

Products Recall Insurance: When the Things That Go Out Have to Come Back In





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The Agenda:

- 1. Introduction: Why Talk About Products Recall?**
- 2. The "Sistership" Exclusion of the CGL**
- 3. The ISO CGL Form 00 66**
 - Coverages
 - Definitions
 - Conditions
 - Exclusions
- 4. Some Non-insurance Risk Management Tips**

Why Talk About Products Recall?

INTRODUCTION

The Most Expensive Product Recalls

(Ira Sager, Bloomberg Business 2013)

"In 2000, Bridgestone/Firestone recalled 6.5 million tires after treads separated on models used in Ford Explorers and Mercury Mountaineers.

"Ford engineers had suggested safety changes that were not heeded by either company.

"The tire failure resulted in some 200 deaths and 3,000 major injuries. Bridgestone spent \$440 million on recall-related costs; the recall cost Ford \$3 billion."



The Most Expensive Product Recalls

(Ira Sager, Bloomberg Business 2013)

"In 2004, pharmaceutical giant Merck voluntarily recalled Vioxx, an arthritis drug, after a study found that patients who took the drug for at least 18 months were prone to suffer heart attacks and strokes. At the time, the company said it expected **\$725 million in lost Vioxx sales**, which it ultimately removed from the market. In 2007, Merck agreed to pay **\$4.85 billion to settle 27,000 lawsuits** over the drug."

Aon: The long-term impact on revenue is bad because:

"A reduction in **forecasted revenue** due to lost product confidence,

"The amount of **time** needed to regain market share,

"Whether or not **market share** should be expected to reach the same levels as before the recall,

"A change in the timing of **cash flow** activity,

"Increased **marketing expenses** necessary to regain market positioning, and

"Analysts forecasts for future product sales and past performance benchmarks..."

Kozenski: Supply Chain Comment

"A May 2010 report issued by Deloitte on behalf of the Food Marketing Institute (FMI), the Grocery Manufacturers Association (GMA) and GS1 determined the average cost of a product recall to be **\$10 million**. That cost alone is enough to bring a large public corporation to its knees, not to mention the unquantifiable effect on reputation."

Tyco: Food Recall Cost Estimator

MULTIPLY retail price of food product by number of units recalled, then

ADD **four percent** for notification costs, then

ADD **ten percent** for transportation costs, then

ADD any other direct costs of recall (such as product destruction, investigation, and other costs)

Why Talk About Products Recall?

This is up from past reports. Marsh said:

"According to a study released by the American Society for Quality (August 2003), each product recall costs an organization, on average, more than **\$8 million**. This **conservative estimate** includes reimbursement expenses to consumers, recall execution costs, and compensatory damages from litigation. It does not include lost sales due to reduced marketplace credibility and lost market share."

Why Talk About Product Recall?

Product	Date	Agency
Strollers	Nov. 10, 2022	CPSC
Mini Crumb Cakes	Nov. 14, 2022	FDA / Voluntary
Generators	Nov. 10, 2022	CPSC
Hand Sanitizer	Nov. 7, 2022	FDA
Frozen Beef	Nov. 9, 2022	USDA
Vehicle Running Lights	Nov. 11, 2022	NHTSA / Voluntary

The Blue Bell Saga



www.citizensreport.org

The Blue Bell Saga

“Federal records show that Blue Bell failed to follow practices recommended by government and industry groups that might have prevented **listeria** contamination of ice cream at all three of its main plants.”

“Beginning in 2013, Blue Bell repeatedly found listeria in its Broken Arrow, Okla., facility—including on floors, a drain and at equipment that fills half-gallon containers with ice cream—indicating ***the company didn't do enough to identify the underlying cause or eliminate the source***, said David Acheson...”

Newman, *Wall Street Journal*, August 1, 2015

The Blue Bell Saga

“Blue Bell declined to comment. In May, a spokesman said, ‘**We thought** our cleaning process took care of any problems, but in hindsight, it was not adequate.’”

Newman, *Wall Street Journal*, August 1, 2015

The Blue Bell Saga

“The recall of all Blue Bell’s products threatened to destroy the 108-year-old company, which last year was the third-biggest U.S. ice cream producer, with sales in 23 states.”

“Blue Bell in May **laid off 37% of its 3,900** workers, and warned shareholders that it faced a capital crisis that could force it to close.”

