defamation."). Because the allegedly defamatory statement was made in the context of the former employee's employment and directed toward his performance during employment, the California court found the defamation "clearly employment related." *See id.*

In *Berman v. Gen. Accident Ins. Co. of Am.*, 176 Misc.2d 13, 671 N.Y.S.2d 619, 622-23 (1998) the New York Supreme Court of New York County mirrored the analysis of *Frank and Freedus* and determined that statements made about a former employee that assessed her performance and provided an explanation of why she was fired fell squarely within the employment-related practices exclusion for specified employment related practices such as evaluation and defamation. *See Berman*, 671 N.Y.S.2d at 623. Furthermore, the New York court refused to accept the argument that the exclusionary language in question should be read as limited to injuries sustained only while the employee is still employed by stating that such an argument is "semantically unreasonable and unacceptable." *Id.* (citing *Loyola Marymount Univ. v. Hartford Accident & Indem. Co.*, 219 Cal.App.3d 1217, 271 Cal.Rptr. 528, 531 (Cal.Ct.App.1990).

Texas courts have left open the possibility that the Employment-Related Practices Exclusion may not be applicable to post-employment conduct. In *Acceptance Ins. Co. v. Lifecare Corp.*, 89 S.W.3d 773, 784-85 (Tex. App.—Corpus Christi 2002, pet. denied) the policy at issue contained an employment-related practices exclusion that read in pertinent part:

1. The following exclusion is added to COVERAGE A (Section I):
 - o. 'Bodily injury' arising out of any:
 - (1) Refusal to employ;
 - (2) Termination of employment;
 - (3) Coercion, demotion, evaluation, reassignment, discipline, defamation, harassment, humiliation, discrimination, or other employment-related practices, policies, acts or omissions; or
 - (4) Consequential 'bodily injury' as a result of (1) through (3) above. This exclusion applies whether the insured

may be held liable as an employer or in any other capacity and to any obligation to share damages with or to repay someone else who must pay damages because of injury.

The claim was that the insured, Lifecare, negligently gave information to Thomas Care about its former employee. The carrier argued that Lifecare was providing an evaluation and the employment related exclusion operated because the insured may not be held liable as an employer or in any other capacity, specifically centering their argument on subsection (3) "evaluation ... or any other employment related practices, policies, acts or omissions." *Id.* at 784-85. However, the court noted there was no allegation against Lifecare that it gave an employment-related evaluation and nor would the court extend the exclusion to Lifecare's non-employment or post-employment activities as described. Therefore, the court concluded that the employment-related exclusion was not applicable to the controlling factual allegations. *Id.* at 786. However, note that the court reasoned as follows:

When the employment ended, the activity is less likely to be employment related except perhaps in some defamation or termination circumstances as illustrated by *Frank & Freedus*. See *Frank & Freedus*, 45 Cal.App.4th at 471, 52 Cal.Rptr.2d 678. Here there is no factual allegation of coercion, demotion, evaluation, discrimination "or other employment related practices, policies, acts or omissions." The only factual allegation is in the nature of a negligent representation. It was claimed Lifecare gave the wrong information about a former employee. While an evaluation may be a negligent representation, a negligent representation is not necessarily an evaluation. *Id.* at 787.

Therefore, the Texas court left open the possibility that the Employment-Related Practices Exclusion may not be applicable to post-employment conduct, especially in circumstances involving defamation.

Like the employer's liability exclusion, the employment-related practices exclusion standard form also applies whether the insured is liable as an employer or in any other capacity. As previously discussed, the phrase "in any other capacity" is intended to encompass claims or suits against employers under the so-called dual capacity doctrine.

Under the dual capacity doctrine, an employer may be liable to the employee for additional damages in tort. Under the CGL form 2147 0798 the exclusion applies "whether the insured may be liable as an employer or in any other capacity" and applies "to any obligation to share damages with or repay someone else who must pay damages because of injury." Texas-Changes Employment-Related Practices Exclusion form CG 2639 0499 does not, however, contain this limiting language. If this Texas endorsement applies, an employer may not be liable under a dual capacity.

Additional insurance coverage may be available for employee claims under Workers' Compensation/Employer's Liability Insurance.

II. Workers' Compensation/Employer's Liability Insurance

Workers' Compensation laws require employers to pay the medical expenses, lost wages and other expenses such as rehabilitation incurred by employees who are injured while on the job. Employers generally provide these payments by purchasing worker's compensation insurance for their employees. Employer's Liability is an additional coverage provided in a workers' compensation policy. Part One of the standard Workers' Compensation and Employer's Liability policy applies to claims for benefits made under state workers' compensation statutes. It does not apply to an employee's claim for damages in a civil suit. See, e.g., *La Jolla Beach & Tennis Club v. Industrial Indemnity Co.*, 884 P.2d 1048 (Cal. 1994).

A. Part Two: Employer's Liability

Part Two of the policy provides coverage for claims of "bodily injury by accident or bodily injury by disease." A carrier may use the same arguments to deny coverage under a CGL policy to deny coverage under the Employer's Liability Insurance, such as whether there was an occurrence which caused bodily injury. Ed E. Duncan, *Insurance Coverage For Sexual Harassment in the Workplace*, 51 No. 2 PRACTICAL

LAWYER 51, 55 (2005). Part Two responds in the event that an employee or his/her family sues for payments in addition to those provided under workers compensation laws. If an injured worker's family members can prove that the business owner is legally liable for a work-related injury or illness, they may be able to collect damages.

