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EXPERT ANALYSIS

# Insureds Find Place to Roost in Foster Poultry Contamination Case

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A federal court in California recently held in *Foster Poultry Farms v. Certain Underwriters at Lloyd's, London*, No. 14-cv-953, 2015 WL 5920289 (E.D. Cal. Oct. 9, 2015), that losses associated with alleged noncompliance with federal sanitation regulations were covered by food contamination insurance as an "error in ... production." This case illustrates the variety of issues that insureds should remember when seeking coverage for potential food contamination claims.

## BACKGROUND

In October 2013 the U.S. Department of Agriculture's Food Safety and Inspection Service ordered Foster Poultry Farms to suspend operations at its largest chicken-processing plant due to a high prevalence of salmonella and noncompliance with federal sanitation regulations. Although Foster took corrective action, FSIS found that it failed to remedy the salmonella problem and informed Foster of a further violation due to live cockroach sightings.

In January 2014, FSIS issued a notice of suspension, after which Foster ceased production for nearly two weeks. Ultimately, Foster destroyed 1.3 million pounds of chicken deemed unsafe for sale.

Foster was insured by a product contamination insurance policy issued by syndicates at Lloyd's, London. Foster sought coverage under the "accidental contamination" and "government recall" provisions of the policy for losses from the suspended production and destroyed product.

When the insurer denied coverage, Foster sued for declaratory relief and breach of contract. It then moved for summary judgment as to both claims.

The U.S. District Court for the Eastern District of California granted Foster's motion. The court's analysis focused on the parties' dispute over accidental contamination coverage, which covered "error in ... production, processing, [or] preparation ... of any insured products ... provided that the use or consumption of such insured products has led to or would lead to ... bodily injury, sickness, disease or death of any person(s) or animal(s) physically manifesting itself within 365 days of use or consumption."

The court held Foster's failure to implement federally mandated sanitation measures was an "error" in production of its chicken products, consumption of which had led and would lead to bodily injury within a year's time as required for coverage under the policy.

In resolving the parties' disagreement about the meaning of the policy language, the court addressed the type of accident as well as the nature of the danger and the type of proof required by the policy. These key issues in the analysis of food contamination claims are a common source of dispute between insurers and insureds. Below, we address the court's holding in the broader context of food contamination coverage and assess what insureds can do when faced with a potential claim.

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## TYPE OF COVERED MISTAKE OR ACCIDENT

Food contamination coverage may be available through a variety of insurance policies, including all-risk policies and specialty coverages for accidental contamination or error. The latter was at issue in the Foster Poultry case. Whether coverage is triggered depends on the policy language, which will typically differ among insurers, and the underlying facts, which are likely to differ even more among claims.

### *All-risk policies*

All-risk policies typically cover only direct physical loss and exclude damages caused by contamination. However, a standard exception to the contamination exclusion covers direct physical loss *resulting from* other damage not excluded by the policy. This exception was considered in *Leprino Foods Co. v. Factory Mutual Insurance Co.*, 453 F.3d 1281 (10th Cir. 2006). There, a cheese manufacturer sought coverage under its all-risk policy for losses resulting from a fruit juice concentrate spill at a warehouse, which caused off-flavor in nearly 8 million pounds of cheese.

The insurer denied coverage based on the policy's contamination exclusion. The manufacturer argued that the losses were covered by the "other physical damage" exception to the exclusion. It said the condition of the warehouse was the "other physical damage" that caused the loss.

Before trial, the U.S. District Court for the District of Colorado excluded evidence about what damaged the cheese because the parties did not dispute that the cheese was contaminated. Without evidence as to the cause, however, the manufacturer was effectively prohibited from presenting evidence regarding the "other physical damage" exception.

On appeal, the 10th U.S. Circuit Court of Appeals held that the District Court erred when it excluded the evidence. It said the jury required information about the fruit concentrate spill to assess whether the exclusion's exception applied. This ruling demonstrates that an all-risk policy *may* cover an insured's food contamination losses by virtue of the exception.

The court in *HoneyBaked Foods v. Affiliated FM Insurance Co.*, 757 F. Supp. 2d 738 (N.D. Ohio 2010), reached a different result. HoneyBaked sought coverage for losses related to a voluntary recall and product destruction after FSIS discovered listeria monocytogenes in ham and turkey products. The listeria was traced to hollow rollers on a conveyor system in one of HoneyBaked's facilities.

