

# IMPLICATIONS OF THE CURRENT LAYOFF PRACTICES ON EPL RISKS

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## INTRODUCTION

Since early 2008, the U.S. has experienced its highest rate of unemployment in 25 years. During the 27 months from December 2007 through February 2010, the total number of mass layoff<sup>1</sup> events was 55,309 and the associated number of initial unemployment claims was 5,580,819. The April 2010 national unemployment rate reached 9.9 percent, even with the addition of 290,000 new jobs, up from 5 percent in December 2007. As shown in Figure 1, we have a long way to go to return to the pre-recession employment picture.

High levels of unemployment have numerous negative effects on the economy as a whole as well as on individual employers and employees. For employers, an important consequence of needing to reduce the size of the workforce is the potential for increased levels of discrimination claims. Employment practices liability (EPL), which includes discrimination claims, has been an area of increasing costs to employers, since even before the downturn. Recent unemploy-

ment trends, however, raise the risk dramatically and highlight the need for employers to manage this potential risk effectively. The intention of this article is to discuss some of the specific EPL claim

trends seen in recent years and to offer suggestions for managing them.

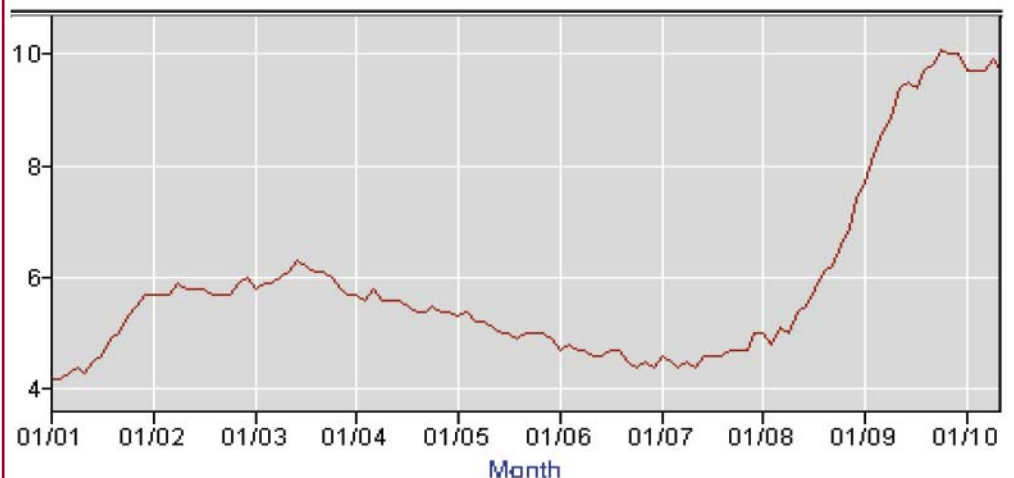
## FEATURES IN CURRENT LAYOFFS

EPL claims follow trends in unemployment; hence, an important place to start in understanding the risk is to have a better appreciation of those trends. The U.S. Bureau of Labor Statistics reported on March 3, 2010 that annual average unemployment rates rose in 2009 in all regions, divisions, and states. Within one year, the U.S. unemployment rate jumped by 3.5 percentage points to 9.3 percent.

While unemployment rates rose in all categories, the rate of increase differed by region, industry, gender, ethnicity, etc. In Table 1, unemployment rates are shown by state. Most heavily hit was Michigan, with the unemployment rate reaching 13.6 percent in 2009 up from 8.3 percent in 2008. Much of this unemployment has resulted from mass layoffs by the automotive industry, yet other factors are relevant as well.

In addition to variations across industries and therefore regions, the current unemployment scenario also affects particular groups of workers differently. Quite significantly, we note that men are much more adversely affected than women. From September 2008 to January 2010, 4.4 million men lost their jobs compared to 2.3 million women, according to the Bureau of Labor Statistics, with the male unemployment rate at 11.7 percent and that for women at 9.7 percent, the largest gap since data

Figure 1. Unemployment Rate



Source : U.S Department of Labor - Bureau of Labor Statistics (June 23, 2010)

