

# The Difference Between Manufacturer's E&O and Product Recall Coverage

There were 623,066 manufacturing businesses in the U.S. as of 2023. In fact, the U.S. manufacturing industry has grown 0.7% per year on average from 2018 through 2023.<sup>4</sup> In 2024, manufacturers are expected to face economic uncertainty based on the ongoing shortage of skilled labor, lingering supply chain disruptions, and new challenges around innovation and climate change.<sup>5</sup> Having the right insurance in place, can help ensure that manufacturers are prepared to face the future. However, for a retail insurance agent, the manufacturing market can be tough to tackle. Modern manufacturing has evolved to include complex supply chains, emerging technologies, and the risk of generating defective products leading to recalls and potential lawsuits. Like any other industry, mistakes happen in manufacturing, which means that in addition to product recall coverage, errors and omissions (E&O) insurance is also an important part of a company's risk management plan.<sup>1</sup>

In order to legally operate in the United States, manufactures are required to purchase and carry Commercial General Liability (CGL), covering the manufacturer for third-party claims arising from bodily injury and property damage. The CGL policy, however, does not respond to first party claims for financial loss and often excludes coverage for recall of products and/or errors and omissions. Coverage also will not provide pure financial loss protection to third parties, rather it must tie back to an alleged claim for bodily injury or property damage. These gaps in coverage, which can be very costly for an insured, can be filled by purchasing product recall and manufacturing E&O policies. These policies are not legally required to operate and while it may seem redundant to carry both at first glance, they cover different risks. Understanding how coverage operates independently and in tandem can ensure a manufacturer has comprehensive coverage.



**Computer/electronic products is the largest manufacturing subsector in the U.S., followed by chemical manufacturing and food, beverage, and tobacco products.<sup>6</sup>**

## DIFFERENT TRIGGERS: MFG E&O VS. PRODUCT RECALL

In general, Manufacturers E&O insurance requires that the insured control the manufacturing process. The coverage doesn't include a bodily injury or property damage trigger and serves as protection for an insured against third-party financial loss claims and lawsuits. On the other hand, recall coverage requires that a product be defective, meaning use of the product has or would cause bodily injury or property damage. However, there are times when a bodily injury or property damage condition does not need to be met in order to trigger recall insurance. For example, in the case of an impaired property event, a third-party product that cannot be used, is less useful, is unfit for, or fails to perform its intended use or function because it incorporates an insured product that is defective or fails to meet product specifications may trigger recall coverage.

## THIRD PARTY LOSS VS. FIRST PARTY LOSS

Manufacturing E&O insurance is intended to cover financial loss, damages, and defense costs the insured is responsible for as a result of a third-party claim. In contrast, product recall coverage is primarily a first-party indemnification policy providing coverage for financial loss due to a covered incident. Third-party recall liability, intended to cover a third-party's financial loss due to a covered incident, is typically included as well.



**Manufacturers account for 10.70% of total U.S. output, employing approximately 8.41% of the workforce.<sup>2</sup>**

## ERRORS VS. DEFECTS

Errors and omissions policies for manufacturing typically cover mistakes, errors, etc. in the insured's manufacturing services. The definition of professional services generally encompasses the entire manufacturing process, including analysis, design, manufacturing, marketing, integration, installation, servicing, supporting, training, software, firmware development, and maintenance of products sold by or on behalf of an insured. In comparison, product recall covers a defect, deficiency, inadequacy, design error or breach of warranty where the use of the product has or would lead to bodily injury or property damage. Recall insurance also applies to governmental agency driven recalls.

## COVERAGE PARAMETERS

Manufacturing E&O can often include coverage extensions for cyber, regulatory, pollution, recall, and replacement for additional premiums. It is important to note that many manufactured end products include component pieces/parts that were manufactured by others. Generally, the manufacturing E&O policy will not exclude products that are made up of component parts manufactured by others. However, if a claim is filed and it is determined that it is due to an error from the third-party manufacturer, the insured's policy may attempt to have the third-party E&O policy pay the indemnity. If the error was in fact first-party insured's, then full coverage would apply, regardless of which manufacturer made the component parts.