Newman, *Wall Street Journal*, August 1, 2015

The Blue Bell Saga

Blue Bell was “behind the story, not in front of it; it looks as if they were forced into action”

The recall was:

- “overly complicated” and
- Cascading

Davia Temin

“[Blue Bell] seems to have taken next steps only when forced to do so by what regulators found.”

Blue Bell “completely lacked compassion...”

Jonathan Bernstein

The Blue Bell Saga

“[The apology letter] could have done more than say ‘sorry’ and ask for future support. It could have cited actions being taken to prevent future problems... and offered a customer hot line. *Social media could have given more personalized and constant information.* [Blue Bell] missed a chance to build trust, educate the public, and take bold action to guarantee food safety.”

Judy Phair, [Crisis of the Week: Ice Cream Recall Snags Blue Bell] *Wall Street Journal Blog*, April 14, 2015


The Most Expensive Product Recalls

(Ira Sager, Bloomberg Business 2013)

"One of the most publicized product recalls in history, bottles of Johnson & Johnson's **Tylenol** were laced with potassium cyanide, killing seven people around Chicago in 1982. The company spent more than **\$100 million** to recall 31 million bottles of Tylenol and relaunch the product."

Kiplinger: 10 Biggest Product Recalls of All Time

Known as “the recall that started them all,” J&J set the standard for the way corporations are supposed to handle such events. In a case of product tampering, seven people in the Chicago area died after ingesting Extra-Strength Tylenol laced with cyanide. J&J spent more than \$100 million to recall 31 million bottles of its best-selling product.



J&J's swift and decisive action is credited with saving the Tylenol brand, which at the time accounted for 17% of the company's profits. Although the stock price swooned initially, it recovered within two months.

The "Sistership" Exclusion of the CGL

STARTING THE INSURANCE DISCUSSION

The CGL and Products Recall:

According to FC&S:

“It was in 1966 that insurance companies began to add to the standard form CGL liability policy exclusions such as the sistership exclusion, which sought to eliminate coverage for activities insurance professionals believed to be **risks of developing and marketing a product.**”

The CGL and Products Recall:

“Sistership” is believed to be derived from a historical accident in the airplane industry...

...in which a plane crashed and its “sister ships” were grounded to fix the common defect that had caused the crash.

The CGL and
Products
Recall:

Exclusion (n) in the ISO CGL
carves out:

"[d]amages claimed for any
loss, cost or expense
incurred by you or others
for the loss of use,
withdrawal, recall,
inspection, repair,
replacement, adjustment,
removal or disposal of" the
named insured's 'product,'
'work' or 'impaired
property'...

The CGL and Products Recall:

Exclusion (n) continued:

"if such product, work, or property is **withdrawn or recalled** from the market or from use **by any person or organization** because of a known or suspected defect, deficiency, inadequacy or dangerous condition in it."

The CGL and Products Recall:

- The language of “withdrawn or recalled” and the language of “by any person or organization” are both significant.
- The “withdrawn or recalled” is generally construed as a limitation on the exclusion, while
- The “by any person or organization” is a broadening of the exclusion.

The CGL and Products Recall:

As to “withdrawn or recalled,” according to FC&S:

“Typically, the exclusion bars coverage for the cost incurred when a product is recalled due to a known or suspected defect or deficiency that may cause injury or damage; and it applies only to **costs incurred in order to prevent future damage/injury, not to damage/injury that has already taken place...**”

The CGL and Products Recall:

As to “withdrawn or recalled,” according to FC&S:

“If the exclusion is applicable, it does not eliminate coverage for **all damage** incurred because of the need to replace a product.

Rather, it eliminates coverage only for **damages incurred for the replacement.**”

The CGL and Products Recall:

As to “by any person or organization”:

- The language dates from 1986 and
- Is designed to combat court cases that held the exclusion applicable only to situations in which the insured recalled or withdrew the product, because
- Courts have been generally hostile to a broad reading of the exclusion.

The ISO Form 00 66 04 13

CONTINUING THE INSURANCE DISCUSSION

Moving Toward a Solution:

Prior to 2004, endorsements were available in the ISO family

These were limited in coverage, even though they were broader than their predecessors.

In 2004, ISO created a stand-alone form for products recall coverage.

The form currently is the ISO CG 00 66 04 13.

Moving Toward a Solution:

According to FC&S:

- ❑ Coverage grants and forms vary tremendously among insurers.
- ❑ Coverage is expensive
- ❑ Companies are reluctant to buy it, but should consider:
 - Size
 - Financial resources
 - Are they high profile
 - The likelihood of tampering or contamination
 - Confidence levels in internal research and development

The ISO CG 00 66 04 13:

Insuring Clause (A):

“We will reimburse you
for ‘product
withdrawal expenses’
incurred by you because of a
‘product withdrawal’ ...

