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APPROVAL OF THE APPELLATE DIVISION

SUPERIOR COURT OF NEW JERSEY
APPELLATE DIVISION
DOCKET NO. A-1922-12T1

TITANIUM INDUSTRIES, INC.,

Plaintiff-Appellant,

v.

FEDERAL INSURANCE COMPANY,

Defendant-Respondent.

Argued May 6, 2014 – Decided September 10, 2014

Before Judges Messano, Sabatino and Hayden.

On appeal from the Superior Court of New Jersey, Law Division, Morris County, Docket No. L-1043-11.

Robert M. Sullivan (The Sullivan Law Group, L.L.P.) of the New York Bar, admitted pro hac vice, argued the cause for appellant (Mr. Sullivan and Frederick M. Klein, on the brief).

Daniel J. Cunningham (Tressler L.L.P.) of the Illinois Bar, admitted pro hac vice, argued the cause for respondent (Mr. Cunningham and Kevin P. Sullivan, on the brief).

PER CURIAM

Pursuant to a long-term supply agreement, plaintiff Titanium Industries, Inc., a manufacturer and supplier of titanium products, sold titanium bar materials to Biomet

Manufacturing Corp. (Biomet). Biomet, a manufacturer of orthopedic implants and devices, used plaintiff's titanium to manufacture screws that were ultimately incorporated into Biomet's products. After Biomet alerted plaintiff to defects in the titanium bars, the two settled their dispute by way of a confidential agreement, only excerpts of which are in the record. Plaintiff, in turn, was able to establish that the defects in the titanium existed when shipped to plaintiff from its supplier.[1] Plaintiff reached a confidential settlement agreement with its supplier, which is not part of the record.

Plaintiff sought indemnification from defendant, Federal Insurance Company, which had issued a commercial general liability (CGL) policy ("the policy") to plaintiff for the relevant time period. Defendant denied coverage, which led to plaintiff filing a complaint seeking declaratory judgment that it was entitled to defense and indemnification under the policy, ordering defendant to reimburse plaintiff for the amount, not less than $963,000, expended in settling Biomet's claim, and awarding damages for defendant's alleged breach of contract. After discovery, both parties moved for summary judgment.

The motion record reveals the following pertinent facts.

[1] All references to the name of the supplier have been redacted from the record by the parties and its identity is not otherwise disclosed.

Brett Paddock, plaintiff's president and CEO, acknowledged in his deposition that under the terms of the long-term supply agreement with Biomet, plaintiff as seller was

> responsible for all costs and expenses of any Field Actions in respect of any Material to the extent such Field Action [was] caused by: (1) . . . ; or (2) the failure of any Material to comply with any Material Specifications or (3) the failure of Seller to comply with the Seller's Quality Management Procedures.

Plaintiff also warranted that the titanium it supplied was manufactured in accordance with applicable specifications and its quality management procedures, and that these warranties survived Biomet's acceptance of the materials. According to Paddock, a "field action" occurs when a company that manufacturers medical devices formally announces a problem and seeks to address it, including by recalling the product. Paddock also asserted in his deposition that, other than a piece of stainless steel that may have been inserted at the top of the screw, Biomet's screws were made entirely of plaintiff's titanium, and therefore plaintiff's product could not be removed from the screws.

In March 2009, Biomet notified plaintiff of a potential defect in some of the titanium material, described as "alloy segregation," i.e., the failure of alloys in a metal to completely melt causing the alloy to separate and undermine the

strength of the finished product. Biomet informed plaintiff that it was initiating a field action. The parties stipulated that the segregation issue existed when plaintiff received the titanium from its supplier, continued while the material was present at plaintiff's facility, and existed when the material was shipped to Biomet. In April 2009, Biomet initiated a recall of certain products it had manufactured using the titanium supplied by plaintiff.

Paddock also claimed Biomet informed him that some of the materials "were in fact distributed all the way through to actual implantation into patients," and thus could not be recalled. The titanium that had not been used to process a final product was returned to plaintiff, which in turn returned that material to its supplier and received "credits." None of the final recalled products, i.e., the screws themselves, were returned by Biomet.

