

Maximizing Recovery On Product Liability Insurance Claims

by Robert M. Horkovich and Alex Hardiman

Often when an insurance company is called upon to pay a product liability claim, it will assert that the coverage provided by the product liability insurance policy is significantly narrower than the policyholder expects. Policyholders should be aware, however, that a number of avenues exist to increase the potential for an insurance recovery, regardless of what the insurance company contends.

Product liability insurance usually is a component of commercial general liability insurance unless it is specifically excluded. In essence, product liability insurance generally covers bodily injury or physical damage to a third party's property as a result of the policyholder's work or product. Thus, according to ISO form language, product liability insurance typically covers "all bodily injury and property damage occurring away from premises you own or rent and arising out of your product or your work" and generally requires that the property damage take the form of "physical injury to tangible property."

A series of exclusions that apply to product liability coverage, however, may significantly narrow the coverage, including that: (1) no coverage exists for repairing or replacing the policyholder's defective product or work; (2) no coverage for loss in value or use to third party's property from a product's failure to function as intended and where property can be restored to use by removal or repair of product; and (3) no coverage for recalls by the policyholder or third parties as a result of a defect.

What Constitutes Physical Damage?

Many coverage disputes involving product liability insurance focus on whether the policyholder's defective product or work caused "physical" damage to a third party's property. In these disputes, the insurance company contends that because the policyholder's defective product did not cause physical damage to another party's property, no coverage exists. Even where a product has not caused any readily apparent and immediate physical damage to a third party's property, however, a policyholder may still be able to recover based on the "incorporation doctrine" or for a third party's repair and removal costs.

A number of courts have found that even if the defective product did not cause physical damage to a third

party's property, to the extent the removal or repair of a defective product that is integrated into third party property causes damage, then the third party's costs associated with the defective product's removal, and repair of any damage caused by that removal, should be covered under product liability insurance. In addition, the costs of removing a product in order to access other covered damage might potentially also be recovered as consequential damages.

The Incorporation Doctrine

Similarly, under the incorporation doctrine, certain courts have found physical property damage based on the defective product being integrated into the third party's property, even if that integration did not cause any immediate or actual physical damage beyond the integration itself. Thus, in the context of deciding which policy periods should respond to a claim, the Seventh Circuit in *Eljer Mfg Inc. v. Liberty Mut. Ins. Co.*, held that physical property damage occurred to third party property at the time the product (a defective plumbing system) was incorporated into the third party's property (a house), even if actual harm to the third property did not occur until later.

Although some jurisdictions have disagreed with the *Eljer* case, its reasoning was adopted and in some cases expanded by a number of other courts. For example, the court in *Hoechst Celanese Corp v. Certain Underwriters at Lloyd's of London*, found that physical injury occurred upon installation of defective plumbing and in *Shade Foods v. Innovative Prods. Sales & Marketing, Inc.*, it was determined physical property damage occurred when defective almonds were incorporated into a third party cereal company's products.

In addition, although the costs of a product recall generally are excluded from product liability coverage, to the extent the recall is associated with the repair or removal of a defective product that has already caused damage, coverage may be available for such costs.

Policyholders should not simply accept an insurance company's determination that no physical property damage has occurred and should be aware of the importance of choosing the right jurisdiction in which to litigate a dispute when the incorporation doctrine or removal and repair costs coverage may be at issue.

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