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## FOOD CONTAMINATION ALERT

### MINNESOTA COURT OF APPEALS APPLIES FIRST-PARTY “PHYSICAL DAMAGE” DECISION TO THIRD-PARTY PROPERTY DAMAGE CLAIM IN AN ADULTERATED FOOD CASE AND REMANDS FOR NEW TRIAL

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On June 26, 2007, the Minnesota Court of Appeals held that an adulterated food product that becomes legally unsaleable can be deemed “physically damaged” under a commercial general liability insurance policy. *United Sugars Corp. v. St. Paul Fire & Marine Ins. Co.*, No. A06-1933 (Minn. Ct. App. June 26, 2007).

In *United Sugars*, the largest marketer of industrial consumer sugar in the United States, United Sugars Corporation (“USC”), brought a breach of contract action against its insurer for coverage for alleged property damage to a customer’s food product. *United Sugars*, No. A06-1933, slip op. at \*1. The CGL policy at issue defined “property damage” as “physical damage to tangible property of others, including all resulting loss of use of that property.” *Id.* The policy did not define the term “physical damage.” *Id.*

In July 2004, USC’s customer, Nestlé, informed USC that it had shut down production of cookie dough because it had discovered bee parts and cigarette butts in USC’s sugar. *Id.* Nestlé concluded that the dough that had been produced using the sugar was “adulterated” under the Food and Drug Administration’s regulations and, therefore, could not be legally sold. *Id.* USC agreed that the cookie dough could not be legally sold due to contact with the contaminated sugar, but neither USC nor Nestlé performed any testing to determine whether the contaminants were actually mixed in with the cookie dough. *Id.*

Nestlé then submitted a \$760,000 invoice to USC, claiming damages for loss of “cookie dough and raw ingredients, cleaning production equipment, and storage of the cookie dough prior to [its] destruction.” *Id.* USC tendered the claim to its insurer, which denied coverage on several grounds, including that “property damage” had not occurred. *Id.* at \*2. USC subsequently brought suit against its carrier. *Id.*

In the coverage action, both parties moved for summary judgment. The trial court denied the insurer’s motion and entered partial summary judgment in favor of USC, reasoning that if Nestlé’s property was contaminated by USC’s sugar, then there would be coverage for the claimed loss. *Id.* However, the trial court also concluded that whether the dough was actually contaminated by the sugar was a genuine issue of material fact. *Id.* At trial, the special verdict form submitted to the jury contained only one question: “On or about July 9, 12, or 13 was Nestlé’s cookie dough contaminated with foreign matter by [USC’s] product?” *Id.* The jury answered “No,” and as a result of the verdict, the trial court entered judgment in the insurer’s favor. *Id.* The trial court also concluded that the insurer did not breach its duty to defend and denied USC’s motion for a new trial. *Id.*

On appeal, the Minnesota Court of Appeals applied the definition of “physical damage” previously used in a first-party property policy case, *General Mills, Inc. v. Gold Medal Ins. Co.*, 622 N.W.2d 147 (Minn. Ct. App. 2001). In *General Mills*, the Food and Drug Administration found traces of a chemical that was not harmful to consumers in cereal produced by oat stocks, but that had not been approved for use on oats. *General Mills*, 622 N.W.2d at 150. Although the insurer argued that there was no “physical damage” because the cereal could be safely consumed, the court disagreed, reasoning that “direct physical loss can exist without actual destruction of property . . . it is sufficient to show that the insured property is injured in some way.” *Id.* at 152. The court concluded that the fact that the cereal could not be legally sold was sufficient to support a finding of physical damage. *Id.*

In *United Sugar*, despite the insurer’s objections that *General Mills* involved a first-party property policy and not a third-party liability policy, the Minnesota Court of Appeals applied the *General Mills* definition of “physical damage” and held that “an adulterated food product can be deemed physically damaged because it is legally unsaleable.” *United Sugar*, No. A06-1933, slip op. at \*3. The court also concluded that the special verdict form submitted to the jury did not accurately reflect the law as stated in the *General Mills* case, “i.e., that mere exposure of a food product to contaminants supports a finding of physical damage as that term is used in an insurance policy.” *Id.* at \* 5-6. Therefore, the court concluded that USC was entitled to a new trial. *Id.* at \*6.

The *United Sugar* court also held that the partial summary judgment entered in favor of USC, combined with the trial court’s determination that a material fact existed concerning whether the dough was actually contaminated, compelled the conclusion that the insurer had breached its duty to defend USC. *Id.* Therefore, the court reversed the trial court’s determination that the insurer had

not breached its duty to defend and remanded the case for a determination of whether USC was entitled to an award of attorneys' fees. *Id.*

The *United Sugar* decision continues the national debate as to what can constitute "property damage" in the context of food production. Cozen O'Connor continues to opine, litigate and monitor this issue and many others involved with coverage in the context of food contamination claims. Our team of food contamination coverage attorneys are prepared to provide immediate, effective assistance. Through meetings, conference calls, seminars, coverage alerts and the preparation of papers and articles, Cozen O'Connor is prepared to assist clients effectively and efficiently handle the next devastatingly injurious foodborne contamination claim.

*For analysis on food contamination issues or how the Food Contamination Coverage Practice Area can assist you, please contact Joe Bermudez of Cozen O'Connor's Denver, Colorado office. Cozen O'Connor is a nationally recognized leader in representing the insurance industry in all coverage areas, including food contamination claims.*