Many states, including Texas, have a statutory scheme of workers compensation that protects employers, if they are subscribers, from liability to their employees for injuries incurred in the course and scope of employment. The Texas Department of Insurance (TDI) regulates workers' compensation in Texas. TDI's Division of Workers' Compensation administers the claims process, handles Workers' Compensation disputes, and provides workplace safety services and enforcement. *See Workers' Compensation Insurance*, Texas Department of Insurance, <http://www.tdi.state.tx.us/consumer/cb030.html> (last visited June 24, 2006). There are circumstances in which the employers are not protected by the workers' compensation policies such as death of an employee caused by the gross neglect of the employer. TEX. LABOR CODE ANN. § 408.001 (b) (Vernon 2000) (statute does not prohibit recovery by heirs for death caused by intentional act or gross negligence of employer). In that case, the heirs and survivors of the deceased employee can sue the employer for punitive damages.

Also, employers are increasingly confronted with third-party actions, where the injured employee sues a negligent third party who in turn, sues the employer for contributory negligence. Workers' compensation insurance is not responsive to these types of claims. However, employer's liability insurance is designed to protect the employer/insured against liability imposed by law for injury to employees in the course of employment that is not compensable under the workers compensation laws. D. Thamann, J.D., CPCU, ARM and D. Reitz, CPCU, ARM, *Workers Compensation*, 2000, pg. 15-16.

The main coverage form in most WC/EL policies include an insuring agreement that reads as follows:

**PART TWO: EMPLOYER'S
LIABILITY INSURANCE**

A. How This Insurance Applies

This employers' liability insurance applies to bodily injury by accident or bodily injury by disease. Bodily injury includes resulting death.

1. The bodily injury must arise out of and in the course of the injured employee's employment by you.
2. The employment must be necessary or incidental to your work in a state or territory listed in Item 3.A. of the Information Page.
3. Bodily injury by accident must occur during the policy period.
4. Bodily injury by disease must be caused or aggravated by the conditions of your employment. The employee's last day of last exposure to the conditions causing or aggravating such bodily injury by disease must occur during the policy period.
5. If you are sued, the original suit and any related legal actions for damages for bodily injury by accident or by disease must be brought in the United States of America, its territories or possessions, or Canada.

B. We Will Pay

We will pay all sums you legally must pay as damages because of bodily injury to your employees, provided the bodily injury is covered by this Employers' Liability insurance.

The damages we will pay, where recovery is permitted by law, include damages:

for which you are liable to a third party by reason of a claim or suit against you by that third party to recover the damages claimed against such third party as a result of injury to your employee;

for care and loss of services; and

for consequential bodily injury to a spouse, child, parent, brother or sister of the injured employee;

provided that these damages are the direct consequence of bodily injury that arises out of and in the course of the injured employee's employment by you; and

because of bodily injury to your employee that arises out of and in the course of employment, claimed against you in a capacity other than as employer.

* * *

C. We Will Defend

We have the right and duty to defend, at our expense, any claim, proceeding or suit against you for damages payable by this insurance. We have the right to investigate and settle these claims, proceedings and suits.

We have no duty to defend a claim, proceeding or suit that is not covered by this insurance.

There are several prerequisites to coverage under the employers' liability insurance. First, the bodily injury must occur to the insured's employee and in the course of the employee's employment. Second, the employment must be necessary or incidental to the insured's work in Texas. Third, the bodily injury by disease must be caused or aggravated by the conditions of employment. Fourth, the employee's last day of exposure to the conditions causing the bodily injury by disease must occur during the policy period.

Section 4 of the "How This Insurance Applies" provisions requires the following to trigger coverage under the Employers' Liability Insurance:

4. Bodily injury by disease must be caused or aggravated by the conditions of your employment. The employee's last day of last exposure to the conditions causing or aggravating such bodily injury by disease must occur during the policy period.

This condition is considered the actual trigger of coverage under the employers' liability coverage with respect to bodily injury by disease claims. *See International Business Machines Corp. v. Liberty Mutual Fire Insurance Co.*, 363 F.3d 137, 146 (2nd Cir. 2004) ("The trigger of coverage as to each claim is each claimant's "last day of last exposure" to those carcinogens while employed at IBM, which is the last day of employment in IBM's California cleanroom facility.").

Under Part Two, an insurer's duty to defend is determined in the same manner as other insurance policies, using the "eight corners rule," which limits the court's review to the four corners of the insurance policy and the four corners of the plaintiff's petition. *See National Union Fire Ins. Co. v. Merchants Fast Motor Lines, Inc.*, 939 S.W.2d 139, 141 (Tex. 1997); *Houston Petroleum Co. v. Highlands Ins. Co.*, 830 S.W.2d 153, 155 (Tex. App.—Houston [1st Dist.] 1990, writ denied). The duty to defend is not affected by facts learned before, during, or after the suit. *Tri-Coastal Contractors, Inc. v. Hartford Underwriters Insurance, Co.*, 981 S.W.2d 861, 863 (Tex. App.—Houston [1st Dist.] 1998, pet. denied).

