3rd Party Monitors Spur Action in McDonald’s Chinese Food Safety Protocols

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Prepared for Professor Peter Gourevitch
Course on Corporate Social Responsibility
Winter 2016
On July 20th, 2014, an undercover reporter for Dragon News secretly filmed workers at the food processing plant Shanghai Husi Foods handling food with bare hands and adding “foul meat” into processing machines. The exposé presented in stark relief the Chinese government’s deficient food safety inspection mechanisms as well as the negligence of the plant’s US-based owner, OSI Group. Among the affected companies were McDonald’s, KFC, and Starbucks. Fortunately, no health issues were reported. In spite of McDonald’s strides in supply-chain transparency and a long-standing, trusted reputation the company’s brand remained vulnerable to inconsistent global standards. What followed from this incident was a deeper reflection by McDonald’s on the compliance and food safety of its food suppliers.

The Chinese market, with consumers emboldened by information exchange technology and social media services, increasingly placed pressure on food companies to credibly address food safety concerns. Foreign companies are the subject of further scrutiny if they are suspected of illicit activities. What factors led to the Shanghai Husi Foods incident? Why had McDonald’s and OSI’s official monitoring mechanisms failed to detect Shanghai Husi Foods activity? From what source did McDonald’s receive pressure to change its corporate behavior? How has this pressure translated into a response by McDonald’s to ensure food safety and rule compliance? What company can serve as a parallel to the incident McDonald’s faced? How might McDonald’s response have been expanded or improved?
Shanghai Husi Foods Incident:

Shanghai Husi Food became a wretched ordeal for its parent company OSI Group LLC (OSI), a US-based meat processor, as well as client-companies like McDonald’s and KFC. Media reports on the incident followed different narratives: that US restaurants, for example McDonald’s, and OSI had been victims of China’s crackdown on foreign companies. Primarily from the Chinese media OSI was blamed as being negligent in its Chinese operations in addition to the company having its own record of food quality and food safety issues. The Shanghai Husi incident appeared to show problems in OSI’s monitoring and screening mechanisms. How did the problem facing OSI reach this scale? Why did McDonald’s initially sustain its ties with OSI during and immediately after the Shanghai Husi incident?

OSI’s decentralized business model promoted greater autonomy for Chinese managers yet the company failed to standardize its reporting mechanisms. From interviews with US employees of the company, their explanation is that OSI did not know what local Chinese managers were doing nor could they assess their actions. (Cendrowski, par. 5) In spite of OSI’s allowance of autonomy, the company did not properly and frequently audit its Chinese subsidiaries. Further, the company did not standardize its subsidiaries’ reporting mechanisms: company documents in Chinese subsidiary plants were written only in Chinese and were not translated into English. (Cendrowski, par. 12) These weaknesses in auditing and monitoring likely provided an environment at OSI plants where unsanitary and non-compliant activity had greater likelihood to occur.

Though other US restaurants such as KFC and Starbucks immediately cut ties with OSI, McDonald’s stayed with OSI-owned Husi Foods divisions during and after the crisis. In a press statement McDonald’s declared, “We and our suppliers have a decades-long proven track record
of providing safe, quality food to our customers worldwide.” (Patton, par. 3) McDonald’s reluctance to sever ties with OSI stemmed from the restaurant’s close and long-lasting relationship. OSI Group headquarters is located 25 miles from McDonald’s US headquarters and the meat processor had been McDonald’s first supplier when the company started business in 1955. (Cendrowski, par. 19) When McDonald’s entered China in the 1990s OSI came as well, McDonald’s said it would stay with its long-term supplier in Asia and the US. (Hornby, par. 19) McDonald’s appears to have approved of OSI’s initial response to the incident on July 20th, “Husi is taking swift action by investigating what happened and overhauling its safety procedures. We have been in direct contact with OSI’s global leaders…they are sending their top food safety experts to China to provide expertise on operations.” (Patton, par. 3) However, by late July McDonald’s had considered suspending its partnership with OSI, seeking alternate suppliers such as Keystone Foods and Cargill Inc. (Burkitt, par. 2) McDonald’s said it had taken time for the company to perform “due diligence on alternative suppliers” and it awaited the results of the Chinese government’s investigation into OSI. On July 25th, days after OSI’s announcement that the company will set up quality control centers, McDonalds “completely stopped using all Husi food products at restaurants” in China citing customers’ “worries about Husi’s products.” (Kyodo, par. 6)

The exposure of McDonalds by 3rd party monitors galvanized public attention on the failings of official monitoring mechanisms of the company. Though the footage provided by the reporters was obtained from an unofficial source, McDonald’s initial supportive response set it in stark contrast to other food companies like KFC and Starbucks who immediately severed ties with OSI Group. Though food safety laws had been made stricter in recent years, regulatory monitoring had failed to catch this incident. Furthermore, McDonald’s own supply chain
monitoring had failed to alert the company of such Husi Foods’ activity. 3rd party monitors such as the Shanghai Dragon News undermined OSI and McDonald’s control of sensitive information. Energized by the exposed fallibility of the highly regarded McDonald’s, Chinese consumers demanded an immediate, credible response by McDonald’s. Consumer pressure came in the form of boycotts, avoidance, and negative commentary on social media and internet commentary sites.