Type of Data : Percent or rate Age : 16 years and over

Table 1. Unemployment rate changes by State, 2008–09 annual averages

State	Rate		change	State	Rate		change
	2008	2009			2008	2009	
Alabama	5.2	10.1	4.9	Montana	4.6	6.2	1.6
Alaska	6.5	8.0	1.5	Nebraska	3.3	4.6	1.3
Arizona	5.9	9.1	3.2	Nevada	6.7	11.8	5.1
Arkansas	5.2	7.3	2.1	New Hampshire	3.9	6.3	2.4
California	7.2	11.4	4.2	New Jersey	5.5	9.2	3.7
Colorado	4.9	7.7	2.8	New Mexico	4.5	7.2	2.7
Connecticut	5.6	8.2	2.6	New York	5.3	8.4	3.1
Delaware	4.9	8.1	3.2	North Carolina	6.2	10.6	4.4
Florida	6.3	10.5	4.2	North Dakota	3.2	4.3	1.1
Georgia	6.2	9.6	3.4	Ohio	6.6	10.2	3.6
Hawaii	4.0	6.8	2.8	Oklahoma	3.7	6.4	2.7
Idaho	4.9	8.0	3.1	Oregon	6.5	11.1	4.6
Illinois	6.4	10.1	3.7	Pennsylvania	5.3	8.1	2.8
Indiana	5.8	10.1	4.3	Rhode Island	7.6	11.2	3.6
Iowa	4.4	6.0	1.6	South Carolina	6.9	11.7	4.8
Kansas	4.4	6.7	2.3	South Dakota	3.1	4.8	1.7
Kentucky	6.6	10.5	3.9	Tennessee	6.7	10.5	3.8
Louisiana	4.5	6.8	2.3	Texas	4.9	7.6	2.7
Maine	5.3	8.0	2.7	Utah	3.7	6.6	2.9
Maryland	4.4	7.0	2.6	Vermont	4.5	6.9	2.4
Massachusetts	5.3	8.4	3.1	Virginia	3.9	6.7	2.8
Michigan	8.3	13.6	5.3	Washington	5.4	8.9	3.5
Minnesota	5.4	8.0	2.6	West Virginia	4.3	7.9	3.6
Mississippi	6.8	9.6	2.8	Wisconsin	4.8	8.6	3.8
Missouri	6.1	9.3	3.2	Wyoming	3.2	6.4	3.2

Source : U.S Department of Labor - Bureau of Labor Statistics

The two most frequently filed claims are racial discrimination and retaliation, followed by sex. Disability charges grew the fastest at 10.3 percent, while age charges showed the biggest drop among the categories over the last two years. Note that the surging disability charges can be attributed at least in part to the recent changes in the Americans with Disabilities Act, effective in January 2009.

Noteworthy to us is that the national origin charges increased by 5 percent from 2008 to 2009, representing the second steepest climb among the categories of EEOC charges. This result seems to track the high rate of unemployment among foreign-born workers. With an increasingly diverse ethnicity in the U.S. workforce, employers likely have an increasing exposure to EPL claims.

A second important aspect to current unemployment trends and resulting EPL claims is the increasing sexual harassment claims from men. According to a March 23, 2010 *Wall Street Journal* article, 16.4 percent of all sexual harassment claims were filed by men in 2009, up from 15.4 percent in 2006 according to the EEOC. In addition, Ron Chapman, an attorney with the employment law firm Ogletree Deakins in Dallas, is quoted saying “In most cases the man suing is someone who has been fired or laid off. The spike in male sexual harassment claims coincides with a recession that has hit men harder than women. In the past, victims of harassment—especially men—might have ‘voted with their feet,’ and found new jobs rather than turning to the legal system. But, now they are more likely to rely on the legal system.”<sup>2</sup>

Table 2. Employment Status of Foreign-born and Native-born by regions

(Numbers in thousands)

Regions	2008			2009		
	Civilian Labor Force			Civilian Labor Force		
Foreign Born	Total	Employed	Unemployment Rate	Total	Employed	Unemployment Rate
Northeast	5,044	4,793	5.0	5,079	4,652	8.4
South	7,610	7,198	5.4	7,593	6,914	8.9
Midwest	2,708	2,547	5.9	2,689	2,422	10
West	8,701	8,122	6.7	8,563	7,620	11
<b>Native Born</b>						
Northeast	23,186	21,903	5.5	23,268	21,336	8.3
South	47,437	44,826	5.5	47,388	43,142	9
Midwest	32,231	30,279	6.1	32,077	29,026	9.5
West	27,369	25,694	6.1	27,484	24,765	9.9

Source : U.S Department of Labor - Bureau of Labor Statistics

collection began in 1948. Furthermore, as shown in Table 2, foreign-born workers are now unemployed at a higher rate (9.7 percent) than are native born workers (9.2 percent). The last time foreign-born workers’ unemployment outpaced native born workers was 2003. Both of these trends may have implications for EPL claims.