Product recall coverage generally includes defense cost, recall cost, consultant fees, expense to refund/repair/replace, as well as extra expenses. Coverage varies by carrier, but can include options encompassing forensic accounting costs, loss of gross profit, third-party recall liability, rehabilitation/product restoration cost, and impaired property.

### CLAIM EXAMPLES

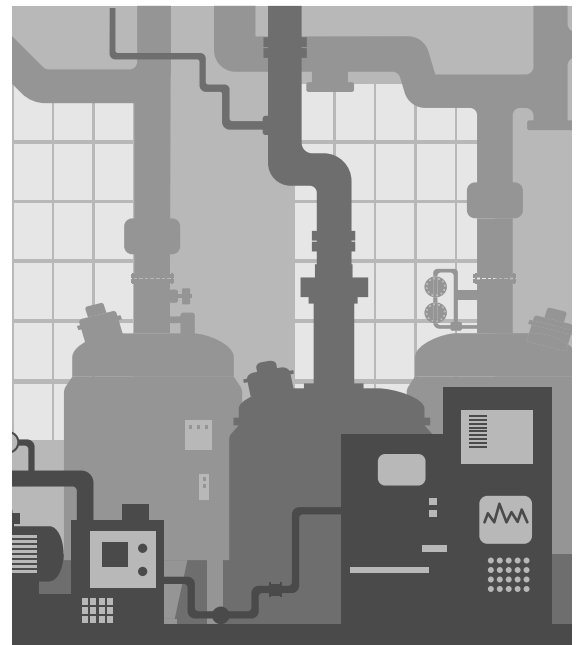
**Scenario 1:** An insured furniture manufacturer lands a deal with a national retailer. They agree to manufacture 5,000 dressers for the retailer, but the dressers show up late and with missing parts. This results in a financial loss to the retailer, for which a manufacturer's E&O can cover defense and indemnity. This scenario would not be a triggerable incident under a recall policy. The product is not defective, it was just an error on the insureds part that led to their client's financial loss.

**Scenario 2:** An insured manufacturer is hired to produce 3,000 cables for automotive brakes, each with a length of 20 inches. The manufacturer agreed and made the cables—except they were 19 inches long and therefore unusable. The customer sued the manufacturer for making the wrong-sized brake cables and alleged financial loss because of their inability to use the product. This could trigger a recall policy under the impaired property trigger and demonstrates where manufacturing E&O and recall coverage coincide. Although every claim is different, recall coverage would likely cover the first-party losses in this event and the E&O would likely pick up third-party, assuming all carriers collaborated in covering the claim.

Claim scenarios like the above don't just impact large companies. In fact, 98.6% of all manufacturing companies in the U.S. are small businesses and the majority of them have fewer than 20 employees. Although these manufacturing companies may be small, the impact they have on U.S. manufacturing is significant.<sup>3</sup> Unfortunately, for a small or medium-size business, just one uncovered claim can be enough to severely impact the company's revenue or result in bankruptcy.

### BOTTOM LINE

As the manufacturing world evolves, the need for the right insurance grows. More and more contracts require manufacturers to be properly insured. Although there may be overlap between product recall and manufacturer's E&O coverages, leveraging both help insure there are no gaps in your insured's program.



**\$2.5 trillion**  
TOTAL U.S. MANUFACTURING  
IN 2021<sup>2</sup>



**75.3%**  
MANUFACTURING  
COMPANIES WITH FEWER  
THAN 20 EMPLOYEES<sup>3</sup>

Agents that make it a point to offer all appropriate coverages can also help to protect themselves against any potential E&O claim for failing to do so.

However, the coverage is nuanced and not all policies are created equal. Every carrier approaches the coverage differently. Partnering with a knowledgeable wholesale broker can help clients avoid coverage gaps. CRC Group is home to brokers with the knowledge and experience required to help agents and insureds navigate the ins and outs of both manufacturing E&O and product recall coverage. With unparalleled market access and specialization in the manufacturing space, Team CRC's ExecPro and Casualty groups work together on risks to get the job done. Reach out to your local CRC Group producer today.

## CONTRIBUTORS

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## END NOTES

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