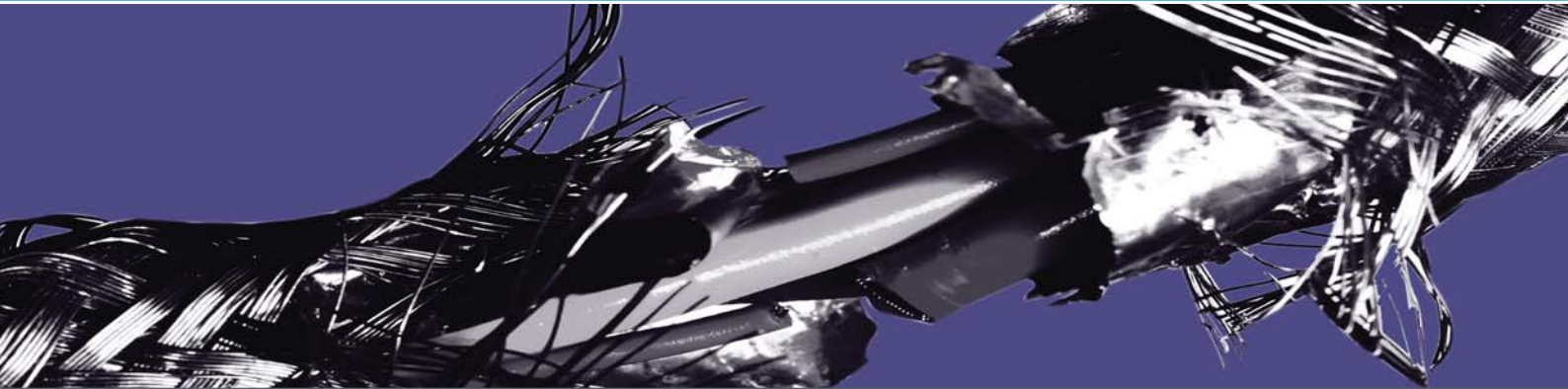


# lifescience &chemicals

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## SUPPLY CHAIN AND LIABILITY RISK IMPLICATIONS OF 'REACH'

In June 2007 a new European Union law came into effect with the aim of not only making chemical substances safer for human health and the environment but also with a view to stimulating innovation. The system to which the legislation refers is commonly known as 'REACH', the Registration, Evaluation and Authorisation of CHemicals.

European companies now have to begin a screening process over an 11-year period to test for safety issues. According to the European Commission (EC) safety information is "sketchy" for around 99% of chemicals placed on the market before 1981, of which there are around 100,000. Approximately 2,500 of these are high production volume chemicals (greater than 1,000 tonnes per year). This regulation will apply to all manufacturers, importers and downstream users of chemical substances of quantities greater than 1 tonne per year.



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### Product and Financial Liability Implications

The EC had hoped that the legislation would lessen product liability. In the short term the identification of currently unknown hazardous properties, as will likely arise, will almost certainly form the basis for new product liability suits. It certainly increases the risk potential for the chemical industry and will influence the way the insurance industry rates the liability exposures it seeks to insure.

In the longer term the legislation should result in safer products. Unsafe products or properties will be removed from the market and replaced with safer alternatives, reducing the risk profile and in all likelihood the number of claims and suits too. Insurers should be able to take a more beneficial view of the industry and be more aggressive in offering capacity.

One unknown factor may have some influence on the degree to which the risk profile changes in future. The EC will shortly be releasing a white paper on European Collective court cases against companies ('class actions'). Obviously the greater the likelihood of class action certification then the greater the degree of risk faced by the chemical industry and in turn the insurance industry when offering capacity.

There are some similarities in REACH with the regulation of pharmaceutical and medical devices. Where drug regulators such as the US Food and Drug Administration (FDA) or the European Medicines Agency (EMA) have taken action to change a product's label or withdrawn it from the market place there has typically been some form of legal action on behalf of plaintiffs to allege, amongst other things, failure to warn consumers of potential bodily injury. Even where drug manufacturers have been found not liable they still incur substantial defence costs to defeat the action.

There may also be some similarities from a professional liability standpoint. It is not unusual for shareholders to levy actions against drug companies following:

- Product liability actions,
- Products failing to get regulatory approval or,
- Discontinued development of pre-registered product.

Any one of these three scenarios may provoke a drop in share price that can trigger shareholder action. All three scenarios are possible under REACH. Whether or not liability will attach is the key question and in many or most of these actions there may never be any

indemnity paid. However substantial defence costs can be incurred.

Companies should be examining their current product liability insurance programmes and stress testing them against possible short to mid-term exposure increases.

## Supply Chain Implications

As indicated above there is a potential for some chemical substances to be withdrawn from the European market due to regulatory action, with a similar end result from possible product withdrawal due to commercial considerations. Some surprises are inevitable. How companies plan for such surprises and react to them will dictate their long-term competitive position, and a robust approach to supply chain risk management will be essential.

Chemical production supply chains are normally lengthy and will involve purchases from third parties of various chemical substances as 'ingredients'. The ramifications of losing a critical substance or a combination of substances can be vast. There is, therefore, an alignment of interest between customers and suppliers that should ensure they work together to meet pre-registration regulation dates and ultimately to maximise the likelihood of substances obtaining registration.

Insurance solutions are becoming available to transfer some of the regulatory exposure to insurers using a variety of triggers. Such considerations may soon be as relevant to chemical companies as they are already to pharmaceutical companies. Traditionally business interruption cover has only been available for a financial loss stemming from a physical damage event. The new generation of insurance products will provide protection to companies from losses originating from non-physical damage events, including regulatory intervention.

The consequences of losing a critical supplier through insolvency or regulatory shutdown can be as catastrophic as the consequence of that same supplier suffering a major fire or natural disaster. However, the likelihood of such an occurrence could well be greater, particularly in the light of REACH, highlighting the attraction of considering these new insurance options.

However, insurers will want to see that companies have a good understanding of their exposures and a robust approach to business continuity planning and risk mitigation before they offer significant capacity.

## How is JLT's Life Science & Chemical Practice Able to Assist?

For a full explanation of how JLT may be able to assist please contact our Life Science & Chemical Leaders below. We have the expertise to analyse your product liability exposures. And we can provide you with benchmarking and design appropriate insurance solutions for your company. We are also launching a new Non-Damage Business Interruption product that is designed to respond to many of the emerging supply chain risks faced by chemical companies today.

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