As already noted, plaintiff and Biomet negotiated a settlement that was finalized in December 2009. The settlement included undisclosed amounts for costs incurred by Biomet related to: scrapping of the items already outsourced and made with the defective titanium; scrapping of the remaining defective screws in Biomet's inventory; employee time spent dealing with the problem; Biomet's lost profits; the amount

expended on testing the titanium; and the cost of returning the titanium.

John Ferree, who worked for defendant, handled plaintiff's claim under the policy, and, on July 23, 2009, he forwarded a reservation of rights letter to plaintiff. Ferree explained in his deposition that plaintiff's claim was not covered by the policy, because the titanium was already defective when Biomet received it, and the titanium was not added to any product which then caused property damage. Ferree also testified there was no "occurrence" under the policy because the titanium did not damage other property. Defendant formally notified plaintiff that it was denying coverage in a letter dated August 24, 2009. Specifically, the denial letter cited plaintiff's failure to allege "bodily injury, property damage, advertising injury, personal injury or occurrence as those terms are defined in the policy." In addition, defendant cited various exclusions in the policy.

Pursuant to the policy, defendant agreed to pay damages that plaintiff became legally liable to pay "by reason of liability . . . for **bodily injury** or **property damage** caused by an **occurrence** to which th[e] coverage applie[d]."[2] "**Property**

[2] When citing the language of the policy, we have included the defined terms that were set forth in bold print.

damage" was defined as "physical injury to tangible property, including resulting loss of use of that property[,]" or the "loss of use of tangible property that is not physically injured." "**Occurrence**" was defined as "an accident, including continuous or repeated exposure to substantially the same general harmful conditions."

The policy contained several exclusions. For example, "[t]h[e] insurance d[id] not apply to **property damage** to **impaired property**" or to

> property that has not been physically injured;
>
> arising out of any:
>
> defect, deficiency, inadequacy or dangerous condition in **your product** or **your work**; or delay or failure by you or anyone acting on your behalf to perform a contract or agreement in accordance with its terms and conditions.
>
> This exclusion does not apply to the loss of use of other tangible property resulting from sudden and accidental physical injury to **your product** or **your work** after it has been put to its intended use.

"**Impaired property**" was defined as:

> tangible property, other than **your product** or **your work**, that cannot be used or is less useful because:
>
> it incorporates **your product** or **your work** that is known or thought to be defective, deficient, inadequate or dangerous; or

> you have failed to fulfill the terms or conditions of a contract or agreement;
>
> if such property can be restored to use by:
>
> the repair, replacement, adjustment or removal of **your product** or **your work**; or
>
> your fulfilling the terms or conditions of the contract or agreement.

The policy also excluded coverage for "**property damage** to **your product** arising out of it or any part of it." "**Your product**" was defined as "goods or products . . . manufactured, sold, handled, distributed or disposed by" the insured, and included "representations or warranties made at any time with respect to the durability, fitness, performance, quality or use of **your product.**"

In seeking summary judgment, defendant reiterated the grounds for rejection set forth in its denial letter. After considering oral argument on both defendant's and plaintiff's motions for summary judgment, the judge issued an oral opinion. She first concluded that whether coverage existed under the policy could not be resolved on summary judgment because of disputed issues of fact regarding the alloy segregation:

> Defendant asserts that plaintiff cannot establish the requisite physical injury to tangible property, because . . . the alloy segregation condition never changed. It existed when plaintiff obtained the titanium, . . . continued to exist while the titanium was in plaintiff's possession, and

> continued to exist in the same deficient state after it was delivered to Biomet.
>
> Plaintiff . . . disputes that the physical injury derives from the so-called "alloy segregation" issue, instead plaintiff asserts that the physical injury relates to the fracturing of the screws made by Biomet as a result of the alloy segregation.
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> Therefore, disputed issues of fact exist concerning whether there is coverage under the insuring provisions for property damage which cannot be resolved on a motion for summary judgment.

