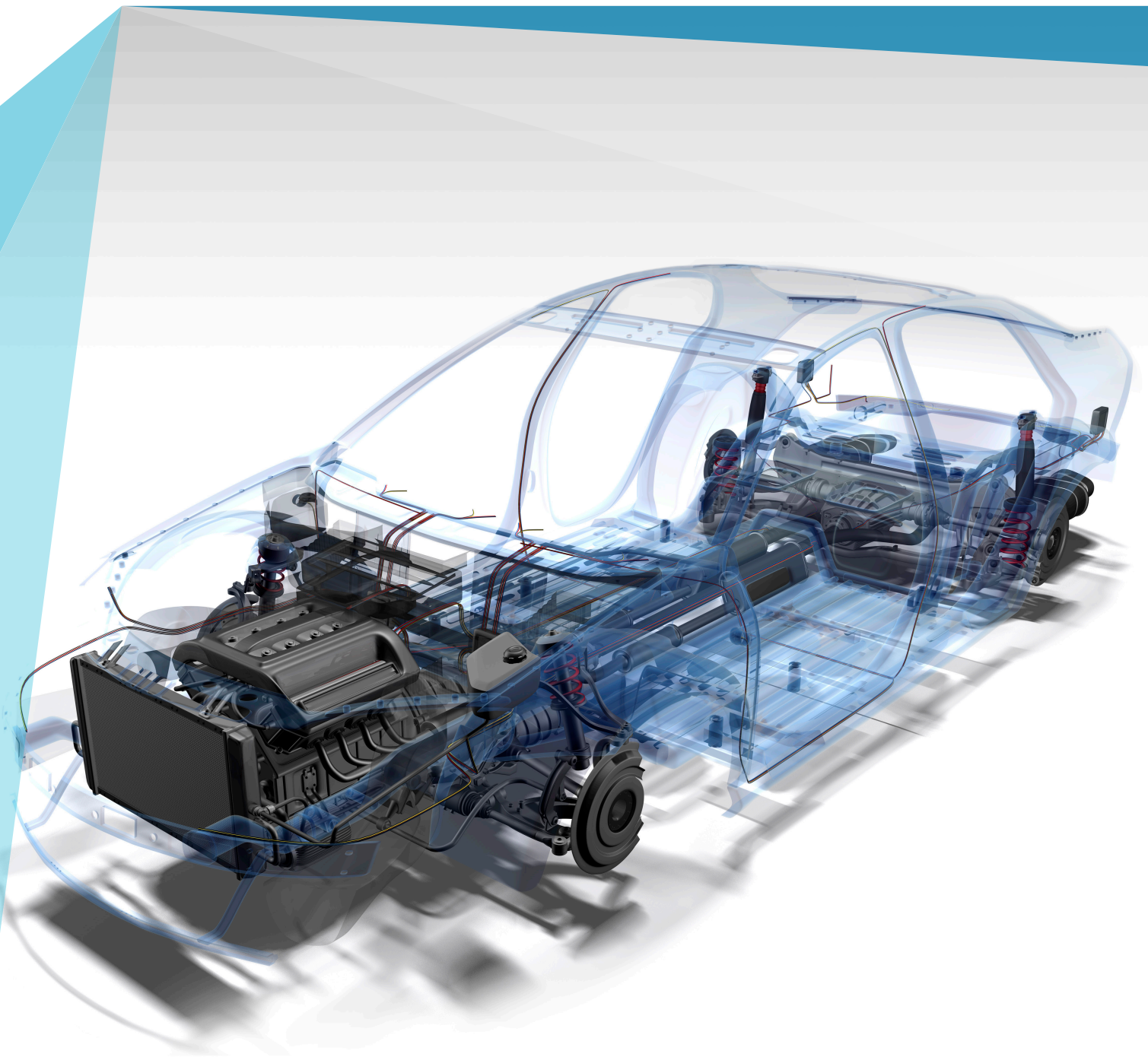


# PRODUCT RECALL SOLUTIONS FOR AUTOMOTIVE COMPONENT SUPPLIERS





## BACKGROUND

Automotive recalls are on the increase, and the number of cars being recalled each time is soaring.

There is no single reason for the automotive recall trend, but growing technological advancements and innovation is a major factor. The greater the complexity of a vehicle, the greater the scope for something to go wrong.

Multi-platform parts generate significant production savings, so if a part fails, the recall is potentially many times greater than it would be if a part was specific to just one model.

