

News & Types: Employment, Labor & Benefits Update

Employer Outsmarts Itself and Loses Over \$5 Million

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Practices: Employment, Labor & Benefits, Litigation

Juanita Berry worked as Vice President of Major Accounts for Telamon Corporation, an Indiana telecommunications company. Using her relationship with AT&T, she was Telamon's senior manager in the New York and New Jersey region, where she oversaw Telamon's AT&T Asset Recovery Program. She was responsible for removing old telecommunications equipment from AT&T sites and selling it. She had considerable authority, including operational oversight over Telamon's facilities in New York and New Jersey and the authority to hire and fire employees, run meetings, and sign contracts on Telamon's behalf.

Unfortunately for Telamon, she was also a thief and a liar. When she removed and sold the old telecommunications equipment, she kept the profits. Telamon discovered her dishonesty in 2011, but not before she stole \$5.2 million. Ms. Berry was fired from her position and later convicted on federal charges of wire fraud and tax evasion in the District of New Jersey. She was sentenced to 60 months' imprisonment and ordered to pay restitution to Telamon of \$3,440,885. But Telamon never saw or expected to see this money from Ms. Berry.

Telamon brought claims against two of its insurance carriers. It failed against both insurance carriers at the trial level and at the court of appeals level. In fact, it lost on summary judgment which meant the court did not even think the claim had sufficient merit to go to trial. And this was in spite of the advantage Telamon started with - the rule that any ambiguity in an insurance policy is construed strictly against the insurance company and in favor of the insured – in this case, Telamon.

So how did Telamon fail? What about the crime insurance policy it had with Travelers Casualty & Surety that specifically covered theft by "an Employee?" Judge Wood, who wrote the 7th Circuit opinion, found a fatal flaw in Telamon's position. It turned out that Telamon did not have a formal employer/employee relationship with Ms. Berry. Rather, Telamon had a series of Consulting Service Agreements with J. Starr Communications, Ms. Berry's one-woman company, through which she provided her services. Having an individual form a legal entity and then having the company contract with that legal entity is a common means to avoid an employer/employee relationship. An employee is a natural person and cannot be a legal entity, such as J. Starr Communications.

Since Ms. Berry was not an "employee", her theft from Telamon was not covered by insurance covering losses caused by employee theft. Fortunately for Telamon, the policy also covered a "natural person... who is leased to the Insured under a written agreement between the Insured and a labor leasing firm, while that person is subject to the Insured's direction and control and performing services for the Insured." After all, wasn't Ms.

Berry (a natural person) leased to Telamon (the Insured) under a written agreement with a labor leasing firm (J. Starr Communications) while Ms. Berry was performing services for Telamon? "No," said Judge Wood.

The defect in Telamon's argument was viewing J. Starr Communications as a "labor leasing firm." According to Judge Wood, a labor leasing firm is a "business concern that sells another person's work for a specified time and for a specified fee." As noted, J. Starr Communications was a one-woman company, whose sole purpose was to provide the services of Ms. Berry. Judge Wood cited other cases involving labor leasing firms, all of which offered the services of multiple individuals, often from multiple locations. "But," noted Judge Wood, "J. Starr was not a firm in the business of leasing labor; it was just Berry's vehicle for providing her own services." So Ms. Berry was neither Telamon's employee, nor was she leased to Telamon by a labor leasing firm. As a result, Telamon struck out on its claim against Travelers under the policy covering employee theft.

Telamon had another policy, a commercial property policy issued by Charter Oak. That policy covered risks of direct physical loss, unless one of its exclusions applied. One of the exclusions was for any "dishonest or criminal act by... employees (including leased employees), directors, trustees, *authorized representatives or anyone... to whom you entrust the property for any purpose.*" (Court's emphasis)

At this point, Telamon might have been feeling pretty good. After all, it lost its claim against Travelers because the court concluded that Ms. Berry was neither an employee nor a leased employee, so this exclusion shouldn't apply. But the court's emphasis of "authorized representative" telegraphed the result. True, Ms. Berry was not an employee nor a leased employee. But she was Vice President of Major Accounts, the most senior person in New York and New Jersey, with operational oversight over Telamon's facilities in those states. She hired and fired employees, ran meetings, and signed contracts on Telamon's behalf. Of course, she was an authorized representative. As an authorized representative, the exclusion in Charter Oak's commercial property policy applied.

Telamon reverted back to its series of agreements with J. Starr Communications. Those agreements did not authorize Ms. Starr to do the specific activity that gave rise to the theft, therefore for this purpose, she was not an authorized representative. But Judge Wood chose to look at Ms. Berry's actual role, which the court noted expanded beyond the agreements' terms. Telamon "did not expect slavish adherence to the list of responsibilities in the Agreements, and so neither should we." Telamon knew about, and permitted, Ms. Berry's activities on behalf of Telamon, even if it was ignorant of the theft. So she was indeed an authorized representative.

Judge Wood noted that, in making its claims, Telamon "crashed into a brick wall. Travelers denied coverage because Berry was not, legally speaking, an employee. And Charter Oak refused to pay because, in practice, she was." But Telamon created its own dilemma. It apparently did not want Ms. Berry on its payroll. But it did want to give Ms. Berry sufficient authority, so that Telamon could profit from her strong relationship with AT&T. It is another case study that shows how clever strategies can sometimes backfire in a big way.

(*Telamon Corporation v. Charter Oak Fire and St. Paul Fire and Marine Insurance Company*, 7th Circuit Court of Appeals, No. 16-1205, March 9, 2017)