Nonetheless, the judge determined that summary judgment for defendant was appropriate because even if there was coverage under the insuring provisions, two exclusions applied. Relying on the "your product" exclusion, the judge reasoned:

> [P]laintiff seeks to recover damages associated with the cost of scrapping the . . . screws in Biomet's inventory, and for screws that Biomet outsourced to other vendors for use in orthopaedic devices. There is no evidence that any orthopaedic device . . . or devices or any other medical product, were scrapped because of the defects in the titanium screws used in any such device.
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> . . . .
>
> [P]laintiff's product is not simply the titanium bars. Your product is defined in pertinent part under the policy . . . as goods, products, manufactured, sold or distributed, and includes representations regarding . . . the quality of use of your product.
>
> By that definition, plaintiff's product

here was titanium bars of a particular grade for use as pins and screws for orthopaedic devices, and it was, in fact, the pins and screws that were in issue here.

To be sure, if the pins and screws were comprised of components other than plaintiff's titanium, the screws and pins would be a different product and the inability to replace the titanium without destroying the other components of the screws and pins would alter the analysis.

There, however, is no indication that the screws or pins include any components other than plaintiff's titanium.

Therefore . . . there is no coverage for Biomet's loss of the screws and pins.

Additionally, the judge concluded that the impaired property exclusion applied:

> [E]ven if Biomet screws are tangible property, other than plaintiff's product, . . . there is no evidence supporting the exception to the exclusion, because the titanium supplied by plaintiff is the only component of Biomet screws. Therefore, the property that is Biomet['s] screws can be restored to use by supplying Biomet with the proper grade of titanium for use in the orthopaedic pins and screws.
>
> To be sure, Biomet will need to convert or process the replacement titanium bars into screws or pins. The costs associated with those efforts are economic damages arising from the failure of plaintiff's product to perform and specify. They are not costs arising from damage to other property, such as damage to the machines used in the manufacturing process, or damages associated with the destruction of other components that would comprise part of

> the titanium screws or pins.
>
> For example, it would be different . . . if we were talking here about the destruction of an orthopaedic device or medical product that had used the defective titanium screw or pin, but . . . there is no evidence in the record that such damage was sustained.

The judge did not address some of the other exclusions defendant argued foreclosed coverage. She entered two orders on November 30, 2012, one denying plaintiff's motion and one granting defendant's motion.

On appeal before us, plaintiff reiterates the arguments raised in the Law Division, specifically that its claim was "a loss" covered by the policy, and that none of the policy exclusions apply. Plaintiff therefore contends that it was entitled to summary judgment on its claims. We have considered these arguments in light of the record and applicable legal standards. We affirm for reasons slightly different than those expressed by the motion judge. El-Sioufi v. St. Peter's Univ. Hosp., 382 N.J. Super. 145, 169 (App. Div. 2005).

In reviewing a grant of summary judgment, we apply the same standard as the trial court. Murray v. Plainfield Rescue Squad, 210 N.J. 581, 584 (2012). We first determine whether the moving party has demonstrated there were no genuine disputes as to material facts. Atl. Mut. Ins. Co. v. Hillside Bottling Co. 387

N.J. Super. 224, 230 (App. Div.), certif. denied, 189 N.J. 104 (2006).

> [A] determination whether there exists a 'genuine issue' of material fact that precludes summary judgment requires the motion judge to consider whether the competent evidential materials presented, when viewed in the light most favorable to the non-moving party, are sufficient to permit a rational factfinder to resolve the alleged disputed issue in favor of the non-moving party.
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> [Brill v. Guardian Life Ins. Co. of Am., 142 N.J. 520, 540 (1995).]

We then decide "whether the motion judge's application of the law was correct." Hillside Bottling, supra, 387 N.J. Super. at 231. In doing so, we owe no deference to the motion judge's conclusions on issues of law, and review those de novo. Ibid. (citing Manalapan Realty, L.P. v. Twp. Comm., 140 N.J. 366, 378 (1995)).

Interpretation of an insurance contract is generally a matter of law subject to our de novo review. Sealed Air Corp. v. Royal Indem. Co., 404 N.J. Super. 363, 375 (App. Div.), certif. denied, 196 N.J. 601 (2008). "An insurance policy is a contract that will be enforced as written when its terms are clear in order that the expectations of the parties will be fulfilled. In considering the meaning of an insurance policy, we interpret the language according to its plain and ordinary

meaning." Flomerfelt v. Cardiello, 202 N.J. 432, 441 (2010) (citations and internal quotation marks omitted).