In *Tri-Coastal Contractors*, Hartford issued an insurance policy that provided Tri-Coastal two types of coverage. *Id.* at 862. Part One provided workers' compensation insurance and Part Two provided employer's liability insurance. *Id.* At issue was whether Hartford had a duty to defend Tri-Coastal in a suit filed by Antwine, its employee, because the employee already received workers' compensation

benefits. The court held that the issue of whether Antwine collected workers' compensation benefits goes to the merits of his lawsuit because he could not sue Tri-Coastal for negligence if he collected workers' compensation benefits for the same injury. *Id.* at 864. The court then stated that Antwine's acceptance of worker's compensation benefits barred him from collecting from Tri-Coastal for negligence or gross negligence and was an absolute defense for Tri-Coastal against Antwine's suit. The court concluded that Tri-Coastal was required to defend itself against the employee's suit regardless if the suit was meritorious. Finally, the court noted that Tri-Coastal purchased insurance from Hartford to cover both the cost of defending a suit and the cost of paying a claim if it was found liable.

In *Vandewater v. American General Fire & Casualty Co.*, 910 S.W.2d 614 (Tex. App.—Austin 1995, reh'g overruled) an employee contracted a virus while employed by Vandewater Construction Company. *Id.* at 615. Because the employee was pregnant at the time, her son Jordan contracted the virus and was born mentally retarded. In effect at the time was a "Workers Compensation and Employers Liability Insurance Policy" issued by American General to Vandewater Construction Company. The employee's claim for bodily injury came within the Workers Compensation part of the policy. Jordan's claim comes within Part Two of the policy, entitled "Employers Liability Insurance." *Id.*

The parties stipulated that the mother contracted the virus in the course and scope of her employment by Vandewater Construction Company and that Jordan was never an employee of that company. *Id.* It was undisputed that Jordan's mental retardation was a "consequential bodily injury to a . . . child . . . of the injured employee." *Id.*

The policy stated as follows:

Section "G" of Part Two provides as follows: Our liability to pay for damages is limited. Our limits of liability are shown in item 3.B. of the Information Page. They apply as explained below.

2. Bodily Injury by Disease. The limit shown for "bodily injury by disease-policy limit" is the most we will pay for any damages covered by this insurance and arising out of bodily injury by disease, *regardless of the number of employees* who sustain bodily injury by disease. The limit shown for "bodily injury by disease-each employee" is the most we will pay for any

damages because of bodily injury by disease *to any one employee.*

Id.

The Austin Court of Appeals held that the policy “unambiguously places a \$100,000 limit on one employee’s claim for bodily injury by disease; and under the express terms of section B.3 this limit applies to a *consequential* bodily injury sustained by an injured employee’s child, such as Jordan.” *Id.* at 616.

The Second Circuit in *International Business Machines Corp. v. Liberty Mutual Fire Insurance Co.*, 303 F.3d 419 (2d Cir. 2002), an insured and its worker’s compensation and employers liability policy insurer disputed whether the insurer had a duty to defend its insured. IBM employees and their children brought suit against IBM alleging they were injured as a result of exposure to chemicals while working at IBM facilities. *Id.* at 421. The children’s claims allege they sustained bodily injury as a result of their parents’ workplace exposure to chemicals both prior to conception and during gestation. *Id.*

Liberty Mutual issued a Workers Compensation and Employers Liability Insurance policy to IBM. *Id.* The relevant portions of the policy stated as follows:

[Liberty Mutual] will pay all sums [IBM] legally must pay as damages because of bodily injury to [IBM’s] employees, provided the bodily injury is covered by this Employer’s Liability Insurance. The damages [Liberty Mutual] will pay, where recovery is permitted by law, include damages:

* * *

3. for consequential bodily injury to a spouse, child, parent, brother or sister of the injured employee ... provided that these damages are the direct consequence of bodily injury that arises out of and in the course of the injured employee’s employment by [IBM]

Id. New York determines an insurer’s duty to defend from the complaint and the policy language. *Id.* at 424.

Liberty Mutual denied any duty to defend stating as follows:

the Infant Plaintiffs’ alleged damages do not arise from “bodily injury to [IBM’s] employees,” are not “the direct consequences of bodily injury that arises out of and in the course of the injured employee’s employment by [IBM]” . . . Moreover, the Infant Plaintiffs’ alleged damages do not arise

from “bodily injury by accident or disease . . . by any employee of the injured.”

Id. at 422.

Liberty Mutual’s policy covers any “consequential bodily injury to a . . . child . . . of the injured employee . . . provided that these damages are the direct consequence of bodily injury that arises out of and in the course of the injured employee’s employment by [IBM].” *Id.* at 424. The court held that the complaint alleges at least the “reasonable possibility” or “potential” that at the conclusion of the *Ruffing* litigation it could be found that: (1) Zachary’s parents were employed by IBM; (2) one or both of his parents suffered bodily injury as a result of workplace exposure to chemicals; and (3) Zachary suffered bodily injury as a result of his parents’ injury. The court then concluded that Liberty Mutual had a duty to defend the action. *Id.*

B. Employer’s Liability Insurance Exclusions

C. Exclusions

This insurance does not cover: liability assumed under a contract. This exclusion does not apply to a warranty that your work will be done in a workmanlike manner;

* * *

5. bodily injury intentionally caused or aggravated by you;

* * *

8. bodily injury to any person in work subject to the Longshore and Harbor Workers’ Compensation Act (33 USC Sections 901-950), the Nonappropriated Fund Instrumentalities Act (5 USC Sections 8171-8173), the Outer Continental Shelf Lands Act (43 USC Sections 1331-1356), the Defense Base Act (42 USC Sections 1651-1654), the Federal Coal Mine Health and Safety Act of 1969 (30 USC Sections 901-942), any other federal workers’ or workmen’s compensation law or other federal occupational disease law, or any amendments to these laws;

* * *

11. fines or penalties imposed for violation of federal or state law;

Under exclusion (1), liability insurance usually excludes “liability assumed under a contract.” *See Gibson & Assoc., Inc. v. Home Ins. Co.*, 966 F.Supp. 468 (N.D.Tex. 1997). However, most liability policies make exception to this exclusion for the assumption of tort liability of a third party in a contract, also known as an “insured contract.” *Id.* This exception is not in the employers’ liability coverage.