Insuring Clause (B):

“We will **pay** those sums
that the insured becomes
legally obligated to pay as
damages for ‘product
withdrawal expenses’
incurred because of a
‘product withdrawal’

...

The ISO CG 00 66 04 13:

"**Product withdrawal**" means the recall or withdrawal:

a. From the market; or

b. From use by any other person or organization;

of "your products", or products which contain "your products", because of known or suspected "defects" in "your product", or known or suspected "product tampering", **which has caused or is reasonably expected to cause "bodily injury" or physical injury to tangible property** other than "your product".

The ISO CG 00 66 04 13:

"Product withdrawal expenses" means

- a. Cost of replacing "your product", repairing the "defect" in "your product" or repurchasing "your product" for your initial purchase price, whichever is less;
- b. Costs of notification;
- c. Costs of stationery, envelopes, production of announcements and postage or facsimiles;
- d. Costs of overtime paid to regular non-salaried employees and costs incurred by such employees, including costs of transportation and accommodations;

The ISO CG 00 66 04 13:

"Product withdrawal expenses" means

- e. Costs of computer time;
- f. Costs of hiring independent contractors and other temporary employees;
- g. Costs of transportation, shipping or packaging;
- h. Costs of warehouse or storage space; or
- i. Costs of proper disposal of "your products", or products that contain "your products", that can not be reused, not exceeding your initial purchase price or your cost to produce the products.

The ISO CG 00 66 04 13:

Conditions to Coverage A:

This insurance applies to a "product withdrawal" only if the "product withdrawal" is initiated in the "coverage territory" during the policy period because:

- (1) You determine that the "product withdrawal" is necessary; or
- (2) An authorized government entity has ordered you to conduct a "product withdrawal"...

The ISO CG 00 66 04 13:

Conditions to Coverage A:

c. We will reimburse "product withdrawal expenses" only if:

(1) The expenses are incurred within one year of the date the "product withdrawal" was initiated;

(2) The expenses are reported to us within one year of the date the expenses were incurred; and

(3) The product that is the subject of the "product withdrawal" was produced after the Cut-Off Date designated in the Declarations.

The ISO CG 00 66 04 13:

Supplemental Payments under Coverage B:

We will pay, with respect to any claim we investigate or settle, or any "suit" against an insured we defend:

1. All expenses we incur.
2. All reasonable expenses incurred by the insured at our request to assist us in the investigation or defense of the claim or "suit", including actual loss of earnings up to \$250 a day because of time off from work.
3. All court costs ...
4. Prejudgment interest...
5. [Post judgment interest]

These payments will not reduce the limits of insurance.

The ISO CG 00 66 04 13:

Both Coverage A and Coverage B exclude:

1. Breach of Warranty
2. Infringement of Copyright
3. Deterioration or Decomposition
4. Costs of Regaining Goodwill or Market Share
5. Expiration of Shelf Life
6. Known defect
7. Governmental Ban

The ISO CG 00 66 04 13:

Coverage A only exclusions:

1. Defense of Claims
2. Third Party Damages
3. Pollution

Coverage B only exclusions:

1. Intercompany suits
2. Contractual Liability
3. Pollution AND pollution-related loss
4. War
5. Loss of Use

Risk Management Tips

SECTION FOUR

Some Non-insurance Risk Management Tips

Lemov and Hewitt, Insuring against Product Liability, Business Law Today (1999)

Organize a formal product safety committee.

- Meet monthly, before problems arise.
- "Representatives of the major departments ...should be an active part of this committee."
- Chaired by a senior corporate official.

Target potential problems.

- Review the company's product line
- Analyze the number and nature of consumer complaints.

Some Non-insurance Risk Management Tips

“Of crucial importance is the use of realistic **pre-market testing** of the company's products. That is the area in which research and development is most useful. The R&D team can do much in terms of loss prevention by analyzing the product in terms of performance, safety, useful life and aesthetics.”

Some Non-insurance Risk Management Tips

- Know the rules. The representatives of the committee should have a general knowledge of the government regulatory and reporting requirements and notification procedures of relevant agencies
- Enlist management support.
- Communicate with employees and customers.

Some Non-insurance Risk Management Tips

- In addition, the product safety committee ...research problems that may be unique to the company's product line.
- Develop an information system.
- Conduct regular audits.