"If the terms are not clear, but instead are ambiguous, they are construed against the insurer and in favor of the insured, in order to give effect to the insured's reasonable expectations." Ibid. "A 'genuine ambiguity' arises only 'where the phrasing of the policy is so confusing that the average policyholder cannot make out the boundaries of coverage.'" Progressive Cas. Ins. Co. v. Hurley, 166 N.J. 260, 274 (2001) (quoting Weedo v. Stone-E-Brick, Inc., 81 N.J. 233, 247 (1979)). Whether ambiguous or not, when a court construes the terms of a policy of insurance, it "'should not write for the insured a better policy . . . than the one purchased.'" Longobardi v. Chubb Ins. Co. of N.J., 121 N.J. 530, 537 (1990) (quoting Walker Rogge, Inc. v. Chelsea Title & Guar. Co., 116 N.J. 517, 529 (1989)); see also Flomerfelt, supra, 202 N.J. at 441 ("[W]hen considering ambiguities and construing a policy, courts cannot write for the insured a better policy of insurance than the one purchased." (internal quotation marks omitted)).

"[P]olicies should be construed liberally in [the insured's] favor to the end that coverage is afforded to the full extent that any fair interpretation will allow." Hurley, supra, 166 N.J. at 273 (second alteration in original)

(citations and internal quotation marks omitted). Exclusions, on the other hand, are generally narrowly construed, and the burden is on the insurer to bring the claim within the exclusionary language. Flomerfelt, supra, 202 N.J. at 442. Nevertheless, "[e]xclusionary clauses are presumptively valid and are enforced if they are specific, plain, clear, prominent, and not contrary to public policy." Id. at 441 (internal quotation marks omitted).

If the insured fails to establish coverage, "there is no need to consider whether coverage is negated by the exclusions" in the policy. Firemen's Ins. Co. of Newark v. Nat'l Union Fire Ins. Co., 387 N.J. Super. 434, 441 (App. Div. 2006). A claim must be "cognizable under the general grant of coverage in the first instance in order" to be a claim to which the policy applies. Weedo, supra, 81 N.J. at 249.

Initially, plaintiff argues that the judge mistakenly concluded there was a genuine dispute of material fact as to whether its claim was for property damage resulting from an occurrence. Plaintiff contends there was no material factual dispute in this regard and, as a matter of law, coverage applied and its motion for summary judgment should have been granted. We agree that no material factual dispute existed regarding the nature and manner of plaintiff's claim. We part company with

plaintiff's analysis, however, and conclude, as defendant argues, that there was no coverage under the policy as a matter of law.

Plaintiff concedes a good portion of precedent upon which we rely. "The consequence of not performing well is part of every business venture; the replacement or repair of faulty goods . . . is a business expense, to be borne by the insured[] . . . ." Weedo, supra, 81 N.J. at 239. Thus, we have said that

> [w]here . . . the only damage caused by the defective product is to the product itself, contract law, and the law of warranty in particular, is best suited to set the metes and bounds of appropriate remedies. Damage to a product itself is most naturally understood as a warranty claim because the cause of action rests on the premise that the product has not met the customer's expectation.
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> [Goldson v. Carver Boat Corp., 309 N.J. Super. 384, 397 (App. Div. 1998).]

We have also noted the "critical distinction between insurance coverage for tort liability for physical damages to other persons or property, and protection from contractual liability of the insured for economic loss caused by improper workmanship."[3] Newark Ins. Co. v. Acupac Packaging, Inc., 328

[3] Here, plaintiff's claims for indemnification are solely based upon its contractual losses. They are not grounded on any tort liability of plaintiff to another party. In fact, the record is bereft of any indication that plaintiff was ever sued in a (continued)

N.J. Super. 385, 391 (App. Div. 2000). Considering a CGL policy that contained similar insuring provisions as contained in the policy here, the Court highlighted this distinction:

> While it may be true that the same neglectful craftsmanship can be the cause of both a business expense of repair and a loss represented by damage to persons and property, the two consequences are vastly different in relation to sharing the cost of such risks as a matter of insurance underwriting.
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> . . . .
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> "The risk intended to be insured is the possibility that the goods, products or work of the insured, once relinquished or completed, will cause bodily injury or damage to property other than to the product or completed work itself, and for which the insured may be found liable. The insured, as a source of goods or services, may be liable as a matter of contract law to make good on products or work which is defective or otherwise unsuitable because it is lacking in some capacity. This may even extend to an obligation to completely replace or rebuild the deficient product or work. This liability, however, is not what the coverages in question are designed to protect against. The coverage is for tort liability for physical damages to others and not for contractual liability of the insured for economic loss because the product or completed work is not that for which the damaged person bargained."