There have been a number of high-profile global recalls following multiple deaths as a result of manufacturing faults. Some manufacturers have faced billion dollar fines, and criminal negligence charges for allegedly “covering up” faults.

These cases have increased the automotive market’s sensitivity to recalls, and faults and failures that might in the past have resulted in a “service fix” are now the subject of a full recall campaign.

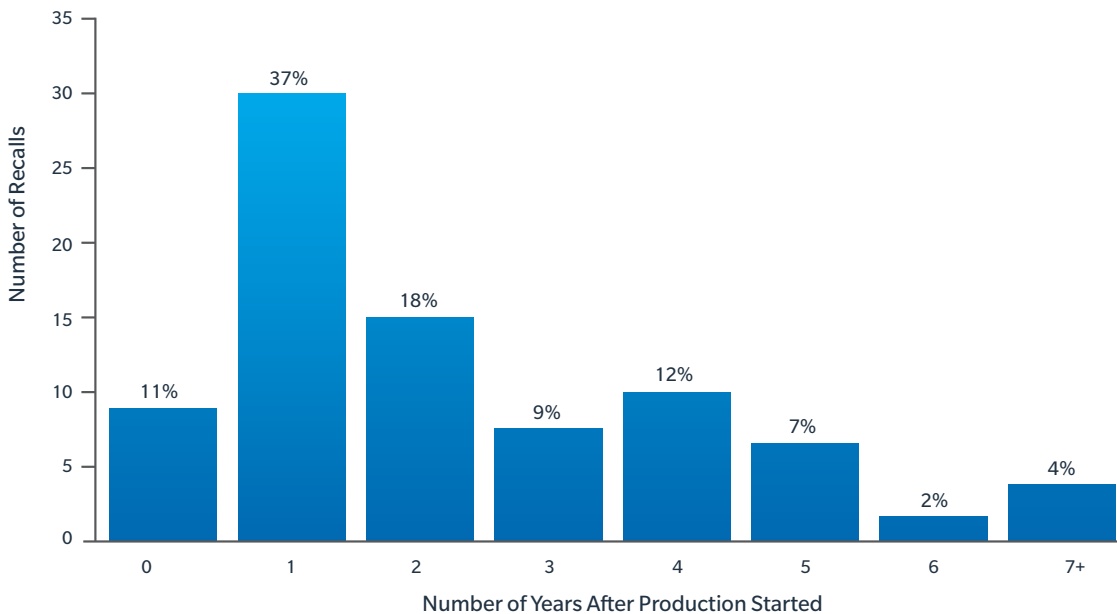
Car manufacturers need to be prepared to face up to every aspect of a product recall in order to protect their brands, corporate reputation, and balance sheet.

## TRENDS, PATTERNS, AND EMERGING ISSUES

Research suggests that there is a considerable time-lag between the point that a vehicle has been registered and when recall incidents occur. Figure 1 from Vehicle and Operator Services Agency (VOSA) shows how many recalls may occur in the build year and then in the following years post-registration. Almost 50% of recalls are initiated a year or more after the vehicle has been built.

Automotive recall insurance policies can be placed with long-term agreements, which can see clients benefiting from no-claims discounts year on year. In addition to this, clients can opt to pay for a longer retroactive date, which would provide cover for products manufactured prior to purchasing a recall policy.

FIGURE 1: NUMBER OF RECALLS AFTER BUILD YEAR



Recall reports in relation to build year of vehicles affected (Example of Ford, All models, UK, 1/1/2000 – 31/12/2013)  
Data source: VOSA (2014) “Vehicle Recalls Search”