HoneyBaked sought coverage under its all-risk policy for the disposed food products and business interruption losses, arguing that the hollow rollers were the sole cause of the contamination loss Alternatively, it argued that the contamination was a "resulting physical loss or damage" covered by an exception to the policy's contamination exclusion.

The U.S. District Court for the Northern District of Ohio found that the damage was not covered because it was caused by listeria, which was the contaminant — and not by the hollow rollers, which merely harbored the contaminant.

The court rejected HoneyBaked's claim that the exception applied. It distinguished the policy's language from the provision at issue in *Leprino*, noting that HoneyBaked's exception was an "ensuing loss" provision, which "cover[s] events resulting from an excluded event which would, but for their origin in the excluded event, have been covered by the policy."

Since the origin of HoneyBaked's loss was an excluded event — contamination — and because HoneyBaked did not demonstrate that the contamination resulted from a covered event, the exception did not apply.

The *Leprino* and *HoneyBaked* cases underscore the importance of reading policies in total — especially where exclusions may be subject to certain caveats — and in context, where the timeline of events may affect the applicability of an exclusion or exception.

## *Specialty policies*

### Accidental contamination

Businesses may also be protected against food contamination loss by specialty "accidental contamination" coverage, which generally addresses the accidental introduction of a contaminant into an insured product. Foster Poultry's policy provided such coverage though it was not the focus of the insured's claim. (The clause in the Foster policy covered "introduction into an insured product of an ingredient or component that is, unknown to the insured, contaminated or unfit for its intended purpose ... provided that the use or consumption of such insured products has led or would lead to ... bodily injury, sickness, disease or death of any person(s) or animal(s) physically manifesting itself within 365 days of use or consumption.")

Generally, the policy will require the "accidental or unintentional contamination, impairment or mislabeling of an insured product" that occurred during a certain period of manufacture or distribution and has caused or would cause "bodily injury, sickness, disease, or death" within a stated time after consumption or use.

*All-risk policies typically cover only direct physical loss and exclude damages caused by contamination.*

Courts are likely to interpret such provisions to require actual contamination — meaning at least some positive test of the insured product — and will not find coverage for mere "contamination by association" with a tainted supplier's product. That was the case in *Ruiz Food Products v. Catlin Underwriting U.S. Inc.*, No. 11-889, 2012 WL 4050001 (E.D. Cal. Sept. 13, 2012), *aff'd,* 588 F. App'x 704 (9th Cir. 2014).

Many Ruiz food products used a beef spice mix received through a third-party supplier. One of the ingredients in the mix tested positive for salmonella. Although investigation confirmed that Ruiz never received mix containing the contaminated ingredient and Ruiz products tested negative for salmonella, FSIS required Ruiz to recall all products that contained the mix.

When Ruiz sought coverage for recall losses under its accidental contamination policy, its insurer denied coverage on the grounds that there was no contamination of Ruiz's insured product and mere "potential contamination" was insufficient.

The court agreed, holding that, given the negative tests, there was no "objectively verifiable evidence" that the product was actually contaminated. Without actual contamination, there was no threat of bodily injury, another key element of the policy.

Similarly, in *Wornick Co. v. Houston Casualty Co.*, No. 11-391, 2013 WL 1832671 (S.D. Ohio May 1, 2013), the court found no coverage where there were no positive test results and no incorporation of a contaminated third-party product. Wornick made meals-ready-to-eat for the U.S. government. The MREs included dairy shake packets manufactured by a third party, and in 2009 the packets tested positive for salmonella.

At the government's demand, Wornick recalled and replaced all MREs that contained the dairy shake packets. Later, Wornick determined that it never received tainted dairy shake packets, and the packets in Wornick's MREs did not test positive for salmonella.

In analyzing whether there was coverage, the *Wornick* court — like the *Ruiz* court — held that the insured product itself must be corrupted and said collateral circumstances are not enough to implicate coverage.

### Error in production or processing

Where actual contamination cannot be proved, losses may still be covered if they result from errors in production or processing — or in storage or distribution — provided that use or consumption of the product has led or would lead to bodily injury, sickness, disease or death within a set time.

*Businesses may be protected against food contamination loss by specialty "accidental contamination" coverage, which generally addresses the accidental introduction of a contaminant into an insured product.*

Such was the case in *Foster*. The court held that Foster's "incorrect" and "mistaken" implementation of sanitary measures required by federal regulations was an "error" in the production of its chicken products, as required by the policy.

