

CLIENT ALERT

STARBUCKS AND HOME DEPOT: LESSONS IN EMPLOYMENT PRACTICES LIABILITY COVERAGE

June 2023 saw nearly \$100 million in awards and settlements combined between two notable cases against Starbucks and Home Depot. The availability of Employment Practices Liability coverage for these amounts is not public information. However, these cases highlight recurring employment law and insurance coverage issues that are certainly not unique to Fortune 500 companies and that should be considered when evaluating employment-related risk management needs and options.

JURY SERVES FORMER STARBUCKS MANAGER \$25.6 MILLION FOR DISCRIMINATION CASE AGAINST THE COMPANY

A federal jury in New Jersey awarded a former Starbucks regional manager \$25.6 million after finding in her favor on claims of racial discrimination. In 2018, Starbucks fired Shannon Phillips during the fallout from the arrest of two black men at a Philadelphia store in her northeastern U.S. territory. Phillips' subsequent lawsuit alleged that Starbucks discriminated against her based on her race in endeavoring to "save face" by targeting and punishing white employees directly or tangentially related to the incident.

Employment-related racial, gender and disability-based discrimination cases are, unfortunately, nothing new. "Reverse discrimination" cases, like Phillips' against Starbucks, are less common but are seeing an uptick as many companies develop and implement DEI (Diversity, Equity, Inclusion) initiatives following the surge of the Black Lives Matter movement and related social and political justice issues over the last few years. In addition, it remains uncertain if there will be a spike in reverse discrimination cases against academic institutions, as the United States Supreme Court recently struck down the use of affirmative action in higher education admission policies following lawsuits against The University of North Carolina and Harvard.

The Starbucks damages award is comprised of \$600,000 in compensatory damages and a staggering \$25 million in punitive damages. As the name suggests, compensatory damages are intended to compensate a plaintiff for specific financial obligations or hardships that would not otherwise exist but for a defendant's acts. In the employment law context, this can include both past and future salary expected (but not paid) and the costs associated with the treatment of emotional distress stemming from an employer's actions.

To support a claim for compensatory damages, plaintiffs will present evidence demonstrating the financial impact of their employer's acts, which can include projections of anticipated future earnings and statements from treating mental health professionals. Subject to its other terms and exclusions, it is commonplace for an EPL policy to generally cover compensatory awards.

Potential coverage for punitive damages is less straightforward and requires a closer look at a policy's definition of "Loss" or "Damages," in addition to local law on insurability of punitive damages. While punitive damages are not frequently awarded, it is nonetheless worthwhile to consider funding sources for these amounts as they can reach seven or even eight figures. The purpose of punitive damages is to "punish" a bad actor. Unlike compensatory damages, the amount of punitive damages awarded is subjective and need not compensate any specific financial aspect of the plaintiff's harm. Since punitive damages are intended to deter undesirable acts and behaviors, the availability of insurance to indemnify punitive damages would potentially stifle their intended effect.

Therefore, the public policy in many states dictates that insurance cannot indemnify its insureds for punitive damages. In an effort to address the discrepancy among the states and provide policyholders with more expansive coverage, EPL policies can include "most favorable jurisdiction language," which means that the insurer will indemnify punitive damages if allowed by the law of a jurisdiction reasonably related to the claim (e.g., depending on state law, the state where the insured is domiciled, a state where the insured has operations, or the state where the insurance carrier is domiciled).

CALIFORNIA EMPLOYEES CONSTRUCT \$72.5 MILLION CASE AGAINST HOME DEPOT

Home Depot has agreed to pay \$72.5 million to settle a federal class action lawsuit in California brought by employees alleging various types of wage and hour violations. Plaintiffs, hourly retail employees who originally filed the lawsuit in March 2016, alleged improper rounding clock-in and clock-out times to quarter hours and failure to pay for time spent collecting and putting on orange aprons ahead of shifts. The settlement has multiple components and is expected to reflect nearly \$28 million for plaintiffs' attorney fees and expenses, with the balance representing the amount to be distributed to the class members.

As with the Starbucks award, the Home Depot settlement lends itself to an examination of potential indemnity for the newly created legal and financial debt. As an initial matter, EPL policies distinguish between "backpay" or "front pay" and "wages." Typically, a standard EPL policy's definition of Loss or Damages specifically includes backpay and front pay as items contemplated as compensatory damages. As previously stated in the context of the Starbucks case, these are amounts that an employee would allegedly be earning but for the wrongful acts of an employer (most likely, wrongful termination or creation of a hostile work environment such that the plaintiff purportedly felt compelled to leave their job).

Backpay and front pay are distinguishable from wages, which are time-based amounts that employees are paid in consideration for the work performed on behalf of an employer. While also compensatory in nature, wages are often specifically uncovered, or excluded from the EPL definition of "Loss" or "Damages." Insurance is intended to cover potential risk, whereas non-payment of wages is an almost certain financial exposure to an employer who fails to pay earned wages to its employees and there are inherent public policy considerations.

Limited coverage for wage and hour claims exists domestically, mainly in the form of defense costs coverage, and it will often be subject to a sublimit within the policy's aggregate limit of liability. For example, a policy with a \$5 million aggregate limit could include a \$250,000 sublimit as part of, and not in addition to, the \$5 million aggregate limit for costs associated with defending wage and hour claims. In addition, while these EPL policies will not typically indemnify the wages themselves, they will indemnify retaliation claims borne out of wage and hour violations. In these cases, carriers are likely to insist on an allocation between defense costs and/or damages associated with the wage claim vs. any related retaliation claim.

WHAT INSUREDS NEED TO KNOW

Whether unilaterally levied by a judge/jury, as in the Starbucks case, or mutually agreed upon between the parties, as in the Home Depot case, insureds can expect significant limitations on coverage for punitive damages and wages. However, additional coverage options are available and should be considered, depending on the nature and scale of an insured's operations. If business operations are limited to states where punitive damages are insurable, the "most favorable jurisdiction"

language may suffice, but insureds should be cautioned that state law is subject to change. A more reliable coverage option can be accessed through the Bermuda market, which offers a "wraparound" policy to complement an existing EPL program and cover only punitive damages. The Bermuda market also offers more comprehensive standalone policies for wage and hour claims, which may be particularly attractive to insureds with any significant contingency of hourly employees in its workforce.

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