# GLOBAL SUPPLY CHAIN

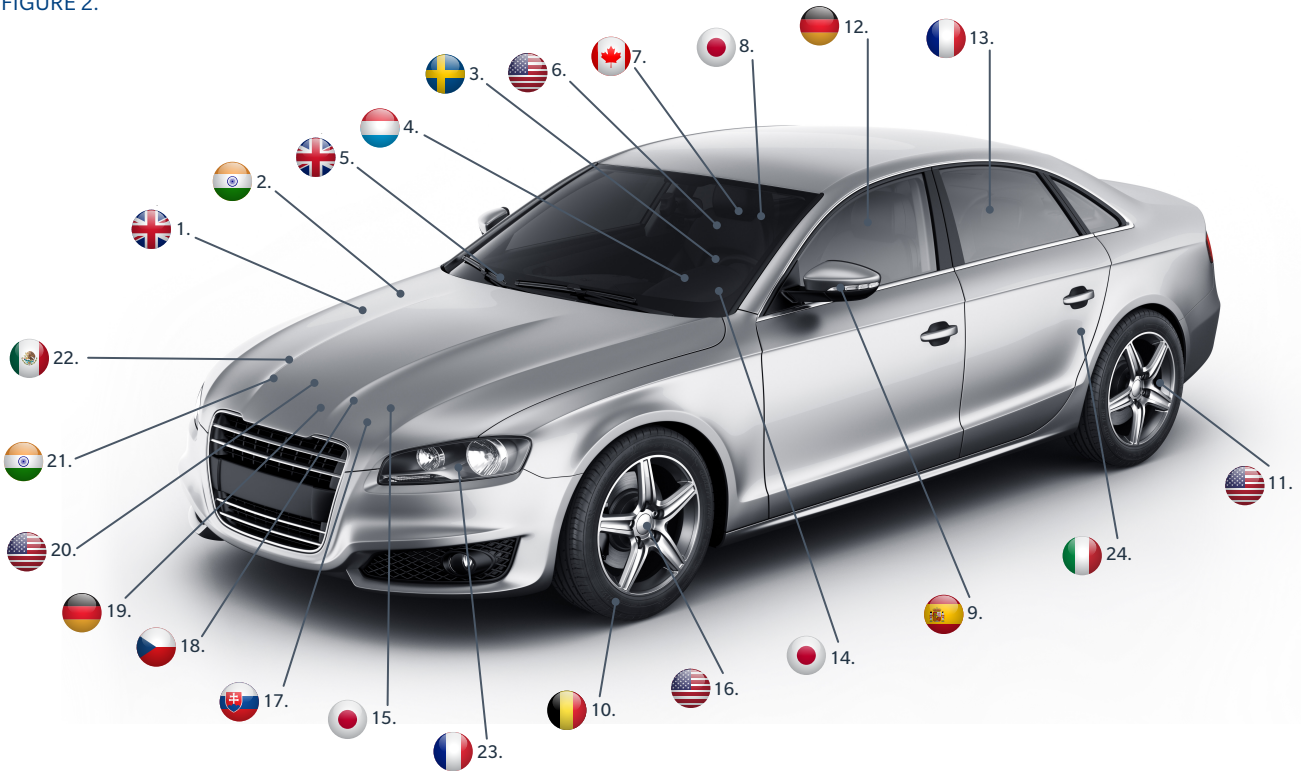
The average road car is made up of approximately 1,800 separate parts<sup>1</sup> (approximately 30,000 components in total<sup>2</sup>) most of which car manufacturers, or assemblers, source from around the globe.

The supply chain is truly international, and potentially a car manufacturer won't know who the materials supplier is at the

foot of the supply chain, let alone have audited its quality control and traceability. It is difficult to identify an unscrupulous supplier using cheaper sub-standard materials, or even counterfeit parts.

Figure 2 illustrates where a number of key automotive components in an average car might originate.

FIGURE 2.



- |  |   |  |
|--|---|--|
| <ul style="list-style-type: none"> <li>1. <b>UK</b> – Designs and manufactures chassis and engine components.</li> <li>2. <b>India</b> – Chassis and engine components.</li> <li>3. <b>Sweden</b> – Airbags, seat belts, safety electronics, steering wheels.</li> <li>4. <b>Luxembourg</b> – Interior trim – instrument panels.</li> <li>5. <b>UK</b> – Small motor window wipers.</li> <li>6. <b>USA</b> – Interior seating.</li> <li>7. <b>Canada</b> – Interiors.</li> <li>8. <b>Japan</b> – Interior trim.</li> <li>9. <b>Spain</b> – Exterior mirror systems.</li> </ul> | <ul style="list-style-type: none"> <li>10. <b>Belgium</b> – Safety and control systems; braking, stability and transmission automation systems.</li> <li>11. <b>USA</b> – Magnetics and magnetic assemblies.</li> <li>12. <b>Germany</b> – Interiors.</li> <li>13. <b>France</b> – Seating, emissions control technologies, interior systems, exteriors.</li> <li>14. <b>Japan</b> – Instrument panels.</li> <li>15. <b>Japan</b> – Body, brake and chassis systems, electronics, drivetrain and engine components.</li> <li>16. <b>USA</b> – Machines rotors and drums.</li> </ul> | <ul style="list-style-type: none"> <li>17. <b>Slovenia</b> – Forgings for chassis and engine components.</li> <li>18. <b>Czech Republic</b> – Sealing systems.</li> <li>19. <b>Germany</b> – Coatings, catalysts, engineered plastics, polyurethanes, coolants, brake fluids.</li> <li>20. <b>USA</b> – Power train and wheel end applications.</li> <li>21. <b>India</b> – Fuel injectors.</li> <li>22. <b>Mexico</b> – Aluminum cylinder heads, engine blocks and transmission.</li> <li>23. <b>France</b> – Headlights.</li> <li>24. <b>Italy</b> – Suspension system.</li> </ul> |
|--|---|--|

