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Recalls – When the Worst Happens

Summary

This paper covers how to manage risk when quality control procedures fail and there is no recall contingency plan. Long-term brand impact, operational response, communication strategies, and the cost associated with various recall options are detailed.

The mere word “recall” can send a shudder all the way through a company, from the receptionist to the executive team, to the boardroom and shareholders. Recalls are costly and risky and can threaten the existence of a company.

How a company reacts to a recall can determine whether the company gets through the incident fairly unscathed — or even not at all. It is all about minimizing corporate exposure and maintaining customer satisfaction.

Prevention and Preparedness

As with any such incidences, prevention and preparedness are key elements. While this is scant consolation to the companies subjected to a recall, this White Paper would not be complete without mentioning these two aspects.

Prevention is, of course, related to quality control, failure analysis, and supply chain management. Strict control from the design stages of a product to delivery would have prevented most recalls. Product recalls are frequently caused by the product being designed without proper consideration for the use and the dangers it may pose. In a rush to market, the product is not properly tested or evaluated. However, as is commonly seen today, a recall can be caused by even one small failure in the supply chain.

As supply chains become increasingly complex, the risk of failure goes up exponentially. Raw materials from subcontractors to a subcontractor to a subcontractor can be consolidated in one part of the world, used in another part of the world for a subcomponent, then stored and shipped to a third continent before being used in the final product – eliminating the likelihood that the buyer of the final component has a chance to review the supply chain risks. A risk assessment of the supply chain is a major aspect of recall prevention.

But even if recalls cannot be prevented, being prepared with a contingency plan is absolutely crucial (for a free contingency plan template, please contact ALOM or see other sources at the end of this White Paper). The contingency plan includes: vendors; legal advisors; compliance team members; a PR agency; call centers; the Web design team; the executive team; and information and authority levels to guide the recall team to move ahead in a fast, controlled manner.

However, most companies simply are doing business without a recall contingency plan.

Forced or Voluntary Recalls

Recalls can be initiated and implemented by authorities as a forced recall or by a company as a proactive step to prevent authorities from issuing a forced recall or just to ensure that customers have a working, safe product. Authorities that can force a recall in the U.S. include the Consumer Products Safety Commission (CSCP), the FDA, the National Highway Traffic Safety Administration, the U.S. Environmental Safety Protection Agency, the USDA Food Safety and Inspection Service, and the United States Coast Guard. The forced recalls mainly take place when the hazards are both serious and fairly likely to happen. Several agencies have a Fast Track program for companies that issue a voluntary recall, cutting down on the required paperwork. The Fast Track programs typically allow a company to complete the recall in an easier, less bureaucratic manner. The CPSC, Office of Compliance, has issued an excellent booklet about recalls.

Recall Impact and Cost

The impact and cost of a recall can be broken into several groups:

- Cost of customer dissatisfaction/avoidance
- Long-term impact on brand
- Operational cost of recall
- Potential litigation cost

The following will outline these impacts/costs as well as how the cost can be contained.

Cost of Customer Dissatisfaction/Avoidance

For most companies, customer satisfaction and customer retention are key to running a profitable business. Any situation where the customers feel they received and paid for a substandard product represents a significant threat to customer satisfaction. The key — that many executives are not getting — is the perceived injustice by the customer. The product may be functionally sound, but if it is perceived to have a significant flaw, it can certainly impact the customer's satisfaction.

In addition, during a recall a company typically asks customers to respond with their own time when getting the product fixed. This can be as simple as returning the product for a new replacement or having the customer re-install a component. The replacement product may furthermore be cumbersome to re-install, as is typically the case with technology products.

Several steps can be taken to improve the customer experience and lessen the impact of a recall:

React fast

As customers hear about the recall, they get concerned and frustrated about what to do with their potentially unsafe product. Speed is really important.

Make it easy for your customers

Make the return or the replacement easy. This includes both the logistics part and the reporting part. This is not a good time to question the honesty or to test the relationship with the customers. Avoid anything that could further enrage the customer. Prevent: long holds on toll-free-numbers; confusing information on your Web site; poor customer interface for online reporting or troubleshooting; cumbersome forms to fill out; and putting the burden of proof on the customer. Instead, review what a great customer experience would entail. For instance, companies can consider sending customers a replacement unit before receiving the original product back instead of waiting to receive the customer's unit prior to shipping a replacement unit. This tactic allows the company to include the return packaging and prepaid label with the replacement unit, making the return very convenient and free for the customer.

Make sure that it is done right

A recall is not a good time to make errors since the customer relationship is already fragile. The order must ship right, work correctly, and arrive in perfect condition. Any refund must be prompt and correct. Impeccable quality of customer interaction becomes a must. This is especially hard for companies where customer interaction is usually not prompt, not very efficient, or generally not of high quality. Internal staff is not trained to provide the high quality interaction needed, and the vendors used are mostly selected for cheaper price. Now is not the time to cut corners with a cheaper, inexperienced vendor.

Understand emotions

Customers feel that the contract has been broken. They paid for a good product, and they either received a bad product, a potentially defective product or – worst case – a dangerous product that may even be life-threatening. This is not – obviously – a normal business transaction. It is a transaction where the recalling company has broken trust, and it must work hard to reestablish the trust. This attitude must permeate everyone who is involved in the recall.

Long-Term Impact on Brand

Recalls have always had a negative effect on brand equity. However, as viral marketing – and online communities – are taking on a life of their own, the brand can suffer irreparable damage within just weeks – or even days. Even false accusations can have that effect, as Wendy's can attest after having to fight the incident in which a customer put a severed finger into a bowl of food, an incident that impacted the company for years.

