

The Risk of Contamination: Are You Ready for a Recall?

Damage to brand and reputation can be as costly as the logistical and operational expenses of a product recall

In the food industry, product recalls are everyday news: canned beans taken off store shelves fearing a bacterial contamination risk; poultry pulled from stores because they may contain possible allergens; and cashews, potentially mixed with peanuts that could cause allergic reactions, recalled from stores and consumers.

Clearly, exposure to a product recall is increasing as companies come under greater scrutiny from regulators, consumers and the media in a bid to ensure that products placed on the market are safe. The question is, however, how prepared are companies to address their regulatory requirements, handle associated recall expenses and protect vital business assets, including their brand and reputation?

Food companies not only need to ensure that their products are in compliance with applicable legislation but also be fully aware of their obligations should a problem arise. The U.S. Food and Drug Administration (FDA) has jurisdiction over food, drugs, cosmetics, medical devices and other products and serves as a monitor over product recalls. Similarly, the Canadian Food Inspection Agency coordinates food safety monitoring and recalls in Canada. Recalls are voluntary, although carried out in conjunction with government agencies, but the recent recall issues relating to imports from China have led to a call for stronger enforcement powers from the agencies. Each agency regularly publicizes product recalls to make them available to consumers.

APPROPRIATE PLANNING

For a food manufacturer, the best approach to prevent a contamination happening is to ensure that it has the right quality control systems in place. Central to this is a company's HACCP (Hazard Analysis and Critical Control Points) plan incorporating a product testing regime which needs to be constantly reviewed.

Another significant exposure to a potential loss is the supply chain. In today's global market, outsourcing manufacturing or importing raw materials may make good economic sense but it comes with risks because companies are putting their brand in someone else's hands. Critical in this process is having an appropriate traceability and recall plan in place. At a minimum the traceability plan must adhere to the "one step up, one step down" principle so that the company can immediately know both the person the product (or its ingredients) came from and the next person to whom it has gone. Being able to trace your product is a regulatory requirement and its effectiveness will be critical in recalling products.

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Food companies tend to rely on certificates of analysis that accompany supplied goods. Ultimately it is impossible to remove the supply chain risk but companies can go a long way to improving that risk by building in testing programs for supplied ingredients and products as well

as carrying out appropriate due diligence and auditing of suppliers.

LOSS SEVERITY

Assessing the loss severity for recall exposure is not a straightforward process. For this, companies need to actually go through the process of working through recall disaster scenarios and modelling can be very difficult given that there are numerous variables that can influence the size and ultimately the cost of a recall. Some companies will look at their recall loss exposure by looking at batches, lots or daily production and, based on testing cycles, create a loss scenario. This is a very useful way to estimate loss potential, but history has shown that it is often the irregular and unexpected situations that cause the largest losses.

In a contamination situation the size of the recall will depend on the amount of identifiably affected products. For example, a company that segments production into small batches, tests each batch and only releases product once test results are known will be in a strong position to prevent a severe loss happening (assuming the contamination is picked up in testing). On the other hand, a company that segments production only into daily production amounts, releases product to the market and only receives test results on those products a week later will be more exposed to suffering a severe loss because, as a minimum, it will have to recall the whole week's worth of production.

Likewise, with the supply chain risk increasing, companies could also look to

assess the potential impact of a contamination of multiple products by a contaminated ingredient. Due to their processes some companies will be more exposed to a severity loss than others but all companies should look to assess that exposure.

A sound business continuity plan will have in place contingency plans like back-up suppliers or the maintenance of spare production capacity in plants. In a recall situation, the last thing a company wants is to be left without the ability to quickly get products back on the supermarket shelves. The longer this takes the higher the potential loss of retailer and consumer confidence.

ASSET PROTECTION

The expenses involved in recalling a product can have a severe impact on a company's bottom line. In a recall situation, it is important to note that a company's General Liability (GL) policy may provide coverage against a third-party claim or product-related lawsuit. However, GL policies typically exclude expenses related to product recall losses. Representative costs associated with a product recall include business interruption, overtime and expenses for employees to handle the recall, product disposal costs, redistribution of new products, and fines paid to government agencies and expenses.

A robust crisis management plan, incorporating both a recall and business continuity plan also needs to include a strong crisis communication plan. While logistical and operational recall expenses can be costly, the damage to brand and reputa-



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tion resulting from improperly handling the situation can prove even more catastrophic. A relatively inexpensive recall can lead to a far greater impact on a company's reputation and sales if media and consumer issues are either not handled well or not perceived by the public to be handled well.

Often the business interruption loss will be limited to the amount of time it takes a company to restart production after a recall. Loss of customers and damage to the company's reputation may have a more lingering effect. This is why product contamination insurers, like XL Insurance,

see value in not only providing their clients with coverage to help pay for outside communication assistance to address a recall situation appropriately, but often offer upfront communications guidance with public relations experts to develop an appropriate plan of action before faced with a recall.

Being prepared for a crisis in advance of it happening is vital, perhaps the difference between disaster and survival.

