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EPLI POLICY DOES NOT EXCLUDE COVERAGE FOR BREACH OF AN ORAL MODIFICATION TO A WRITTEN EMPLOYMENT CONTRACT

The Seventh Circuit Court of Appeals, in its April 9, 2007 decision in *Krueger Int'l Ins. Co. v. Royal Indem. Co.*, held that an oral modification to a written employment contract abrogates the exclusion in an Employment Practices Liability Insurance policy ("EPLI") for losses attributable to the employer's breach of written employment contracts. Addressing the parameters of coverage provided by EPLI, the court reasoned that because an employer needs coverage for binding representations outside its control (*i.e.*, a senior employee's oral promise, often unauthorized by the employer), as opposed to written contracts controlled exclusively by the employer, coverage extends to an oral modification of a written employment contract.

The employer conduct at issue in *Krueger* occurred when the insured's CFO – in the course of explaining to four employees the financial implications of their proposed resignation – orally represented a stock redemption valuation procedure which differed from that set forth in the company's shareholders' agreement. When these four employees subsequently resigned, however, their shares were redeemed in accordance with the written shareholders' agreement procedures as opposed to the method set forth by the CFO, resulting in a lower buy-back price. The employees sued the employer to recover the difference and were awarded $5.3 million.

The EPLI policy at issue provided coverage for damages arising out of the breach of oral employment contracts, but specifically excluded coverage for losses premised upon the breach of written contracts. The court in *Krueger* concluded that the agreement at issue was an "oral-written hybrid". Finding these "oral-written hybrids" more similar to an oral representation than a written contract, the court found the exclusion inapplicable.

Although the oral-written hybrid analysis did not govern the court's decision because the orally modified redemption provision upon which the employees' damages hinged was part of a shareholders' agreement not insured under the EPLI coverage, the court's pronouncement regarding the scope of the exclusion for losses arising out of the breach of a written contract may have a significant impact on the risk being assumed by insurers who write EPLI coverage.

Should you have any questions or comments, please do not hesitate to contact us.

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