(continued)
negligence or products liability action by any patient with a hip implant containing the defective titanium, or that plaintiff ever made any settlement payments to such persons.

> [Weedo, supra, 81 N.J. at 240 (quoting Roger C. Henderson, Insurance Protection for Products Liability and Completed Operations -- What Every Lawyer Should Know, 50 Neb. L. Rev. 415, 441 (1971)).]

As we have said, "the risk of one's own faulty work is always borne by the party performing the work. That party's liability to others for its own faulty work is a matter of warranty and not a matter of insurance coverage." Hillside Bottling, supra, 387 N.J. Super. at 234.

Plaintiff seeks to distinguish this case from the persuasive precedent we cite by arguing that "[t]he property damage at issue here concerns the damage caused to Biomet's screws; not to [plaintiff's] raw titanium material." Implicit in this argument is the assertion that plaintiff's property -- the titanium bar material -- has been sufficiently transformed so that it is something else, that is, some other property that was damaged.

Plaintiff specifically argues the facts here are similar to those presented in Acupac. There, the insured, Acupac, manufactured foil laminated pacquettes containing cosmetic lotion, which were attached to advertising cards and bound into magazines. Acupac, supra, 328 N.J. Super. at 388-89. The pacquettes leaked, and, upon further examination, it was determined they were defective in that they could not withstand

the pressure of being bound into the periodicals. Id. at 389. When the customers asserted a claim against Acupac, it referred the claim to the plaintiff, its insurer under a CGL policy, which, except for the claim of "physical injury to the cards onto which the lotion actually leaked," denied the claim. Id. at 390-91.

The policy at issue in Acupac contained language similar to the policy in this case, including the general insuring provisions that incorporated the definition of property damage and an impaired property exclusion similar to the one in defendant's policy. Id. at 391-92. We distinguished Weedo, supra, 81 N.J. at 233, Heldor Indus. Inc. v. Atl. Mut. Ins. Co., 229 N.J. Super. 390 (App. Div. 1988), and Unifoil Corp. v. CNA Ins. Cos., 218 N.J. Super. 461 (App. Div.), certif. denied, 109 N.J. 515 (1987), by noting,

> unlike those cases, claims [here] were asserted for damage to property -- the cards -- that were the property of others, separate and distinct from the pacquettes prepared by Acupac. Simply put, as implicitly recognized by [the plaintiff] in correctly deciding to pay claims regarding the cards on which the lotion had actually spilled, Acupac contends that its defective product caused damage to other tangible property, not merely to intangible enhancements of the original items.
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> [Acupac, supra, 328 N.J. Super. at 398.]

We reversed the grant of summary judgment to the plaintiff-

insurer, id. at 402, concluding that

> if Acupac can establish its contention that all or a substantial portion of the pacquettes would have leaked onto the cards if subjected to the binding process, rendering the cards inutile for their intended purpose, coverage should be afforded because the cards were, for all intents and purposes, physically damaged.
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> [Id. at 400.]

The facts of Acupac are sufficiently dissimilar to those presented here so as to convince us it does not apply. The pacquettes in Acupac were attached to advertising cards not manufactured by the defendant, and which were in turn bound into periodicals not produced by the defendant. Here, plaintiff's product -- raw titanium -- was fashioned into screws, a process anticipated by the parties' relationship and the terms of the long-term supply agreement. Plaintiff's titanium was otherwise unaltered and was not appended to other property that was, itself, damaged.[4] Biomet's claims were for the breach of plaintiff's warranties regarding the intended use of its titanium, and the risk of any replacement or repair of plaintiff's faulty goods was a risk assumed by plaintiff as a cost of doing business, not a risk passed onto defendant via the

[4] Plaintiff does not contend that Biomet's attachment of non-titanium screw heads to the screws is a significant factor in the analysis. Indeed, the record contains only Paddock's hearsay claim that such may have been the process.

policy. Id. at 396 (citing Heldor, supra, 229 N.J. Super. at 396).