### FEATURES AND TRENDS IN EPL CLAIMS

Over the past half century, the U.S. has moved away from an “at will” employment

system to one in which various groups and individuals are protected. The categories of Equal Employment Opportunity Commission (EEOC) discrimination claims are described in Table 3. Statistics of claims by type are provided in Table 4, which illustrate that race and retaliation claims represent the largest areas of claims, followed closely by sex. We observed a small drop in overall claims from 2008-09, but the general trend has been upward and expected to rise in accordance with the increased unemployment rate.

Consistent with these conditions, the share of sexual harassment claims filed by men rose more in some states with higher than average unemployment rates. For example, in Michigan, where the unemployment rate stood at 14.6 percent in January 2009, the percentage of claims by men increased to 26.6 percent in 2009 from 16.7 percent in 2007. California saw a rise to 23.6 percent in 2009 from 18.7 percent over the same period. In states where unemployment did not climb as much, claims actually dropped. Nebraska, which had a 4.7 percent unemployment rate in 2009, saw claims drop from 23.4 percent in 2007 to 12.7 percent in 2009.<sup>3</sup>

Table 3. Types of EEOC claims

Type	Definition according to EEOC
Age	Discriminating against a person because of his/her age with respect to any term, condition, or privilege of employment, including hiring, firing, promotion, layoff, compensation, benefits, job assignments, and training
Disability	Discriminating against qualified individuals with disabilities in job application procedures, hiring, firing, advancement, compensation, job training, and other terms, conditions, and privileges of employment
National Origin	Treating someone less favorably because he or she comes from a particular place, because of his or her ethnicity or accent, or because it is believed that he or she has a particular ethnic background, or because of marriage or other association with someone of a particular nationality
Race	Discrimination against a person because of his/her racial group or perceived racial group, his/her race-linked characteristics (e.g., hair texture, color, facial features), or because of his/her marriage to or association with someone of a particular race or color
Religion	Discriminating against individuals because of their religion in hiring, firing, and other terms and conditions of employment
Sex	Discriminating against any employee or applicant for employment because of his/her sex in regard to hiring, termination, promotion, compensation, job training, or any other term, condition, or privilege of employment
Retaliation	Unique in that it applies to all of the other claims, such that employers may not take retaliatory action against employees who oppose discrimination, file charges, or otherwise participate in litigation related to any of the claims mentioned above

Source: Jessica Faye Carter - Workplace Diversity Examiner

These two trends: increasing levels of foreign-born workers and unemployment among them as well as increasing levels of unemployment among men relative to women and their increasing use of sexual harassment claiming options, may well change the underlying underwriting factors for EPL insurers.

Our discussion above has focused on the incidence of EPL claims, but severity is also an important underwriting concern. According to *American Chronicle*, EPL judgments or awards increased almost four times from 1994 to 2005. The median award in EPL cases was over \$250,000 exclusive of legal fees in 2005 and EPL claims comprised 30 percent of all civil litigation in the U.S. court. Furthermore, legal cost typically exceed the cost of the settlement or judgment with its average cost over \$100,000 for a single plaintiff and over \$3,000,000 for class action suits.<sup>4</sup>

### CURRENT EPL RISK MANAGEMENT PRACTICES

Despite the growing and large frequency and severity of EPL claims, many employers seem not to prepare for the risks. According

to a recent Hartford Steam Boiler survey, managers of small firms are concerned about EPL risks; yet only one percent of these firms actually purchase EPL insurance.<sup>5</sup> Furthermore, EPL claims hit small and mid-sized businesses as much as large organizations. The more intimate working environment, in fact, can lead to heightened risks because firings are much more personal and closely scrutinized, according to the article of *National Underwriter P&C*. Upon the EPL claims, the legal cost of depending is too much for the employer of SMB.

In Table 5 the current EPLI buying propensity by market size segment is illustrated. One important potential is that small business may simply be unaware of the exposures. According to Jeffrey O'Shaughnessy, once owners of small businesses learned, more than 90 percent of small business owners showed interest in buying an EPLI policy.<sup>6</sup>

### IMPLICATION AND SUGGESTION

Our purpose with this article is to identify key changes in the EPL environment that are likely to affect both employers and their insurers. The ultimate intent is to

offer suggestions for managing EPL risks. What we have identified are new trends in unemployment with men reaching new heights of unemployed status, especially when compared with that of women, and of foreign nationals increasingly in the unemployed status. With increasing sexual harassment claims by men and with over one million foreign nationals obtaining permanent residency each year, these trends are important risks to organizations.