Under exclusion (5), whether the insured intended harm or injury to result from an intentional act within the meaning of this policy exclusion is a question of fact for the factfinder. *See State Farm Fire & Casualty Company v. S.S. & G.W.*, 858 S.W.2d 374, 378 (Tex. 1993). Under the definition of intent stated in the RESTATEMENT (SECOND) OF TORTS, an insured intends to harm another if he intends the consequences of his act, or believes that they are substantially certain to follow. *Id.* (citing RESTATEMENT (SECOND) OF TORTS § 8A (1965)).

An employer's liability insurance policy specifically excludes coverage for bodily injury intentionally caused by the insured. In *Butler & Binion v. Hartford Lloyd's Insurance Co.*, 957 S.W.2d 566 (Tex. App.—Houston [14th Dist.] 1995, writ denied), an expelled partner sued its law firm and recovered for breach of the partnership agreement, in a judgment rendered by the Houston Court of Appeals, 905 S.W.2d 597. The firm's liability insurers refused to indemnify it under the commercial general liability or workers' compensation/employer's liability policies, and the insured firm sued the insurers for breach of contract and bad faith. The claims of the expelled partner against the law firm for breach of contract and of fiduciary duty were allegations of intentional conduct, and were barred from coverage under the workers' compensation/employer's liability policy provision for bodily injury by accident or disease and under exclusion for injury intentionally caused by insured. 957 S.W.2d at 569.

The court noted that unlike workers compensation insurance, however, employer's liability insurance specifically excludes coverage for bodily injury intentionally caused by the insured. *Id.* The petition did not mention accidental conduct or disease related damages, but only asserted exclusively intentional conduct which precluded coverage under both the workers compensation and employer's liability policies. *Id.* The Houston Court of Appeals held that there were no factual allegations in the petition showing the insurers' potential liability under any provision of either the commercial general liability policy or the workers compensation/employer's liability insurance. *Id.* at 570. Therefore, the insurers owed no duty to defend the law firm on this basis in the lawsuit filed by Bohatch. *Id.*

Employers' liability exclusions (8) and (11) become applicable where there is bodily injury caused by violations of federal workers' or workmen's compensation law or federal occupational disease laws

or penalties assessed for violations of federal or state law.

Employer's liability insurance provides coverage to companies in the event that an employee alleges that the employer's negligence or failure to provide a safe workplace was the cause of the employee's injury or illness. If there is no coverage under a CGL policy or worker's compensation/employer's liability policy, the insurance market has created additional policies to address employment-related claims such as employment practices liability insurance.

III. Employment Practices Liability Insurance

Employment Practices Liability (EPL) insurance came into existence in the early 1980s with coverage for defense costs for various employment-related claims. *See Duncan, supra*, at 57. Then, in the 1990s, EPL policies began providing coverage for defense and indemnity and were designed solely for wrongful termination claims. *Id.* Then as more insurers began entering the market coverage was expanded to provide protection for claims for employment law judgments, bonds, post-judgment interest, and back pay. *Id.* Today, coverage under an EPL is specifically written to insure employers against claims for wrongful termination, discrimination, harassment, defamation, negligent hiring, and punitive damages (as permitted by state law). *Id.* Many of the policies also provide coverage for discrimination and harassment made against employers by third parties, including vendors and customers of employers. *Id.* at 58. Under the ISO policy, however, there is no coverage for claims by third parties. *Id.* at 62. Depending on the policy definition of "employees", independent contractors, leased workers, and temporary workers may not qualify as "employees." *Id.* at 61. These individuals may not be considered insureds for the same reasons, but endorsements are available to broaden the definition of employee. *Id.*

Typically, EPL policies exclude claims based on, arising from, or in any way related to the Fair Labor Standards Acts, the National Labor Relations Act, the Worker Adjustment and Retraining Notification Act (WARN), and claims arising out of downsizing, layoffs, workforce restructurings, plant closures or strikes; the Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA); the Employee Retirement Income Security Act (ERISA); the Occupational Safety and Health Act (OSHA); and the costs associated with providing "reasonable accommodation" under the Americans with Disabilities Act (ADA) to disabled employees or costs associated

with modifying facilities to make them accessible to the disabled.

A. Employment Practices Liability v. Commercial General Liability

EPL policies differ from CGL policies in many aspects. There is not a standard EPL form in existence like those for CGL policies. EPL policies insure against liability arising from employment practices, while CGL policies provide only general liability coverage, insuring against claims for bodily injury and property damage (i.e., tangible damages). Additionally, CGL policies exclude coverage for intentional acts, which are commonly claimed in employment suits, and bodily injury to employees arising out of and in the course of employment or out of performing duties related to an employer's business. Also, while CGL policies cover occurrences that cause damage during the period of coverage, EPL policies only cover claims that an employer knew about or should have known about and that the employer reported to the insurer during the coverage period. EPL policies are written on a claims-made basis and typically have defense costs included within policy limits. James B. Dolan, Jr., *The Growing Significance of Employment Related Practices Liability Insurance*, 73 DEF. COUNS. J. 197, 197 (2006).