Instead, the facts in this case are most similar to those presented in Unifoil. There, the plaintiff, a manufacturer of foil-laminated paper used in lottery tickets, sought defense costs associated with a claim brought by the ultimate user of the paper, who alleged it was defective, and when incorporated into the actual tickets, rendered them inutile. Unifoil, supra, 218 N.J. Super. at 463-64. The plaintiff argued it was entitled to a defense under the CGL policy issued by the defendant, because its product, the foil-laminated paper, had been incorporated into, and had caused damage to, its customer's property, the lottery tickets. Id. at 469.

We rejected that claim, noting that "contract law governs the insured's responsibility." Id. at 471. "[C]overage is for tort liability for physical damages to others and not for contractual liability of the insured for economic loss because the product or completed work is not that for which the damaged person bargained. Id. at 470 (quoting Weedo, supra, 81 N.J. at 240). There was no coverage under the policy because "the damages for which the insurer was allegedly responsible, were not more than the incidental and non-injury contract damages resulting from the alleged breach." Id. at 471.

Plaintiff has brought to our attention other case law from the federal courts that it claims requires a contrary result in this case. We acknowledge those cases; however, the precedent from our Supreme Court controls our review. In short, there was no coverage under the policy for losses claimed by Biomet that were based solely upon the defective platinum supplied by plaintiff in contravention of express warranties made in the long-term supply agreement.

In light of this conclusion, we need not consider all the various exclusions in the policy. However, even if we are incorrect in our interpretation of the nature and scope of the coverage provisions of the policy, the "your product" exclusion in the policy in particular, defeated plaintiff's claim. That provision excluded coverage for "property damage to your product arising out of it or any part of it." "Your product" was defined as "goods or products . . . manufactured, sold, handled, distributed or disposed by" the insured, and included "representations or warranties made at any time with respect to the durability, fitness, performance, quality or use of" plaintiff's titanium.

Plaintiff contends the exclusion does not apply, relying primarily upon Imperial Cas. & Indem. Co. v. High Concrete Structures, Inc., 858 F.2d 128, 129 (3d Cir. 1988). The insured

in that case was a distributor of sheet steel. Id. at 130. It contracted to sell steel to a manufacturer of washers that, in turn would be heat-treated and sold to automobile makers. Ibid. After the manufacturer stamped washers out of the steel supplied by the insured, and they were heat-treated by another party, the washer surfaces developed defects and were found unsuitable for use. Ibid.

The manufacturer sued the insured for breach of warranty, alleging that the washers were defective because the steel supplied was defective. Ibid. Applying Pennsylvania law, the court held that the insurer had a duty to defend because the damage to the washers constituted property damage under the policy, and the policy's exclusion denying coverage for damage to the insured's own product did not apply. Id. at 131, 134-36. The court found that the manufacturer had "created a new product having a value in excess of the value of the product supplied by the insured, and suffered damage to more than just the insured's product." Id. at 134-35.

However, Imperial is distinguishable in the sense that alterations made by the manufacturer and others to the raw steel product were substantially more significant than those made to plaintiff's titanium, at least as explained on this record. Indeed, in Imperial, it was the heat-treatment applied by a

third party after the manufacturer fashioned the washers that exposed defects in the steel supplied. Id. at 130. Moreover, Imperial explicitly applied Pennsylvania law, and, while we need not dwell on an analysis of differences that may exist between State's law and ours, it suffices to say that the court in Imperial specifically rejected the essence of our Court's holding in Weedo. See id. at 134 n.7 (rejecting the insurer's claim that "[the] tort-oriented comprehensive general liability insurance" did not cover the insured's "contract liability").

Plaintiff also maintains that Unifoil does not control because we specifically did not rely upon the exclusionary language of the policy in reaching our decision. But that is not so. See Unifoil, supra, 218 N.J. Super. at 472 ("In sum, and after analyzing each allegation against plaintiff in the Michigan action, we determine that the claims all fall within the policy exclusion."). In this case, based upon the record that exists, we conclude that plaintiff's request for indemnification under the policy was properly denied pursuant to the "your product" exclusion. That conclusion provides a separate and sufficient basis for upholding the entry of summary judgment.

Affirmed.