Although these trends may be somewhat new, traditional EPL risk control measures are still valid means to reduce the frequency and severity of the EPL claims. Appropriate control techniques include: establishment and implementation of hiring systems that comply with all regulations and laws; development of clear and complete employee handbooks; as well as completion and documentation of regular employee performance reviews; use of a documented termination procedure when necessary; and conclusion of employment with exit interviews.<sup>7</sup>

Despite the fact that these may seem quite common and natural activities, they often are overlooked even by the most advanced and sophisticated employers. Furthermore, with concern over potential discrimination through simple policies that result in adverse results for a protected class (referred to as "disparate impact"), employers must recognize that even seemingly neutral policies can lead to potential litigation and even violation of the law. With layoffs affecting particular segments of the population harder than others, this particular concern becomes greater. In addition to the traditional methods mentioned above, therefore, employers ought to implement policies to identify possible conditions in which protected classes of employees may be harmed more often than the general population.

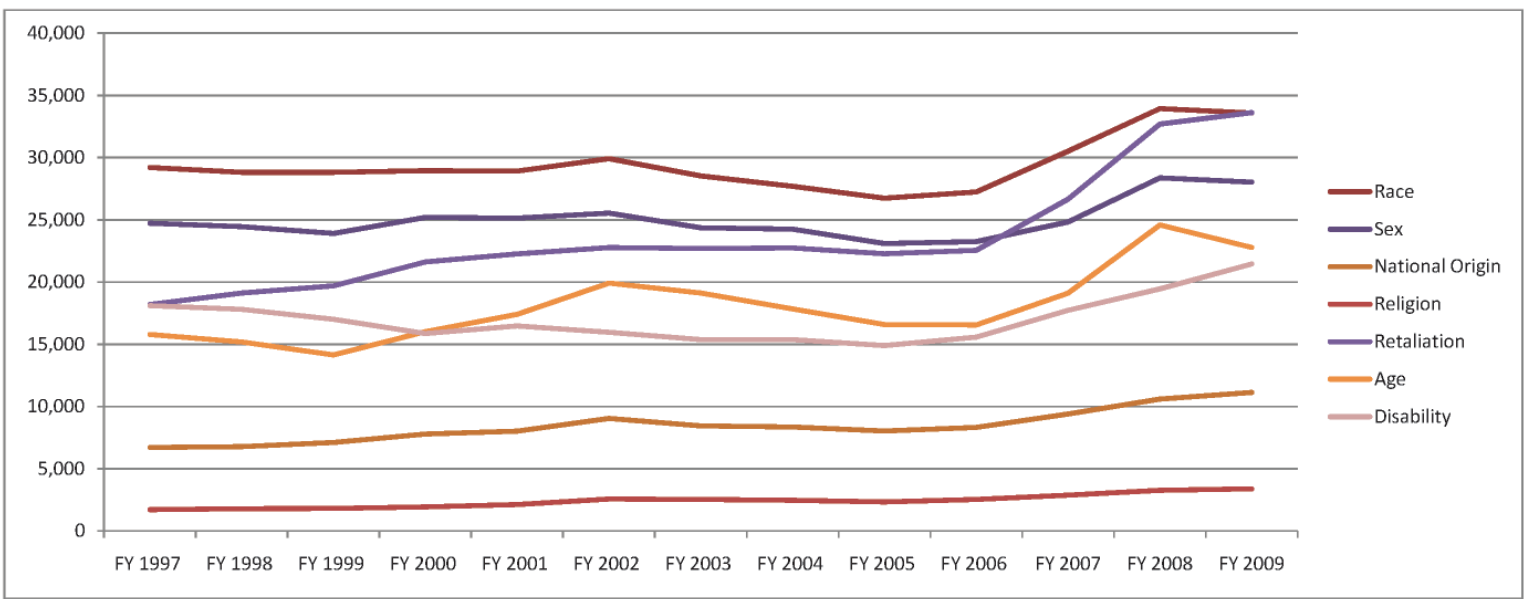
In addition, employers of all sizes ought to consider the full benefits that derive from purchase of insurance. Often the premium is quite high relative to the limit of coverage (and relative to a broader general liability policy); however, the insured typically obtains coverage for legal defense in connection with the liability protection. That legal defense protection can be even more valuable than the loss protection, given the insurer's legal expertise and interest in minimizing the ultimate payout.

