

Exporters: Managing Product-Liability Exposures



Mr Marc Breuil, Regional Vice President - Casualty, AIG SE Asia and Greater China, looks at the product liability exposures faced by manufacturers and exporters and spells out who must buy what cover, when to buy, where to buy and how to manage the claims. An interesting read!

“A Texas jury has awarded US\$253 million including punitive damages against the US pharmaceutical company Merck & Co Inc – the manufacturer of Vioxx.” (CNN/Money, Aug 22, 2005)

Approximately US\$115 million in damages was awarded in three separate verdicts against a Taiwanese food supplier of jelly candy: each case was tried in California, USA, and involved young children having choked on the candy.

Those product-liability cases illustrate the potential catastrophic nature of the risk facing manufacturers. In Europe and in the US, managing this exposure almost always involves the purchase of products liability insurance from specialised markets.

Can Exporters' Risks Be Avoided?

It might be thought that an effective quality control system might suffice to avoid product-liability claims. In reality, it does not. In most major markets, consumer goods manufacturers and distributors can face strict liability situations when their goods cause harm to the general public. Strict liability means liability without fault. Manufacturers can be held liable without any negligence in their business conduct. It is estimated that manufacturing defects only account for 5% of US products liability cases. The vast majority of these cases either involve design defects (approximately 60%) or inadequate instructions or warnings (approximately 35%).

The toy industry is routinely exposed to costly products liability litigation. Strict liability also explains why products such as tyres are considered among the toughest exposures: tyre cases – even those involving worn-out or under-inflated tyres – frequently result in verdicts of several millions of US dollars per case.

In Asia Who Is At Risk?

Product liability claims know no boundaries or jurisdictional limitations. Asian exporters are more exposed today than ever. From a macro perspective, Asian economies have become more and more dependent on their exports or re-exports. Major distributors in Europe and the US source thousands of products from Asian suppliers including food, electronics furniture machinery parts, etc. Finished goods manufacturers buy millions of components from Asian parts manufacturer specialised in areas like electronics, phones, TVs or sound equipment. The good news is Asian products are everywhere; the bad news is so is the potential exposure.

There is no discrimination in products liability: the average products liability case in the US ends up costing approximately US\$5 million dollars between defence costs, settlements and or judgments. While the average cost of such cases is driven up by a small number of “mega” cases, scores of smaller less publicised cases routinely can involve awards of several hundreds of thousands or even millions of US dollars. Hundreds of thousands of US dollars are routinely spent on the defence of products liability cases alone. Defendant lawyers often will endeavour to have their cases settled before getting to court rather than face the uncertainty of a jury award. Indeed, 60% of the US jury awards involve judgments in the excess of US\$1 million.

Similar trends in claims frequency and severity are being observed in the UK, Australia and Western Europe where recent legislation is more and more protective of the ultimate consumers.

Exporting Goods Or Importing Products Liability Claims?

With many Asian economies being fueled by export and



trade, Asian suppliers have correspondently begun to “import” products liability suits through the products they sell overseas.

Making matters worse, product-liability litigation can affect all industries and all manufacturers – whether working in the consumer goods or business to business sectors. Whether they supply component parts, original equipment or branded goods or whether they are involved in import/exports or act as purchasing agents, anyone can be dragged into expensive product litigation.

As a result, law firms in Asia are seeing increasing number of enquiries about product labeling, product disclaimers, certification, insurance due-diligence and litigation management services, several of which are related to liability cases.

When You Apply For Cover

From a technical standpoint, product liability is a complex risk to quantify. It involves both severity and potential frequency depending on the specific products nature, its manufacturing process and the like. Preliminary underwriting information must include the sales figures broken down by sales territory and by product line. Underwriters will seek to evaluate the risk profile attached to each product, its end-users, the manufacturing quality and certification, the products defect rates, etc. Underwriters will need to check for both ad-hoc and industry-wide claims experience in order to model the risk. The underwriting process for US- and European-bound goods should be overseen by actuaries and underwriters who truly understand US or European legal environments. Each territory usually requires its own rating model and specific wordings adapted to the forums where the claims are likely to come from. What is key is understanding the jurisdiction where the actual product or component will ultimately end up.

Availability Of The Coverage

The high level of awards and the possibility of losses illustrated above lead many reinsurers to exclude US exposures from their liability treaties. As a result, many local companies prefer to avoid offering cover for US exposure. AIG understands that the export sector is vitally important to Asian economies. Even so, product-liability insurance is still often lacking in Asia. Up to 80% of the local exporters are still uninsured for products liability.

This explains why many large foreign buyers of Asian

goods impose specific product-liability insurance requirements on their suppliers. While some of the suppliers’ exposure was previously insured within the foreign buyer’s global programs or retentions, some foreign buyers are no longer willing to assume the suppliers risks or to subsidise their suppliers’ insurance budget. More importantly, they know that un-insured suppliers could be a source of bitter conflicts. In order to better manage their relationship over the long term, standard insurance requirements now call for the foreign buyers to be named as an additional insured in the supplier’s products liability policy. Cognisant of the long-term exposure of this risk, many large foreign buyers require proof of coverage from an insurer rated at least A+ by Standard and Poor’s or equivalent ratings from other main rating agencies.



Claim Handling: A Key To Products Liability Insurance

Companies providing products liability insurance for exports need to have claims handling capabilities in the territories where the goods are exported. This implies understanding local laws, culture and languages, so as to effectively represent the insured’s interests. This is most important in the more litigious territories such as the North America, Australia, Europe or even Japan. Only then can they adequately defend both the supplier’s interests and the distributor’s interests. Exporters can benefit from an insurer with a comprehensive and internal claims network and avoiding those who purely defer claims handling to third party adjusters. In complex products liability cases as those found in Europe and North America, exporters can save time and money by relying on an insurer with a network of experienced claims professionals familiar with product-liability litigation. Choosing the right defence, finding the right experts and lawyers, knowing when to settle, and for how much are critical to the outcome of the case. This requires product-liability specialists in investigations, assessment and representation.

Warning: Are You Adequately Covered?

Product-liability insurance is only part of the solution. Exporters need to invest both management time and resources into several key risk-management areas. Particular attention must be given to product certifications and quality control practices: using outside laboratory tests can be one way of achieving this.

Users’ manuals and instructions must be compliant with export markets standards. Labels and warnings must be reviewed from both a legal and technical perspective. Labels, for example, must be readily visible and durable and contemplate types of potential misuse of the products.

Exporters cannot avoid products liability exposure: it is merely a question of time before claims are made and potential losses arise. ■

