

ALERT

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GLOBAL INSURANCE GROUP

News Concerning
Recent Insurance Coverage Issues



FOOD FIGHT! IS THE PCA PEANUT BUTTER OUTBREAK COVERED?

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It is one of the largest food contamination outbreaks in U.S. food history. Over 642 sickened in 44 states, including 9 deaths, and nearly 2,400 products recalled. Despite providing only 1% of the country's peanut products, Peanut Corporation of America's ("PCA") shipments of contaminated legumes to schools, institutions, government agencies and food manufacturers has caused wide-spread economic devastation. For many, the legacy of the PCA Outbreak will continue long after the investigation.

Several lawsuits have already been filed. Actions in Georgia and California have been filed on behalf of children sickened with salmonella. Another suit was filed in Minnesota on behalf of an elderly woman who consumed PCA peanut butter and, as a result, died. A fourth action filed in Virginia addresses coverage issues raised by PCA's primary and umbrella insurer.

As we have learned over the past several days, PCA knowingly and intentionally shipped contaminated products. As more damaging information from the FBI raids and the Congressional investigations is released, it appears PCA is unlikely to gain coverage from its insurers. However, the issue of coverage for dozens of PCA's food manufacturer customers raises a much more complex set of questions.

On the first-party side, many of PCA's food industry customers will seek coverage for the resulting recall losses. Over the course of the investigation, we understand that the FDA has been visiting PCA customer facilities in order to address and remediate the cross-contamination issues. These events usually result in costs associated with the temporary shutdown of operations in order to clean and contend with contamination issues. The multifaceted costs connected with the actual recall of products will also quickly mount. Loss of market and customers will result in claims. Under Business Interruption

coverage, issues such as business income, extra expense, period of restoration and loss determination will be raised by the PCA Outbreak.

Another issue raised under first-party policies is whether there has been a direct physical loss. Though many would initially assume so, there is the very real likelihood that no direct physical loss has taken place. The very same issue was involved with the Canadian Mad Cow Embargo a few years ago. Additionally, the application of certain exclusions, such as the pollution, contamination, governmental action and faulty workmanship exclusions, will effect coverage. Spoliation issues may also have a significant impact on coverage issues.

In the third party context, critical, complex issues will be raised. For PCA's insurer, additional insured claims have likely been tendered or will be shortly. Though PCA's claims are unlikely to be covered, the additional insureds do not face the same coverage hurdles. However, PCA's insurance resources are sure to fall considerably short of the mark.

With over 642 sickened in 44 states and 9 deaths, bodily injury claims from across the country will also likely be tendered. Though the acute symptoms associated with salmonella will be at the forefront of these claims, the issue of long-term effects will have to be considered. As alleged in certain of the lawsuits filed in association with the PCA Outbreak, salmonella poisoning can lead to chronic disease. Scientists are only beginning to research the possible connection between food poisoning and long-term illness. The potential long-term effects raise issues of medical monitoring claims and whether such claims are covered under traditional third party insurance. The courts that have wrestled with this issue are split.

An issue raised as to both bodily injury and property damage claims is the number of occurrences. The vast majority

of courts determine the number of occurrences by identifying the cause of the loss rather than the effect. There are an overwhelming number of potential causes involved with an international food contamination outbreak. Factors such as the number of contaminated product batches, the number of individual shipments, the respective decisions to ship contaminated products, the preparation of contaminated products and the sale of contaminated products, all may be determinative. Moreover, though many jurisdictions use the same standard, the question of whether a single occurrence or multiple occurrences took place will likely result in many different and potentially conflicting decisions.

Property damage claims associated with the PCA Outbreak will involve novel and significant issues. The threshold issue of whether property damage took place will have to be addressed. As voluntary recalls of nearly 2,400 products have taken place, the fundamental question that must be addressed is which products were actually physically injured by salmonella contamination. Insureds will also seek coverage under the product incorporation doctrine and claim related loss of use damages.

A significant number of issues will be determined by the application of exclusions. Generally, the application of several common exclusions will be addressed in the context of the PCA Outbreak. For example, the sistership exclusion is usually at issue with product recall matters. Though the exclusion appears to be applicable as to most product recall claims, certain courts have strictly construed the exclusion and narrowed its application.

As general liability policies were never intended to cover damages arising out of an insured's faulty work or product, the application of the business risk exclusions should always

be at issue in the product recall context. Specifically, the application of the damage to your product and impaired property exclusions will raise significant issues.

An exclusion that should be critically at issue in the PCA Outbreak, though most will not initially consider its application, is the pollution exclusion. The majority of courts that have applied the exclusion in the product recall context have rejected the argument that the exclusion merely applies in the industrial pollution context. An essential question to be addressed is whether salmonella is a contaminant under the definition of pollutants.

Certain policies may contain other less common exclusions that will also be applicable in the context of the PCA Outbreak.

Among another host of issues to be considered is the potential violation of the voluntary payments provision by insureds involved in the PCA Outbreak. Unless they have previously sought their insurers' consent, involved insureds may violate the voluntary payments condition contained in almost all third party liability policies.

This Coverage Alert considers only certain of the coverage issues that will be raised by the PCA Outbreak. Cozen O'Connor is closely monitoring the Outbreak and the resulting coverage issues that will be raised around the country.

For analysis on food contamination and product recall coverage issues or how Cozen O'Connor's national team of food contamination/product recall coverage attorneys can assist you, please contact Joe Bermudez, Leader of the Food Contamination/Product Recall Coverage Practice Area. Cozen O'Connor is a nationally recognized leader in representing the insurance industry in all coverage areas, including food contamination and product recall claims.

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