

As Demand For Recall Policies Surges, Coverage Obstacles Lurk

By Bibeka Shrestha

Law360, New York (October 25, 2012, 9:12 PM ET) -- A recent wave of high-profile food recalls have sent more companies running to insurers for product recall coverage, but the few court disputes over these special policies have already revealed ways carriers can swipe coverage from policyholders, attorneys say.

Recall insurance has soared in popularity as regulators overseeing the food industry have become more vigilant and better at identifying foodborne illnesses and their causes. The trend also coincides with the passage of the Food Safety Modernization Act in January 2011, legislation that handed the U.S. Food and Drug Administration the power to order recalls for the first time.

Robert Chesler, an Anderson Kill & Olick PC policyholder attorney, said he'd seen a jump in the number of middle-market companies taking out recall coverage within the past few years. Food processors, distributors and wholesalers are all seeking out these policies, he said.

"Companies are far more careful about recalls and more likely to have recalls if there's any suspicion," Chesler said. "Fear of the FDA knocking on your door is great enough to maintain the market for these insurance products."

According to a report released Wednesday by the U.S. Public Interest Research Group, food recalls led to 37 deaths and caused \$227 million in economic costs between January 2011 and September. During that period, there were about 1,700 illnesses tied to recalled food, including salmonella outbreaks tied to cantaloupes, ground beef, raw tuna, mangoes, papayas and peanut butter.

Data that the FDA and the Food Safety Inspection Service provided to PIRG showed that about 700 illnesses were directly linked to food recalls in 2011, while there have already been more than 1,000 foodborne illnesses tied to recalls this year.

Jonathan Cohen, a Gilbert LLP insurance attorney with expertise in the food industry, said more companies had been turning to him recently to evaluate their need for the coverage and help them work with insurers and insurance brokers to hammer out a recall policy.

"We're in one of those periods where they're getting a lot of attention and people are interested in them," Cohen said.

But attorneys caution that case law on these policies is far from well-established. There are only a handful of court cases that have tested recall policies, and these disputes are usually very fact-specific, according to Cohen.

"Some insurers more than others have shown an interest or willingness to fight, particularly where there's gray areas in the policies," Cohen said.

One coverage issue that has cropped up is whether food products actually need to be contaminated to trigger policies or whether a reasonable expectation that contamination has occurred is enough. Policies generally say they will provide coverage if an illness arises from contaminated food or when it's likely that such an illness will occur.

"There's a gray area as to what that means," Chesler said.

There's also room for debate on whether product recall coverage kicks in when food has been contaminated, but it's uncertain whether the tainted product will cause illnesses down the road, and whether contamination needs to happen during the manufacture or preparation of food in order for these policies to provide coverage, attorneys say.

"These are pretty cutting-edge issues right now," Cohen said. "The case law in this area is very new."

Litigation around these issues is likely to escalate as companies increasingly take out recall coverage and as more and more recalls happen, according to attorneys.

"I think there will be more claims," Chesler said. "The policies are still rather new and a lot of litigation issues haven't been uncovered yet."

As more claims come in, Chesler expects insurers to slap more restrictions on recall policies, but for now the recall policies have provided meaningful coverage in cases of actual food contamination, he said.

Some insurers find it in their self-interest to keep any coverage battles out of court for the time being, as competition has heated up among carriers offering recall coverage, Cohen said.

"Insurers have an incentive to try to avoid coverage fights because they don't want to create a reputation that is not good for them in the short term," Cohen said. "They have these kind of competing interests."

First-party recall policies are typically designed to cover a policyholder's often hefty bill for taking all product off the shelves, testing and destroying the product, cleaning contaminated equipment and providing notification to third parties, according to Chesler.

Third-party recall coverage, on the other hand, would cover a lawsuit brought by a supermarket or other companies for their economic losses from a recall, Chesler said.

According to Cohen, recall policies are still far from standardized and the coverage they offer is fast-evolving. Some companies have been pressing insurers to add coverage for business losses stemming from highly publicized recalls of products that are similar to those offered by policyholders, he said.

For example, reports of tainted peanut butter might prompt customers to swear off products containing peanuts for some time, hurting scores of companies whose product was never contaminated.

"Insurers have not added coverage where policyholders have wanted it," Cohen said. "Insurers tend to be careful and worried about adding coverage [for which], in their view, they have trouble figuring out the instance of risk."

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