B. Coverage Under Employment Practices Liability

Most EPL policies provide a duty to defend to the insured. The carrier's duty to defend typically arises regardless of whether the deductible, or amount of the employer's out-of-pocket expenses, has been met. Additionally, the insurer retains the right to choose the counsel who will defend the insured. EPL policies also may be written with no duty to defend, unlike a CGL policy. Under an EPL policy with no duty to defend, the employer must manage its own defense and retain counsel. The insured will then be required to reimburse the insured for the cost of the defense and any settlement or judgments.

Under an EPL policy, a "claim" includes administrative charges filed against the insured by the EEOC or a comparable state agency. The insured should report the claim in a timely manner to the carrier whose policy is in effect when the claim is made. See Duncan, *supra*, at 58. If an insured waits until a suit is filed the reporting period may have expired and there may be no coverage for either the administrative charge or suit. See *Pantropic Power Products v. Fireman's Fund Insurance Co.*, 141 F.

Supp. 2d 1366, 1371-72 (S.D. Fla. 2001), *aff'd* without op., 34 Fed. Appx. 968 (11th Cir. 2002).

In *Woo v. Fireman's Fund Insurance Co.*, 114 P.3d 681 (Wash. Ct. App. 2005), an insured dentist filed suit against its insurer when the insurer declined to defend the insured against an underlying tort action by a former employee who had been subjected to a humiliating practical joke while she was under anesthesia. *Id.* at 683. Dr. Woo sued Fireman's Fund alleging bad faith breach of duty to defend. *Id.* The insurance dispute arose from a lawsuit filed by surgical assistant Tina Alberts against her former employer, oral surgeon Dr. Woo. *Id.* at 682. According to her complaint, during the five years of her employment, Dr. Woo learned of her interest in pot-bellied pigs and her pet pig, Walter. *Id.* He began to make offensive comments to her about pigs and then showed her pictures of his boar hunting trip and a skinned pig hanging on a hook and made comments like, "[T]here is how Walter will look." *Id.* During the last six months of her employment, Alberts began to complain about Dr. Woo's treatment of staff and to demand overtime pay. *Id.*

When Alberts chipped a baby tooth that had never been replaced by a permanent tooth, Dr. Woo agreed to remove the chipped tooth and another tooth for her. *Id.* at 683. According to usual procedure, a co-worker took an impression of Alberts' teeth and temporary false teeth known as "flippers" were created for Alberts to wear until the teeth were replaced by permanent implants. *Id.* But Dr. Woo ordered additional flippers designed in the shape of boar tusks. *Id.* The patient alleged that Dr. Woo ordered temporary teeth shaped like boar tusks, placed them in patient's mouth, took pictures, and then told the patient that the tusks and pictures were "a trophy to take home." *Id.*

In construing the employment practices liability coverage, the court had to determine whether these allegations constituted a "wrongful discharge" arising out of "wrongful employment practice", despite fact that employee left office after procedure and never returned. *Id.* at 686-87.

The employment practices liability portion of the policy issued to Dr. Woo provided coverage for "damages as a result of sexual harassment, discrimination, or wrongful discharge that arise out of a wrongful employment practice." *Id.* at 683-84. The policy defined "wrongful discharge" as:

the unfair or unjust termination of an employment relationship which: breaches an implied agreement to continue employment;

or inflicts emotional distress upon the employee, defames the employee, invades the employee's privacy, or is the result of fraud.

Id. at 684. The policy defined "wrongful employment practice" as:

any negligent act, error, omission or breach of duty committed in the course of: relations with employees; interviewing, hiring or refusing to hire anyone who applies for employment; or decisions to hire, promote, discipline or fire employees.

Id.

Dr. Woo alleged that his patient's complaint includes a claim for constructive discharge which would be covered by the "wrongful discharge" portion of the EPL policy. *Id.* at 686. The court held that although the patient's complaint alleged that she left the office and never returned, the alleged cause of the injuries was the practical joke. *Id.* "It does not allege any facts which would conceivably constitute the tort of wrongful discharge recognized in our statutes or case law. There is no wrongful termination tort based on **boorish** behavior by one's employer, unless such behavior violates an employment contract, discrimination statutes, the constitution, or public policy." *Id.* (emphasis added). The court held that no cause of action had been plead triggering coverage under the EPL portion of the policy. *Id.* at 687.

C. Employment Practices Liability Issues

Claims-made coverage could create an issue for an employer regarding (1) wrongful acts which take place before the policy begins but result in a claim during the policy period and (2) wrongful acts that take place during the policy period but result in a claim after the policy ends. *See Duncan, supra*, at 58. For wrongful acts taking place before the policy period begins, an employer should obtain prior acts coverage. *Id.* The wrongful acts will be covered as long as the claim is made during the policy period and reported in accordance with the policy terms. *Id.* For wrongful acts taking place during the policy period, but reported after the end of the policy, an employer should obtain an extended reporting period.

Coverage disputes arise over coverage for "known losses." For example, in *Service Casualty Insurance Co. v. Travelers Insurance Co.*, 2004 WL 2218381 (W.D. Tex. 2004) (unpublished opinion), a dispute arose whether there was coverage under the

Employment Practices Liability Plus policy, and if so, whether the CGL insurer could recover any monies under the theory of equitable subrogation for the settlement reached with the claimant. *Id.* at *4.

