

FLSA Exclusion Bars Coverage Under EPL Policy

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The United States Court of Appeals for the Tenth Circuit, applying Kansas law, has held that an employment practices liability policy afforded no coverage for a class action based on an exclusion for alleged violations of the Fair Labor Standards Act or "similar" state law. *Payless Shoesource, Inc. v. Travelers Cos., Inc.*, No. 08-3246 (10th Cir. Nov. 10, 2009).

A group of present and former employees of the company filed a class action against the company alleging that the company "unlawfully required hourly employees to work 'off the clock' without compensation and did various other things proscribed by the California Labor Code, the California Business & Professions Code, and state common law." The company tendered the lawsuit for coverage under its EPL Policy. The insurer denied coverage based on the policy's exclusion "for an actual or alleged violation of the Fair Labor Standards Act (except the Equal Pay Act), the National Labor Relations Act, the Worker Adjustment and Retraining Notification Act, the Consolidated Omnibus Budget Reconciliation Act of 1985, the Occupational Safety and Health Act, the Employee Retirement [Income] Security Act of 1974, any workers' compensation, unemployment insurance, social security, or disability benefits law, other similar provisions of any federal, state, or local statutory or common law or any amendments, rules or regulations promulgated under any of the foregoing." Following settlement of the underlying action, the employer filed suit against the insurer seeking coverage. In the coverage litigation, the insured contended that the phrase "other similar provisions of any federal, state, or local statutory or common law" in the exclusion must be read as applying only to the immediately preceding clause and not to the Fair Labor Standards Act (the FLSA). In the alternative, the insured argued that the placement of the modifier within the exclusion rendered the exclusion ambiguous.

The appellate court affirmed the trial court's entry of summary judgment in favor of the insurer. In so holding, the court noted that "a punctuation peccadillo notwithstanding, the meaning of the parties' contract is unambiguous" and by "operation of the plain terms of the agreement, [the company] has no claim for coverage."

First, the court rejected the insured's contention that the applicability of exclusion was narrowed by the perhaps grammatically incorrect placement of the modifier. According to the court, the insured's argument was implausible because the "other similar provisions" clause was separated from prior clauses by a comma and not a conjunction, which, unlike a comma, would have suggested a connection with the preceding clause.

In addition, the court noted that the "other similar provisions" clause appeared at the end of the exclusion, which is "where modifiers meant to address all of the preceding items are often found." In addition to these textual points, the court made the more fundamental point that the insured's interpretation of the exclusion would lead to an absurd result, in that the insurer would have "disclaimed responsibility for liabilities arising under certain federal laws but then assumed responsibility for some (but not all) liabilities arising under parallel and even identical state laws."

The court also rejected the insured's argument that the placement of the modifier rendered the exclusion ambiguous. The insured argued that the misplaced modifier violated rules of proper grammatical construction, thus creating an ambiguity. According to the court, "in the more mundane task of contract interpretation, [courts] must be no less entitled to acknowledge the parties' plain meaning without being straight-jacketed by a grammatical rule into reaching a patently unintended result."

Finally, having concluded the exclusion barred coverage for claims alleging violations of laws "similar" to the FLSA, the court addressed whether the exclusion applied to bar coverage for the suit against the company. The court determined that all of the state law violations were "similar" to the FLSA and thus excluded from coverage under the terms of the policy. In so holding, the court also found that the word "similar" was not ambiguous in the context of the exclusion.