Table 4 : EEOC Charge Statistics by Discrimination Type

	FY 1997	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002	FY 2003	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
Total Charges	80,680	79,591	77,444	79,896	80,840	84,442	81,293	79,432	75,428	75,768	82,792	95,402	93,277
Race	29,199	28,820	28,819	28,945	28,912	29,910	28,526	27,696	26,740	27,238	30,510	33,937	33,579
	36.20%	36.20%	37.30%	36.20%	35.80%	35.40%	35.10%	34.90%	35.50%	35.90%	37.00%	35.60%	36.00%
Sex	24,728	24,454	23,907	25,194	25,140	25,536	24,362	24,249	23,094	23,247	24,826	28,372	28,028
	30.70%	30.70%	30.90%	31.50%	31.10%	30.20%	30.00%	30.50%	30.60%	30.70%	30.10%	29.70%	30.00%
National Origin	6,712	6,778	7,108	7,792	8,025	9,046	8,450	8,361	8,035	8,327	9,396	10,601	11,134
	8.30%	8.50%	9.20%	9.80%	9.90%	10.70%	10.40%	10.50%	10.70%	11.00%	11.40%	11.10%	11.90%
Religion	1,709	1,786	1,811	1,939	2,127	2,572	2,532	2,466	2,340	2,541	2,880	3,273	3,386
	2.10%	2.20%	2.30%	2.40%	2.60%	3.00%	3.10%	3.10%	3.10%	3.40%	3.50%	3.40%	3.60%
Retaliation	18,198	19,114	19,694	21,613	22,257	22,768	22,690	22,740	22,278	22,555	26,663	32,690	33,613
	22.60%	24.00%	25.40%	27.10%	27.50%	27.00%	27.90%	28.60%	29.50%	29.80%	32.30%	34.30%	36.00%
Age	15,785	15,191	14,141	16,008	17,405	19,921	19,124	17,837	16,585	16,548	19,103	24,582	22,778
	19.60%	19.10%	18.30%	20.00%	21.50%	23.60%	23.50%	22.50%	22.00%	21.80%	23.20%	25.80%	24.40%
Disability	18,108	17,806	17,007	15,864	16,470	15,964	15,377	15,376	14,893	15,575	17,734	19,453	21,451
	22.40%	22.40%	22.00%	19.90%	20.40%	18.90%	18.90%	19.40%	19.70%	20.60%	21.40%	20.40%	23.00%

Note : Individuals often file charges claiming multiple types of discrimination

Source : EEOC (Equal Employment Opportunity Commission)



Importantly, EPL insurers also offer extensive loss control services, including training programs that help insureds understand their HR management responsibilities and show insureds how to create/maintain a workplace environment that will prevent employment practice violations. Other services include specimen employee handbooks, review of existing handbooks, telephone access to experienced attorneys or consultants to discuss a particular problem, confidential EPL audits, and consultants to help the insured prepare its response at hearings before the

EEOC or state or local agencies. Thus, risk control services can be an important feature of EPL insurance (EPLI). Because EPL insurers can vary widely in the types and quality of services, the available risk control services are one factor to be weighed in selecting an EPL insurer.<sup>8</sup>

For insurers, we anticipate that underwriters are aware of the changing trends in underlying employment (and more importantly unemployment) conditions. The world around us, however, is changing so rapidly that

sometimes keeping up is difficult. Underwriters and actuaries need to be on the forefront of these conditions, work to prepare their insureds against potential liability, and price anticipated changes into their rate structures.

In general, employment practices liability continues to be an important, growing, evolving area where risks can be significant. It also offers employers an opportunity to be ahead of the game through excellent risk management and acquisition of superior coverage.

Table 5 : Current buying propensity by market size segment

Market Size Segment	Percent with Coverage
Small Commercial	1.1%
Middle Markets	11.7%
National Accounts	9.8%

Source : MarketSatnce      Note : Standalone EPLI was applied

**FOOTNOTES**

- 1 Mass layoff event: Fifty or more initial claims for unemployment insurance benefits filed against an employer during a five-week period, regardless of duration. Source: Bureau of Labor Statistics of U.S. Department of Labor.
- 2 Mattioli, Dana. "More Men Make Harassment Claims." *The Wall Street Journal*, March 23, 2010.

- 3 Ibid.
- 4 Lipton, Brett. "Employment Practices Liability Insurance Claims on the Rise." *American Chronicle*, April 12, 2010.
- 5 O'Shaughnessy, Jeffrey. "Small Firms Can Face Big EPL Exposures," *National Underwriter, P&C*; Mar. 29, 2010; pg. 16.
- 6 Jeffrey O'Shaughnessy, "Small Firms Can Face Big EPL Exposures," *National Underwriter, P & C*, Mar. 29, 2010.

- 7 Malecki, Donald., Arthur L. Flitner, and Jerome Trupin. *Commercial Liability Risk Management and Insurance: AICPCU*, 2008.
- 8 Malecki, Donald., Arthur L. Flitner, and Jerome Trupin. *Commercial Liability Risk Management and Insurance: AICPCU*, 2008.

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