

By Kenneth Ross

Protect Yourself From a Recall

With reputational and brand risk a significant concern, U.S. organizations must carefully evaluate foreign suppliers to avoid costly consequences.

In 2007, there were news stories nearly every day about new and continuing safety issues and recalls involving Chinese-made products, including food for pets and humans, car tires, toothpaste and consumer products, especially toys.

For nonconsumer products, it is hard to know how many Chinese products were recalled. And, even if we had a number, I'm sure it would be understated, because it probably wouldn't include U.S.-made products that contained Chinese component parts, or raw materials that caused or contributed to the recall.

Toward the end of 2009, a good example of the risks of buying from foreign suppliers involved the problems homeowners and homebuilders were having with Chinese-made drywall. This drywall has allegedly caused many infections and illnesses, and significant property damage. Unfortunately, homebuilders and their insurance companies have had to defend these cases themselves because of their inability to bring the Chinese manufacturers into U.S. courts. Total damages from this drywall

issue are estimated between US\$15 billion and \$25 billion.

Given the risks, there are a number of issues that manufacturers and product sellers have to consider when trying to prevent future product safety and product liability problems for foreign-made components and raw materials used in their products.

Initial Question

The first issue to consider is whether it is acceptable to purchase safety-critical products or component parts from countries with less sophisticated and robust safety, quality and legal systems. Usually, U.S. manufacturers or product sellers do not buy from foreign sources to buy better-quality products. They hope to have an acceptable level of quality and safety, but at a cheaper price.

Thus, given the increased risks and increased (but still ultimately cheaper) costs of dealing with foreign manufacturers (especially those not known for producing high-quality products), are the cost savings enough to justify the risks to people, property, the environment and the like? Given typical product profit

margins, if foreign suppliers do not take care of the entire cost, organizations could lose most or all of their profits with one product liability case or recall. And, this doesn't include damage to the U.S. manufacturer's or retailer's reputation in the marketplace.

Prevention Techniques

When buying foreign-made products, it is crucial to examine some well-known prevention techniques and see what else should be done. The techniques discussed here assume that the foreign company designs and manufactures the product. If it subcontracts any of this to other foreign companies, then supply management professionals need to consider which of these techniques need to be applied to any such manufacturers.

Contracts. U.S. manufacturers and retailers should have detailed contracts and specifications when dealing with foreign suppliers. With foreign manufacturers that have no assets in the United States, and therefore, no easy way to be sued, it is more difficult to enforce contracts in general as well as harder to deal with issues not explicitly set forth in the contract.

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Some of the issues that could be included in such contracts and specifications involve required documentation, in English, supporting certifications or other safety and quality testing, and confirmation of the foreign manufacturer's understanding of U.S. safety regulatory issues, including post-sale safety.

Insurance. Supply management professionals should also think about how they are going to enforce this contract if necessary (mediation, arbitration or litigation). Will they have to take legal action in the supplier's country? Or, will the supplier agree to jurisdiction in the United States? And, is the foreign company financially capable of paying for any recall or any deductible in an insured matter?

If the company goes bankrupt or closes its doors and the insurance premium isn't paid, the U.S. manufacturer may be the only party remaining to pay for any product liability litigation or recall. Organizations should consider requiring foreign manufacturers whose financial standing is less than stellar to post some type of bond with provisions as to when they can access the proceeds.

Design and manufacturing procedures. Safety and quality procedures for foreign manufacturers shouldn't be any different than for U.S.-based manufacturers. However, they should be rigorously enforced. It is very important that supply

management professionals know what the foreign manufacturer is doing and how it is documenting the results. This applies to engineering evaluations, such as failure modes and effects analysis (FMEA), and certifications from testing agencies.

Manufacturing issues. The manufacturer should ask the following questions as they pertain to possible manufacturing defects. What type of quality testing is the foreign supplier performing — full, partial or random? How does the supplier conclude that its product meets specifications? Does it believe that "close enough" is acceptable? Is that acceptable to the supply management organization? Also, should the organization have full-time people at the plant in the foreign country monitoring its manufacturing and quality-control processes? These issues should all be part of the manufacturer's risk assessment in determining how much safety and quality is necessary and acceptable.

Post-sale issues. The foreign manufacturer needs to have competent personnel in-house to receive and evaluate post-sale safety and quality issues. It has to agree to allow

the U.S.-based organization to review this information if it is appropriate. And there should be some agreement on when it is appropriate.

Certainly, the organization needs to be immediately notified if a component or material provided or inserted by the foreign supplier is recalled anywhere in the world. And, the organization should be sure that the supplier's personnel, or its advisers, are familiar with the U.S. governmental reporting responsibilities as they relate to defects and possible recalls. The supplier must also know the procedure for notifying the organization about the defect or recall.

Defending the product. U.S. manufacturers don't want to be put in a position where their only defense is blaming a foreign supplier. This is especially true if the supplier is not represented in the courtroom.

Thus, even while supply management professionals are evaluating who to do business with and what procedures they want a foreign supplier to adhere to, they must also think about how it will appear in court if the supplier has to defend the adequacy of its part or product. Is the supplier sincere? Can the supplier's representative speak well (preferably in English)?

Does the supplier have documents that have been written carefully and correctly, discussing what it did to be sure it produced a safe and quality product? Will the supply management organization's witnesses be able to understand and use these documents to defend the adequacy of the product or part?

It's Up to You

All of the techniques and concerns mentioned here are also important for U.S.-based suppliers. However, given the reality of problems that have occurred with foreign products, it is even more important to go the extra mile when buying outside the United States.

Ultimately, the manufacturer or product seller gets to make a business decision about who to buy from and what to require them to do. While it may be difficult to know whether or not a foreign manufacturer is taking the same precautions, the company will need to decide what the deal-breakers are. In that way, it will be better prepared to make a rational business decision and assume the future level of risk that it deems acceptable.

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