Importantly, the court rejected the insurer's argument that Foster needed to further prove "actual contamination" of the chicken product to establish coverage; it said "contamination" was not an element of the error provision. This is yet another reminder of the importance of distinctions in policy language.

## NATURE OF THE DANGER

The *Foster* court also considered whether the product at issue would have caused "bodily injury, sickness, disease or death" if consumed. In doing so, it rejected the insurer's argument that salmonella does not render a product harmful because the organism can be destroyed through proper cooking. Rather, the record — which showed numerous hospitalizations resulting from the consumption of Foster's chicken and FSIS' belief that the product would cause "serious, adverse health consequences" — established that salmonella was dangerous even with proper cooking.

However, by citing to *Little Lady Foods v. Houston Casualty Co.*, 819 F. Supp. 2d 759, 761 (N.D. Ill. 2011), the court recognized that not all "contaminants" or erroneous products are dangerous. In *Little Lady* the insured's burrito products tested positive for listeria — but not for listeria monocytogenes, the only harmful strain. Because the insured's product lacked the harmful strain, the product was not "actually dangerous" and the policy did not cover the insured's recall and destruction losses.

Whether a "contaminant" or product is harmful will not always be as readily apparent as it was in *Foster* or *Little Lady Foods*, and the issue may require a jury's deliberation. For example, the court in *Hot Stuff Foods v. Houston Casualty Co.*, 771 F.3d 1071 (8th Cir. 2014), considered whether consumption of monosodium glutamate in a mislabeled product "may likely result" in sickness.

The parties' experts disagreed about whether illness was limited to sensitive populations or was more generally problematic; scientific studies were inconclusive. Given the material facts in dispute about MSG's effects and risks, the court said the coverage question should go to the jury.

As a result, the nature of a given contaminant or erroneous product is an important consideration when assessing coverage and anticipating disputes.

## TYPE OF PROOF

### *Regarding danger*

Another key question is the level of evidence the insured must produce to prove that the contaminant or erroneous product would have been harmful if consumed. In *Foster*, the court rejected the insurer's argument that the insured must produce "conclusive evidence" that "each and every one of its products would cause harm if consumed."

The court noted that an average insured would not reasonably expect to be required to meet such a heavy burden to receive coverage. Instead, the *Foster* court held "a reasonable probability of such harm occurring would be sufficient," especially since a contrary interpretation would encourage businesses to put potentially harmful products into commerce and thereby risk public welfare.

Consequently, it was enough that salmonella was linked to the Foster facility and that "egregious sanitary conditions" "may have" rendered Foster's products adulterated. This means that the inability to prove contamination with respect to every recalled or destroyed product will not necessarily bar coverage.

### *Regarding causation*

The *Foster* court also rejected the insurer's argument that Foster needed to prove a causal link between the "error" and any injury, finding that "causation" was not an element and could not be read into the policy. Therefore, Foster did not need to identify "which error or combination

of errors in its production caused the harm," "how its product would have caused the harm" or "what specific kind of harm would be caused by consumption of its product."

This is contrary to what a California state court required in *Fresh Express Inc. v. Beazley Syndicate*, 199 Cal. App. 4th 1038 (Cal. Ct. App., 6th Dist. 2011). In that case, Fresh Express recalled spinach that, at the time, appeared to be implicated in a national E. coli outbreak. Fresh Express' insurance policy covered losses that "ar[o]se because of ... accidental contamination," which included errors in production that caused Fresh Express to reasonably believe that use or consumption of the product had led or would lead to bodily injury.

The court found that although Fresh Express committed "errors" by violating some of its own internal rules, no evidence connected those errors to the outbreak, especially since another spinach producer was found to be the source.

In addition, the Food and Drug Administration was not aware of Fresh Express' errors when it issued its initial advisory that consumers refrain from eating spinach. This is in contrast to *Foster*, where the product tested positive for salmonella and FSIS identified specific unsanitary conditions that it associated with the spread of salmonella.

## CONCLUSION

The court's decision in *Foster* offers lessons relevant to food contamination cases regardless of the type of policy at issue or the underlying facts. Chief among these lessons is the importance of policy phrasing, whether with respect to the nature of the insured event, the danger affecting a consumable product or causation. Insureds should understand the implications of the provisions in their policies based on the varying factual scenarios that may present an insurance claim arising out of food contamination.



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