

ALERT

Product Recall Insurance: New Specialty Insurance Policies Lead to Plenty of Questions

By Joshua Gold and Rhonda L. Johnson

The stakes involved in a product recall are enormous. Most product recalls present a double-edged sword for policyholders: (1) the not-insignificant expenses incurred in recalling a product from the marketplace; and (2) the potential liability exposure to third parties claiming injury or damage as a consequence of ingesting or handling the "offending" product.

Policyholders require reliable insurance protection sold by a dependable insurance company to respond to the risks posed by product recall situations. One of the newer insurance products being sold by the insurance industry is product recall and contamination insurance. Several insurance companies now market and sell product recall insurance policies. Depending upon the policyholder's specific needs, however, the policy limits offered with these new insurance products may be insufficient to fully transfer the policyholder's risk in the event of a product recall.

Certain product recall insurance policies promise to cover the policyholder's costs incurred in recalling a product that has been contaminated, tampered with or has been the target of extortionists. Product recall insurance policies may also provide insurance coverage for business interruption losses and for costs to restore the product to its intended levels of quality or to re-establish the product's market share to the level existing before the contamination, tampering or extortion took place.

Product recall policies have obvious appeal to policyholders—especially those who have already endured the significant costs associated with removing a product from the market pursuant to a government ordered recall or, voluntarily, due to potential product contamination. Indeed, the recent misfortune of many product makers and their customers underscores the serious consequences of a product recall.

Because the product recall insurance policy is a relatively new insurance product, however, policyholders should be mindful of certain issues that may arise when a claim is made, and be careful to avoid the pitfalls that are built into certain of these insurance policies. Insurance claims under product recall policies have already been battled by insurance companies in litigation. Nevertheless, the provisions and promises contained within product recall policies have gone largely untested thus far.

Policyholders should be aware that some insurance companies will challenge their conduct during a recall to avoid liability under the insurance policy—even where the policyholder acts prudently and quickly to stem the potential losses of a product recall. Specifically, some product recall insurance policies require proof of "symptoms" of bodily injury or

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sickness before coverage is available. Thus, a policyholder that takes proactive measures to remove a product before the onset of serious harm to its users may be challenged by its insurance company claims handlers to demonstrate clearly that symptoms of physical injury would have ensued but for the quick response in removing the product from the market. Putting aside the issue of whether a policyholder would be wise in demonstrating how potentially harmful its product was to consumers, such a position by the insurance company forces the policyholder to bear a scientific burden to demonstrate medical consequences of exposure to the product in situations where it may be very difficult to recreate the actual risk to human health. In effect, the insurance company imposes an obstacle to insurance coverage where the policyholder seeks to quickly mitigate the adverse consequences of a product by recalling it before users are actually harmed.

Other obstacles to a recovery under product recall insurance policies involve compliance with time-sensitive provisions. For example, it is a common feature of product recall insurance policies to include a clause shortening the statute of limitation for the filing of a lawsuit against the insurance company should a dispute arise over insurance coverage. Many insurance companies seek to impose a clause shortening the time for filing a lawsuit to as little as one year. While such a shortened suit clause is unenforceable under the laws of many states, some states will nevertheless find such a provision enforceable against a policyholder. This can lead to devastating consequences for a policyholder.

Policyholders should be aware that product recall insurance policies contain time-sensitive provisions similar to those contained in a commercial property insurance policy, including: (1) a notice provision; (2) a "statement of loss" provision; and (3) a suit limitation provision. Policyholders are well-advised to comply with these time-sensitive provisions very carefully, as even a slight delay by a policyholder in responding to these terms is frequently used by insurance companies to argue for a complete forfeiture of the policyholder's insurance coverage. ■

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