

Get the lead out

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For years now, lower production costs in developing countries have been a competitive advantage for many businesses. But as recent product recalls have shown, it's a strategy that requires significant attention to the potential risks involved.

Most every business seeks to build a public profile, but there are some cases where the phrase "all publicity is good publicity" does not apply.

Recent headlines such as "Boy Catches Fire After Wearing Pajamas With 500 Times The Safe Level of Formaldehyde" and "Scandal and Suicide in China: A Dark Side of Toys" are not the type that New Zealand retailers (pajamas) or American manufacturers (toys) want to see.

As retailers and product manufacturers become increasingly reliant on geographically-remote developing-nation suppliers, the risks of inferior materials or shoddy workmanship seeping into the manufacturing process also increase.

While much of what is manufactured in developing nations is undoubtedly of excellent quality and meets high standards for health and safety, the exceptions that inevitably occur can have a devastating impact on a business.

How risks have increased

While North American businesses have used offshore suppliers for generations, the risks to business are much greater today than they were even 20 years ago. There are several reasons for this:

- **Greater consumer awareness:** Consumers today are far more aware of their environment, and are taking active steps to avoid unwanted exposures. Pesticide-free lawns, chlorine-free pools, organic meats and produce these are just a few of the ways that people are showing a greater awareness of their exposure to potential toxins. This greater awareness extends to the day-to-day consumer products that people use, and even the hint of a problem can lead people to look for alternatives.
- **Increased competition:** Developing nations are just that growing and developing. And as this development takes place, the competition for business intensifies and the temptation to cut corners and costs increases. The product-quality problems that are surfacing in the Chinese manufacturing sector today stem in part from the growing pains associated with the increased competition for business.
- **More sophisticated testing:** Product testing methodology has improved significantly over the past twenty years. Testing that used to measure particles in parts per hundred are now measuring parts per quadrillion. The improvements in our ability to detect products flaws is not surprisingly uncovering a greater number of potential problems that previously would have been missed.

Costs can be significant

The harm to a company's reputation and subsequent loss of business are obvious costs that can result from product quality concerns. But there are other potential costs that could be of equal or greater concern.

If a product recall is required, there can be enormous costs to undertaking such an operation, from establishing and implementing the recall process to paying for the consumer shipping costs to send the product back.

Lawsuits are an additional concern, and not just to cover damages that have already been realized. Just recently, two U.S. class action lawsuits were filed in an effort to compel Mattel, the importer of millions of Chinese-made toys recalled due to lead paint and small magnets to pay for lead testing for children who may have been affected by the toys. So companies are being asked not only to compensate those who have suffered harm, but to pay for testing to determine whether such harm exists.

Preventative medicine

If you source or manufacture products offshore, there are a few steps you can take to help protect your business from potential liabilities stemming from quality concerns.

The first is to gain a more complete understanding of your suppliers and the suppliers they may use in the manufacturing process. Depending on your business, this could involve increased or more comprehensive product testing and reporting, site visits, or the placing of permanent staff on location.

The second is to test based on standards that are more stringent than those required by law, as standards can often toughen over time. Even if no standards currently exist for certain manufacturing ingredients and components, if you think their presence could pose problems in the future, taking a proactive approach now by using alternative methods of production could position your business well for the future.

The third is to take immediate, proactive steps to address any issues that do emerge. For example, in the 1990s, concerns about lead in Chinese-made window mini-blinds sold in Canada resulted in a retailer immediately recalling the product and reimbursing customers for the full cost. While the recall was costly, the subsequent class action that was launched against the retailer was dismissed on a summary judgment motion by the retailer when the court concluded that the retailer had taken all reasonable steps in handling the situation and no damage was shown to have occurred. WeirFoulds LLP acted for the retailer in that court action. (See *Ewaskiw v. Zellers Inc.* (1998), 40 O.R. (3d) 795 (Gen. Div.))

Finally, even if your business is not product-based, but you are sourcing professional or other services from offshore, be diligent about the standard of service and level of expertise that is being provided. As with product manufacturers, you may need to undertake a greater level of oversight to ensure appropriate standards are being met.

Questions?

If you have questions about your business risks relating to offshore sourcing or outsourcing, we can help. Please feel free to call us to consult with any member of our team.

For more information or inquiries:



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