Christina Shakoor was employed by Gillespie Motor from 1994 until she was terminated or "constructively discharged" on March 31, 2001. *Id.* at *1. Gillespie Motor was insured by Service Casualty under a CGL "occurrence basis" policy from February 1, 1999 through March 15, 2001. Travelers issued a "claims made" Employment Practices Liability Plus Policy to Gillespie Motor effective March 15, 2001 through March 15, 2002. *Id.*

Travelers retained counsel to defend Gillespie Motor and defended the claim for approximately two years. *Id.* On the eve of trial, Gillespie Motor demanded that one or both of the insurance carriers settle the Shakoor suit. *Id.* The Shakoor suit was settled for \$125,000 by Service Casualty. *Id.*

Travelers relied on exclusion III.C. Which states as follows:

This insurance shall not apply to, and the Company shall have no duty to defend or pay Defense Expenses for any Claim:

* * *

For or arising out of facts, transactions or events which are or reasonably would be regarded as Wrongful Employment Practices, about which any Responsible Person had knowledge prior to the inception of coverage under the Policy....

Id. at *4. The policy became effective March 15, 2001. The parties do not dispute that "retaliation and discrimination against an employee, because that employee previously filed a worker's compensation claim is a Wrongful Employment Practice." *Id.*

The court determined that the issue was "whether prior to March 15, 2001, Bonugli was aware of 'facts, transactions or events which are or reasonably would be regarded as Wrongful Employment Practices.'" *Id.* Travelers argues that there were facts, transactions or events constituting "discriminatory and retaliatory conduct" occurring prior to March 15, 2001. *Id.* at *5.

Travelers argues that coverage is precluded when Gillespie Motor was aware of a "known loss" or "progressive loss" from "facts, transactions or events which are or reasonably would be regarded as Wrongful Employment Practices." *Id.* Under the fortuity doctrine:

the purpose of insurance is to protect insureds against unknown, or fortuitous, risks, fortuity is an inherent requirement of all risk insurance policies. The fortuity doctrine precludes coverage for both a 'known loss' or a 'loss in progress.' A 'known loss' is a loss the insured knew had occurred prior to making the insurance contract. A 'loss in progress' occurs when the insured is, or should be, aware of an ongoing progressive loss at the time the policy is purchased. Insurance coverage is precluded where the insured is or should be aware of an ongoing progressive or known loss at the time the policy is purchased.

Id. (quoting *Scottsdale Ins. Co. v. Travis*, 68 S.W.3d 72 (Tex. App.—Dallas 2001, pet. denied)).

The court in *Service Casualty* held that the allegations of the Shakoor petition specifically outline “facts, transactions or events which are or reasonably would be regarded as Wrongful Employment Practices” that took place prior to March 15, 2001. *Id.* at *6. Therefore, coverage for the Shakoor litigation was excluded by paragraph III.C. and the fortuity doctrine. *Id.*

Additionally, EPL policies typically contain a “consent to settle” provision. The provision states that the “insurer has a right to settle a claim in any manner it deems proper, but the company will not settle any claim without the insured’s consent.” *See Duncan, supra*, at 60. A consent to settle clause may be modified by a “hammer clause.” A hammer clause states that “if the insured refuses to consent to a settlement recommended by the company, the company’s liability shall not exceed the amount for which the claim could have been settled but for the insured’s refusal.” *Id.* Additionally, some policies contain a “soft hammer” clause. These clauses require that the insured and insurer share any costs exceeding the amount for which the case could have been settled but for the insured’s refusal. “This clause is a recognition by insurers that at times it is in the mutual interest of the insurer and insured to continue to litigate a case which could have been settled at a favorable costs and that they should both share the risk of an unfavorable outcome.” *Id.*

The EPL policy may contain a contractual liability exclusion. For example, this would exclude coverage to a “subcontractor who has agreed to hold a general contractor harmless because of sexual harassment on the part of a subcontractor’s employee, unless the subcontractor would have been liable for such acts in the absence of the hold harmless agreement.” *Id.* at 62.

Under the ISO form, “employee” includes “leased workers” and “temporary workers” but not independent contractors or job applicants. *Id.*

Potential areas for coverage disputes relating to an EPL policy include the insurability of intentional acts, determining what a claim is, and an awareness exclusion. *See Dolan, supra*, at 198. Typically, discrimination is considered an intentional act and generally liability insurance does not apply to damages that are expected or intended from the point of view of the insured. However, if an insured is held vicariously liable for an employee’s wrongful acts, coverage exists for the named insured, but no coverage exists for the wrongdoer-employee.

As discussed previously, what constitutes a claim can impact coverage for an insured under the EPL. Claims are typically written, or oral, demands for money damages. The definition of “claim” dictates whether a policy will cover possible future claims. Coverage may be affected by a response of the insured to a question in the application for EPL coverage regarding the awareness of circumstances that could reasonably be expected to result in a claim; or affect coverage because of an awareness provision on claims made during a policy period when based on acts occurring prior to inception of the policy coverage; or policy language requiring notice to the insurer of a circumstance which may give rise to a possible future claim. *See Dolan, supra*, at 198. If there is a failure of an insured to make a full disclosure in the policy application, an insurer may cancel the resulting policy for fraud in the application. A carrier has the burden to prove there was fraud on the part of the insured. Awareness provisions may “preclude coverage even if the application did not contain questions about probable claims.” *Id.* The burden of proof for the awareness exclusion is on the carrier.

One additional insurance coverage available for employers to protect against employment claims or lawsuits is Employee Benefits Liability insurance.

