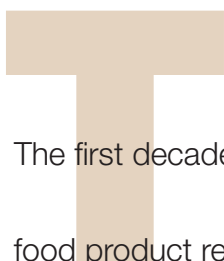


Managing Food Product Liability Risks in the New Decade

By Jonathan M. Cohen



The first decade of the 21st century saw the expansion of food product recalls and product-liability claims to an increasingly broad array of companies and industries. Many of the trends that caused product-liability concerns to grow more prevalent in the 2000s threaten to make the 2010s a decade of unprecedented product-related risk. The lessons from the 2000s, however, also provide companies with opportunities to improve their management approaches for product-related risks that the new decade might bring.

Growing Trends

One important trend in the 2000s was that a growing number of companies began to rely on increasingly broad supply chains, which in turn created new, and sometimes unpredictable, risks. This trend materialized in two key ways. First, many companies began to rely on foreign suppliers for products or product components, including those manufactured in China and other nations. For

most companies, foreign suppliers created substantially increased efficiency and improved products. For some companies, however, foreign supply chains resulted in increased exposure to product-related risks.

Most notably, companies relying on Chinese-manufactured products recently have faced significant product-liability risks arising from those products. Companies in a wide array of industries have seen recalls and claims arise from Chinese-made products, including recalls caused by the presence of lead paint on children's toys and melamine in baby formula and pet food.

Similarly, changes in the way that companies obtain components for their products even from domestic producers have resulted in significant new risks. Because supply chains have broadened, problems experienced even by small domestic manufacturers can mushroom into disproportionately widespread product recalls and claims.

For example, in the late 2000s, a small peanut-butter manufacturer, Peanut Corporation of America (PCA), allowed its product to become tainted with *Salmonella*. Although PCA manufactured only a tiny percentage of national peanut butter production, companies nationwide integrated PCA's peanut butter into their own products. As a result, those companies incurred massive recall costs and potential tort liability, and even companies with no PCA exposure saw sales of peanut butter products severely decline. Ultimately, the peanut butter industry reportedly lost more than \$1 billion.

Changes in the way that the supply chain functions have rendered some traditional risk-spreading techniques less effective. For example, many com-

panies that distribute or incorporate products manufactured by other companies historically have relied on indemnification agreements. However, products made by manufacturers in some countries, such as China, may enjoy limited liability as a legal or practical matter, limiting the value of any indemnity that they provide. Likewise, small, domestic companies with few assets and little insurance might be unable to pay their indemnity obligations. The broadening supply chains thus may significantly decrease the value of indemnification agreements.

A Time to Act

To counteract these trends, companies should support indemnities with stalwart vigilance in supervision of the production and shipment of their supplies, requirements that suppliers acquire insurance that protects the downstream company and increased attention to whether the downstream company's own insurance provides adequate protection should indemnities and the supplier's insurance policies prove insufficient.

It also may be important to require suppliers to include their downstream customers not only as beneficiaries of an insurance policy, but also as expressly named insureds that have the right to recover directly from the insurer for the downstream company's own product-related claims and losses. Frequently, smaller suppliers might welcome the opportunity to work in cooperation with their larger corporate customers to put into place adequate recall and liability insurance programs.

In addition, companies with broad supply chains must understand how a supplier's bankruptcy might affect indemnification agreements and insurance rights and proceeds. One important consequence of bankruptcy may be that companies that share insur-

ance policies with bankrupt suppliers might face the risk that the bankruptcy might freeze access to that policy until the bankruptcy is resolved. Companies potentially competing for insurance proceeds with a bankrupt supplier should examine the options to prevent or ameliorate such an outcome. One potential option would be to participate on a bankruptcy committee to ensure that the company has an opportunity to protect its rights fully. Bankruptcy also presents opportunities for mass-tort defendants. In the 2000s, bankruptcy became an important strategic tool that many product-liability defendants used.

New Risks

Besides broadening supply chains, fast-paced technological innovations also have created new product-related risks. For example, the food industry already has seen risks resulting from the expansion of the use of genetically modified seeds, plants and even livestock. In December 2009, one manufacturer of genetically modified rice was held liable to pay approximately \$2 million to two Missouri farmers after an experimental genetically engineered variety of rice contaminated their crops. That manufacturer faces hundreds more similar claims by other farmers. The insurance industry and other commentators have identified other developing technologies, such as the use of nanotechnology, as creating the potential for new liabilities.

Companies developing or relying on emerging technologies should review their insurance policies to ensure that the policies cover losses and liabilities resulting from those technologies. Generally, a company's liability policies and property damage policies cover new risks of loss unless expressly excluded. However, as the insurance industry hones in on new potential sources of loss, insurers might attempt to require

policyholders to accept exclusions or other coverage limitations intended to address those risks. Policyholders should resist new exclusionary language.

Policyholders also should recognize that insurers sometimes seek to rely on language that the insurer inserted to address one, specific risk as a basis to apply to other risks, even where the language had not been intended to apply to those new risks. Policyholders should be careful to ensure that any language that they agree to include be written carefully and narrowly.

If a claim from a new technology arises, policyholders also should be vigilant to obtain all of the coverage to which they are entitled. Insurers might attempt to rely on exclusions or other policy terms already present in many standard insurance policies to limit available coverage. For instance, carriers might try to argue that the release of genetically modified materials into the supply chain constitutes pollution that triggers standard-form pollution exclusions. Policyholders should be prepared for such arguments, and they should recognize that insurers' similar arguments have failed in other contexts.

Many of the new challenges in the 2010s likely will be extensions of trends that have been developing for many years. By learning the lessons of the past and effectively applying them to risk management, companies can avoid common pitfalls to thrive in the new decade. ■

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