1. Source: CS Monitor (2007) "Vrrrooom! What does it take to build a car?"  
 2. Source: Toyota (2014) "Production and Sales"



# CONTRACTUAL PRESSURE

Most supplier contracts with an original equipment manufacturer (OEM) will contain a provision that relates to recall liability. Typically it will simply make the supplier responsible for the costs incurred by OEMs when running a recall campaign. Often it will go further and require that a third party insurance policy is in place, sometimes even stipulating the limit.

Historically cover has only been provided to cover legal liability between suppliers and purchasers. However, cover is now provided based on contractual liability.

# REGULATORS

Original equipment suppliers have a legal obligation to report safety defects to National Highway and Traffic Safety Administration (NHTSA), and other national regulatory bodies as reflected in figure 3.

FIGURE 3: LEGAL OBLIGATION TO REPORT SAFETY DEFECTS TO NHTSA

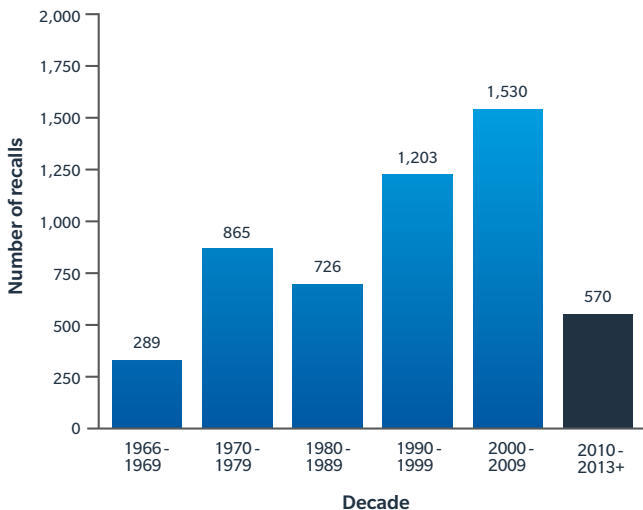
Safety Related	Emission Related	Non Conformance	Product Rework (Non-Safety)	Customer Satisfaction Update
<ul style="list-style-type: none"> <li>Legally required.</li> <li>Driven by risk assessment and governmental bodies.</li> <li>Criteria: harm to life or risk of injury to passengers or third parties.</li> <li>Example: parking brake might not work properly.</li> </ul>	<ul style="list-style-type: none"> <li>Legally required (for Euro 1-6 emission levels).</li> <li>Driven by large numbers of vehicles failing emission tests or product related mis-design that fails emission regulations.</li> <li>Very rare.</li> </ul>	<ul style="list-style-type: none"> <li>Legally required.</li> <li>Driven by legal requirements, e.g. to mark a vehicle properly.</li> <li>Example: missing or wrong vehicle identification number, missing airbag stickers.</li> <li>Often not expensive and quite rare.</li> </ul>	<ul style="list-style-type: none"> <li>Large segment.</li> <li>Rework components before they fail.</li> <li>Driven by high number of failures with significant customer satisfaction impact.</li> <li>At OEMs discretion.</li> <li>Government bodies can be involved.</li> </ul>	<ul style="list-style-type: none"> <li>“Silent recalls”, fix at the next workshop stop.</li> <li>Same as reworks, but without any publicity.</li> <li>Largest segment of reworks in the field.</li> </ul>
<b>Legally required</b>				