IV. Employee Benefits Liability Coverage

Consider the following scenario:

A pastor dies unexpectedly. He leaves behind a loving family including his second wife and two small children. He has a child from a previous marriage as well. He modified his life insurance when he remarried making his new wife the beneficiary of his life insurance policy - a benefit provided by his local Church. There is one small problem. The

beneficiary change form never got mailed into the insurance carrier! A small but important administrative oversight in a busy Church office. The death benefit was paid to the ex-wife, leaving the Pastor's new family without financial means.

Employee Benefits Liability Coverage, <http://www.cciwdisciples.org/Insurance/liability%20ins.htm> (last visited June 27, 2006). This situation illustrates what could be a typical claim by an employee against its employer. If the employer has Employee Benefits Coverage, the employer may be entitled to a defense and indemnification depending on the particular terms of the policy and allegations asserted against the employer for claims such as this.

In 2001, the ISO introduced the Employee Benefits Liability Coverage Endorsement (EBL). This was a response to the landmark case of *Gediman v. Anheuser Busch*, 193 F. Supp. 72 (E.D.N.Y. 1961). In *Gediman*, an employer was held accountable to the estate of a former employee for providing incorrect information. The ISO endorsement is a claims-made policy and "applies to the negligent acts, errors or omissions committed by insureds in the administration of the named insured's employee benefit program, defined to encompass group life insurance, group accident and health programs, profit-sharing plans pension plans, unemployment insurance, workers compensation, disability benefits insurance, and kindred plans." Donald S. Malecki & Arthur L. Flitner, COMMERCIAL GENERAL LIABILITY COVERAGE GUIDE 165 (8th ed.). The EBL endorsement does not apply to fiduciary liability plans within the scope of Employee Retirement Income Security Act of 1974 (ERISA). *Id.* (see Exclusion (g) of the EBL endorsement).

The EBL coverage insures the employer against claims by employees or former employees resulting from negligent acts or omissions in the administration of the insured's employee benefits program. A typical EBL endorsement states, in relevant part, as follows:

"We will pay those sums that the insured becomes legally obligated to pay as damages because of loss sustained by any of your employees or former employees, or by the estate, heirs, legal representatives, beneficiaries or assigns of such person, arising out of any act, error or omission that occurs in the 'Administration' of your 'Employee Benefits Program.' We will have the right and duty to defend any 'suit' against you seeking those damages, even if any of the allegations of the 'suit' are groundless, false or fraudulent."

Musmeci v. Schwegmann Giant Super Markets, Inc., analyzed how an employer's self-insured retention in its excess GL policy with Excess Employee Benefits Coverage would define the term "claim". 332 F.3d 339, 352 (5th Cir. 2003) (construing Louisiana law). Under Louisiana law, the self-insured retention (SIR) provision reading "\$250,000 each claim" in the employer's excess general liability insurance policy, although containing no definition of "claim," referred claims made against the insured rather than the insured's demand for coverage. *See id.* The Fifth Circuit analyzed the Excess Employee Benefits Liability coverage to determine how "claim" is defined and referred to in the EBL policy. The EBL refers to claims made "against the insured" or claims "by the employee." *Id.* Therefore, the SIR applied to each retiree's claim, in the retirees' class action challenging the insured's termination of an employee benefit plan and seeking coverage from the insurer under the policy's excess employee benefits coverage provisions, rather than to retirees' claims collectively. *Id.* at 355.

The typical EBL policy defines "Administration" as follows:

G. For the purposes of the coverage provided by the endorsement, the following definitions are added to the **Definitions** Section:

1. "Administration" means:

- a. Providing information to "employees," including their dependents and beneficiaries, with respect to eligibility for or scope of "employee benefit programs"
 - b. Handling records in connection with the "employee benefit program";
 - c. Effecting, continuing or terminating any "employee's" participation in any benefit included in the "employee benefit program."
- However, "administration" does not include handling payroll deductions.

Additionally, the term "Employee Benefits Program" is defined as:

"any of the following employee benefit plans and programs maintained for the benefit of your employees or former employees:

"(1) Group life insurance, group accident and health insurance, employee pension plans, employee stock subscription plans, profit sharing plans, workers compensation, unemployment compensation, social security and disability benefits insurance"

Therefore, generally speaking, an employee benefits liability endorsement may provide coverage to policyholders only if there was a negligent act, error, or omission in the administration of an employee benefits program.

The following is an excerpt from an article published in *Mealey's Emerging Insurance Disputes* on October 4, 2005 written by William M. Savino and Stephen J. Smirti, Jr. discussing the "administration" requirement for coverage under an Employee Benefits Liability policy.

In *Maryland Cas. Co. v. Economy Bookbinding Corp. Pension Plan Trust*, 621 F. Supp. 410 (D.N.J. 1985), an insurer sought a declaratory judgment that it did not have a duty to defend or indemnify its insureds for acts giving rise to an underlying suit alleging that the insureds had violated their fiduciary and statutory duties to the employee pension plan. In part, the underlying action alleged that the trustees had violated their fiduciary duties and ERISA by investing too large a percentage of pension plan funds in the company's own securities. The court determined that the employee benefit liability endorsement limited coverage to liability incurred in relatively routine, ministerial acts, and excluded from coverage actions taken in "the decision-making and monitoring involved in managing the Plan's investments."

In reviewing each claim to determine whether the alleged acts fell within the administration of the pension plan, the court noted that miscalculation of the percentage of funds invested in the company's own securities may have fallen under the policy's definition of "Administration." However, the court determined that the underlying plaintiffs were complaining of "the investment itself," which did not fall within the policy's definition of "Administration."