Customer dissatisfaction at a very basic level "only" involves a transaction between a company and a person and/or another company. We are not making light of that relationship. Current customers are the lifeblood of any company – and the most likely to buy again. However, the long-term brand involves more than the specific sum of the customer transactions and perceptions during the recall.

Damage to the brand can make it unlikely that anybody ever will buy that brand. Perceptions can change overnight as talk-show hosts use the name in their jokes.

The only way to protect the brand during a recall is to react quickly, considerately, honestly, transparently, and with integrity.

Operational Impact and Cost

The table (Table 1) illustrates different customer-related actions that can be taken as part of a recall, as well as the expected impact and the cost. Both will vary depending on product and the overall scenario.

Recall committees would do well to consider a cost/benefit analysis. The proverbial pound-wise/penny-foolish discussion comes to mind. A recall can easily cost $50 - $500 per unit shipped , of which maybe 5% - 20% (or $10-$25) can be attributed to the actual interaction with the customer, such as call center interaction, operational transactions when receiving the old unit or shipping the new unit, and freight. A 10% savings in this area may have very little impact on the overall cost of the recall, but may have a huge impact on the image of the company, customer satisfaction, and the long-term consequences.

Table 1. Operational Impact and Cost

	Impact	Cost	Notes
Effective public communications	High	Medium	Cost may vary. This could encompass different types of communications from the more passive press releases to actively monitoring and impacting viral marketing
Effective customer communications/recall w. direct communications to impacted customers	High	Medium (note: cost of maintaining a high-quality customer database may be high)	
Responsive call center/chat room	Medium	Low	The cost difference between a high-quality responsive call center and a less-responsive call center is marginal compared to the potential risk
Easy to locate and navigate/use recall information on Web site	Medium to high	Low	
Communications through sales channel	Medium to high	Medium	
Fast and easy processing for replacement of product	High	Varies	Cost can be kept minimal if few questions are asked
Plug & play replacement unit	Varies	Varies, may not be applicable	
Free return shipping	Medium	Varies, low in most cases	
Overnight shipment of replacement unit	Varies depending on product type	Varies, low in most cases	
Offering a full refund	High	Varies	If no replacement units are available, the refund may be the only acceptable solution
Proper refurbishment of units	High	Medium	If sending out replacement units that are refurbished from returned units, the refurbishment must be done flawlessly to avoid compounding the problem
Sensitivity to stored data when dispositioning defective product	High (note: cost of not doing may be high)	Medium	Return units may have stored data that is sensitive, such as medical information
Environmentally responsible disposition of defective product	Medium	Low	Since this is a high-profile situation, it is dangerous to add to any negative perceptions

Costs – The Entire Picture

While transaction-based costs are obvious there are several expenses that are less obvious;

Managing the recall. The recall must be managed by very competent staff with full authority, full access to the resources needed, and knowledge about product, supply chain, customers, sales channels, etc. This makes for a very expensive, highly-paid committee.

Compliance management. The cost depends on whether the recall is voluntary, whether a Fast Track option is available, and which agency the company is interfacing with. In addition, public companies have reporting requirements with shareholders having a legitimate interest in information.

Corrective Action. As the legal, communications and practical aspects of the recall gets planned, it is time for learning and correcting. It is important to start the process early so relevant information can be collected as defective or non-defective units are returned. Statistical analysis should be performed and communicated throughout the company.

Suppliers. If the recall is caused by problems in the supply chain, a complete analysis of the supply chain may be necessary. As supply chains get exceedingly complex, this may be very time consuming and costly.

Opportunity cost. As senior staff focus on the recall, other issues may be unattended to. However, just as important is the sales force. To avoid a demoralized sales force, the recall committee must communicate fast, clearly, and honestly with the sales force, providing specifics about what the company is doing, and how the company intends to move forward.

Communications management. The company should perform a complete stakeholder analysis to review that it has communicated appropriately with each stakeholder. This could include vendors who might be concerned about the company's cash flow or survival, service providers who may have to provide changed services during the recall period, public service announcements, employee communications, non-affected customers, as well as the general public.

Repositioning the brand. On the marketing side, serious consideration must be given to the brand to ensure its survival or comeback.

Potential Litigation Costs

In addition to the cost of managing the recall, companies are faced with the risk of litigation, either in the form of individual lawsuits or class action lawsuits. Risk mitigation becomes a legal issue, which also includes the issue of whether a jury would see the company as "doing the right thing."

Litigation costs can surmount other costs and can ultimately be detrimental to the company's survival. Certainly, any litigation involves distraction from the company's business. In addition, punitive and other damages can be substantial.

The costs spent on mitigating customer issues and taking action fast can easily be recovered in minimized risk of lawsuits – or minimized risk of punitive damages.

Legal advisors should be on any recall team and readily available.

A Final Word About Managing Your Recall

Recalls must be managed by high-level staff inside a company. However, it may be very productive to use high-level, trusted service providers to implement many of the recall functions. In fact, internal resources often get over-taxed during a crisis situation, causing a drop in service and customer dedication.

Other sources:

CSCP – Consumer Products Safety Commission (www.spscs.gov)
FDA – Food and Drug Administration (www.fda.gov), for policies, see vm.cfsan.fda.gov/~lrd/recall2.html
Reverse Logistics Association (www.reverselogisticstrends.com/index.php)
Center for Business Intelligence, Recall Conference (www.cbinet.com/conferences.cfm)
American Society for Quality Control, The Product Safety and Liability Prevention Technical Committee (PS&LPTC), (www.asq.org) has published a book 9 (www.asq.org/qic/display-item/index.html?item=10181)

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