Source: SGS

# STATISTICS

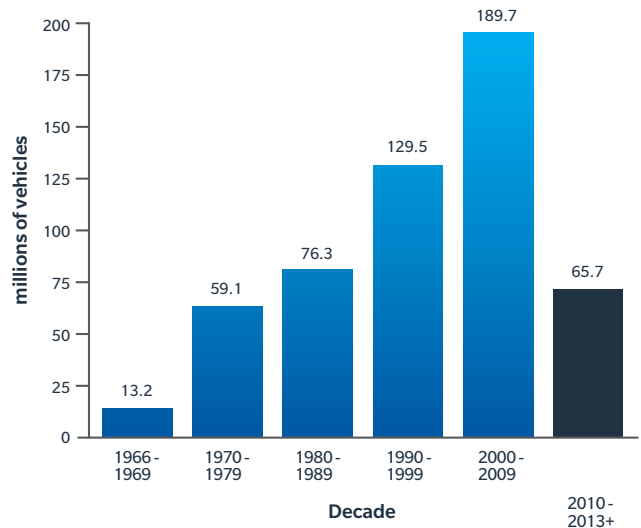
Figures 4 and 5 highlight the increasing trends in the number of recalls since 1966, as well as the increasing number of individual vehicles recalled in each decade up to 30 September 2013.

FIGURE 4: VEHICLE RECALLS BY DECADE



Source: Automotive News (2013), “Total Recall”

FIGURE 5: VEHICLES POTENTIALLY AFFECTED



Source: Automotive News (2013), “Total Recall”

## 2014 HEADLINES

The first six months of 2014 saw almost 40 million vehicles recalled, surpassing 2004's previous full record year record of just over 33 million<sup>1</sup>. With increasing consumer scrutiny on car makers it is not surprising, and managing this risk is becoming a focal point for the industry.

## SOLUTIONS

At Marsh we believe that risk transfer and risk management together offer the best solution. Risk management helps to prevent and mitigate a recall incident. Risk transfer helps to protect the balance sheet against the major financial impact that a recall can bring.

We have access to an established insurance market that provides comprehensive cover on both a first and third party basis.

## AVAILABLE COVER INCLUDES:

### PRODUCT GUARANTEE

The trigger to the policy goes beyond a fault that could lead to a safety issue (bodily injury/property damage). Cover is instead based on a component failing to perform its intended function, whether that is through poor workmanship, materials, or design.

### FIRST PARTY RECALL COSTS, INCLUDING (BUT NOT LIMITED TO):

- Transportation.
- Additional staffing.
- Redistribution.
- Destruction.
- Recall notices and communications.
- Business interruption (by endorsement).
- Defence costs.

### THIRD PARTY RECALL COSTS, INCLUDING (BUT NOT LIMITED TO):

- De-installation and re-installation.
- Replacement parts.
- Repair or refund.

### THIRD PARTY FINANCIAL LOSS

A client's legal liability to pay the financial loss (business interruption, or loss of profit) of a customer.

## GOVERNMENTAL RECALL

In most countries the highways agencies have the authority to force manufacturers to recall vehicles that present safety issues, or do not meet industry standards. There is cover available that responds to a forced recall.

*(For policy details of any of the mentioned forms of cover, please request the policy wording).*

## BENEFITS OF AUTOMOTIVE RECALL INSURANCE

- Cover is available retroactively, for parts manufactured prior to inception.
- Cover is available for motorcycles, passenger cars, light commercial vehicles (LCV), heavy commercial vehicles (HCV), and after-market parts.
- All automotive parts, including "safety critical" can be covered.
- Single contract(s) can be covered, rather than basing premium on whole turnover.
- Cover is on a worldwide basis, both overseas sales, and manufacturing.
- Can include contract manufacturers.
- Coverage available where safety related, regardless of whether the insured product is installed.
- Fixed premiums rather than adjustable at the end of the policy period.

## RISK MANAGEMENT

Most insurers in this class provide a 24/7 response hotline from automotive industry recall specialists, who clients can call in order to assist in managing a recall incident.

The right support and advice can be critical in the early stages of a crisis. The capabilities on offer range from recall logistics and testing, through to media crisis communications.

The majority of Insurers also partially fund risk management and quality control projects in order to reduce the likelihood of an incident.

## MARKET CAPACITY

- Up to USD100 million.

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1. Source: The Detroit Bureau (30 June 14) "U.S. Automakers Obliterate One-Year Recall Record... In Six Months"

## MARSH GLOBAL RECALL SPECIALISTS

Marsh has a global product recall team with over 50 years of experience in this class of insurance. Spread across the globe, with hubs in the United Kingdom and North America, the team has designed and placed insurance programmes for some of the largest and most well-known brand owners, advising on key issues such as supply chain, brand and reputational risk. In addition to the placement team, the recall team can call upon experienced and dedicated claims handling personnel who will manage a claim on behalf of a client, from initial notification through to settlement.

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