In *Darby Lumber, Inc. v. Indiana Lumbermens Mutual Ins. Co.*, 30 Mont. F.Rpts. 219 (D. Mont. Aug. 28, 2002), the case involved an employee stock ownership plan ("ESOP") created by Darby Lumber, Inc. To implement the ESOP, an Employee Stock Ownership Trust (the "Trust") purchased 565,217 of the one million outstanding shares of Darby Lumber stock for \$6.5 million. At the time the ESOP and the Trust were created, Robert and Peggy Russell were executive officers, directors,

stockholders, and employees of Darby Lumber.

Several years later, employee participants in the ESOP filed suit against Darby Lumber, the Russells, and others alleging that the defendants had violated ERISA by overvaluing the stock sold to the Trust, causing the Trust to pay too much for its 565,217 shares.

Darby Lumber tendered the complaint to Indiana Lumbermens Mutual Insurance Company, which had provided Darby Lumber with a general commercial liability insurance policy that included an employee benefit liability endorsement in the aggregate amount of \$1 million. The endorsement covered "any negligent act, error or omission of the 'Insured' or of any other person for whose acts, errors or omissions the 'Insured' is legally liable, in the administration of the 'Insured's Employee Benefit Programs." The coverage extended to Darby Lumber, its executive officers, directors, stockholders, and employees. The coverage also extended to "profit sharing plans, pension plans [and] employee stock subscription plans."

Indiana Lumbermens disclaimed coverage, asserting that the allegations in the underlying complaint did not fall within the coverage of the policies. Darby Lumber then filed suit seeking a declaratory judgment that the policy covered the acts alleged.

Darby Lumber relied on the endorsement's definition of "Administration" as:

- "(1) Giving counsel to 'Employees' with respect to the 'Employee Benefit Program';
- "(2) Interpreting the 'Employee Benefit Programs' for employees;
- "(3) The handling of records in connection with the 'Employee Benefit Programs';
- "(4) Effecting enrollment, termination or cancellation of 'Employees' under the 'Employee Benefit Programs' provided all such acts are authorized by the Insurance."

Darby Lumber contended that coverage existed because the ESOP could not exist, and no employees could be enrolled, without a purchase of Darby Lumber stock. Darby Lumber argued that the purchase of stock effected enrollment, and that the allegations of wrongdoing related to the valuing and purchase of stock therefore fell

within the administration of the ESOP and the Trust.

Indiana Lumbermens countered that the acts alleged in the employee complaint did not fall within the definition of "Administration." It argued that it was the investment itself, and the valuation of Darby Lumber's stock, that was being complained of, not the administration of the ESOP. Further, it argued that "effecting enrollment, termination or cancellation" did not extend to creation and funding of the ESOP and the Trust.

The court pointed out that Darby Lumber and the Russells were accused, in part, of overvaluing Darby Lumber stock that they sold to the Trust to be invested in the ESOP. It concluded that the miscalculation of the value of the stock might involve, under certain circumstances, relatively routine ministerial acts within the definition of "Administration." The court, however, contrasted the type of "ministerial acts" that might fall within coverage to the "decision-making and monitoring" involved in "managing" a benefits plan that did not. The latter were clearly "excluded from coverage" by the definition of "Administration."

Recently, the U.S. Court of Appeals for the Ninth Circuit affirmed the district court's decision that underlying suits did not involve "Administration" as defined in insurance contracts issued by Wausau Underwriters Insurance Company and Employers Insurance of Wausau that contained an employee benefits liability insurance endorsement. In *Travelers Cas. & Surety Co. v. Wausau Underwriters Ins. Co.*, 2005 U.S. App. Lexis 7500 (9th Cir. Apr. 28, 2005), the court noted the definition of "Administration" contemplates "Administrative and ministerial" acts, not acts of a discretionary, decision-making nature. The Ninth Court concluded that the wrongful acts alleged in the underlying complaints involved the discretionary acts of the employer in failing to pay into the program under which the employees were claiming. Such acts were not "merely administrative." Thus, they did not fall within the definition of "Administration" as "giving counsel to employees with respect to those benefits." Indeed, the court stated that it agreed with the district court that "[t]here is simply no principled way to shoehorn a claim alleging failure to fund a profit-sharing program into an insurance

provision covering 'providing interpretations,' 'giving counsel,' 'handling records,' or 'effecting the enrollment, termination or cancellation of employees' in an employee benefits program."

The court found that it was "plain on the facts of the [employees'] Complaints that [Wausau] did not insure the types of claims alleged in the Underlying Actions."

William M. Savino & Stephen J. Smirti, Jr., *Key Requirements For Coverage Under Employee Benefits Liability Endorsement*, MEALEY'S EMERGING INSURANCE DISPUTES, available at http://www.rivkinradler.com/rivkinradler/Publications/newformat/200510SavinoSmirti.shtml#ftn_6 (last visited June 27, 2006).

As an endorsement to a CGL policy, EBL coverage typically is written subject to a separate limit corresponding to the CGL policy limit applying to the other coverages provided. The result is that coverage may also apply follow form when an umbrella policy is issued. "This is especially advantageous because employee benefits liability can be labeled as an exposure that is subject to a frequency of loss with a severity potential." Donald S. Malecki, *Employee Benefits Liability & Fiduciary Liability*, ROUGH NOTES (Nov. 2000).