Customer Pressure Against McDonald’s Partnership with OSI Group Chinese Divisions

In a country plagued by food safety scandals, the Shanghai Husi Foods incident struck Chinese consumers as a troubling surprise. Foreign brands such as McDonald’s were attractive to Chinese consumers partly due to popular views that the companies are operated at higher standards than domestic Chinese businesses. (Hornby, par. 4) China’s food safety has improved since 2008 when state-owned Sanlu group, the largest milk-powder company, was discovered to have contaminated milk formula with melamine tainted-milk which saw six infants’ deaths and about 300,000 reported illnesses. (Burkitt, par. 11; Yeung, p. 10) Concerns about food safety have been rising increasingly, a 2013 Pew Research survey of 3,200 Chinese consumers where 38% said food safety was a “very big problem,” an increase from 12% in 2008. (Pew, 2013) Immediately following the Shanghai Husi Foods incident on July 20, a Sina Shanghai online survey performed on July 22 of 25,000 respondents found that 77% believed the restaurant brands affected had been aware of Husi’s “faulty practices” and 69% said they would no longer eat at restaurants run by Western companies; 39% said they did not care about the latest food scandal and that they were used to poor food safety standards. (Zhang, par. 3) In spite of an environment known for poor food safety concerns, McDonald’s suspension announced before a
full investigation and improvements OSI plants drew from the McDonald’s concern of the very likely negative impact of “customer worries” on McDonald’s current and future market position. By August McDonald’s had reported that its global sales had fallen 14.5% in the Asia/Pacific Middle-East/Africa segment driven by the food scandal as customers boycotted U.S.-owned restaurants. (Forbes, par. 10; Parsons, par. 1)

Sources of McDonald’s Rule and Standards Compliance Framework

McDonald’s restaurant system depends on the strength of three fundamental pillars of support to ensure the company’s high standards are implemented system-wide: franchisees, employees, and suppliers. Though franchisees enjoy some autonomy they must follow McDonald’s “principles of quality, service, cleanliness and value.” (Kroc, par. 8) Employees are monitored by franchise managers who ensure appearance, hygiene, cleanliness and food preparation standards are followed according to McDonald’s company standards. (Business Operations, par. 2) Lastly, Suppliers must acknowledge and follow McDonald’s “Code of Conduct,” and share the codes with facilities within supply chains, review and share training material as well as provide supplier guidance documents and identify all facilities that fall within the supplier’s scope. Supplier’s facilities must complete training and review documentation, pay and complete annual self-assessments, complete baseline audits and schedule follow-up on-site audits with McDonald’s. (Code of Conduct, p. 7) Suppliers are also responsible for prompt reporting of actual or suspected violations of law, their Code and Standards, as well as Supplier Guidance documentation. Weakness or non-compliance in any of the above pillars threatens McDonald’s company reputation and business operations.
Changes Made in Response to Consumer Food Safety Concerns

In an attempt to assuage the food safety consumers of Chinese consumers McDonald’s publicly announced and implemented steps to regain trust in its food safety commitment. An important step was the company’s shift away from its trusted partner OSI which led to unprecedented shortages in meat and produce for McDonald’s in the following weeks and months. The shift away from OSI Group had also been unusual as McDonald’s has relied heavily on longstanding relationships despite instances of code violation. Dan Gorsky, a senior vice president of McDonald’s North America Supply Chain commented on McDonald’s approach to suppliers, “We truly love it when suppliers bounce back from their poor performance periods. In every instance that I can think of, the supplier has become a stronger, more robust, more focused, more competitive and innovative business partner.” (Vitasek, par. 15) For the Chinese consumers McDonald’s severing of its connections with OSI Group served as admittance that the food safety issue had exacted a credible internal change.

Though an internal change of food providers was a necessary step, McDonald’s also established itself as a source for food safety information. In addition to store remodeling and an “advertising blitz” (Burkitt, 2014), unlike on its US and Japanese websites the company has published detailed supplier and compliance information. On McDonald’s Chinese website internet users can view business licenses, delivery inspection reports and testimonials. (See Appendix 1 and 2 for Screenshots and Food Inspection Report)

In addition to overhauling its food-safety strategy, McDonald’s has also announced it would add unannounced audits of facilities coordinated with third-party auditors. (Burkitt, Sept. 2014) McDonald’s also said it would create anonymous hotlines for suppliers and their employees to report on unethical or noncompliant practices. Additionally, the company would
dispatch quality-control specialists to all meat-production facilities supplying McDonald’s. (Burkitt, 2014) Lastly, the company said it had created a new head of food safety in China who would report to McDonald’s CEO. These internal processes and staff changes made public sought to achieve some reputation re-building after confidence in McDonald’s previous internal mechanisms and staff had shown such glaring deficiencies. In spite of these changes, McDonald’s reputation still carried a negative image: several months after the Husi Foods incident the company still saw losses in global sales: revenue fell 11% in Q1 2015 from a year earlier. (Nicolaou, par.2)

An E.coli Outbreak Response at Jack in the Box

On January 15,1993 the Washington State Health Department alerted Jack in the Box president Robert Nugent that an outbreak of E.coli had been attributed to hamburgers purchased at Jack in the Box restaurants. (Crisis Communication, par. 1) In the ensuing weeks four had died and several hundred had been affected by E. Coli poisoning linked to Jack in the Box. Initially Jack in the Box avoided responsibility, pointing out that the infected customers had eaten at other fast food restaurants. On January 18th the company announced it had taken measures to ensure all menu items were prepared in accordance with Department of Health advisories. (par. 3) On January 21st Jack in the Box assumed some responsibility by announcing that the E. coli had come from contaminated meat from their supplier, Vons Companies. Vons responded saying that “We continue to be confident that Vons processing did not contaminate the meat. Health authorities have made it clear that proper cooking would have prevented this tragedy.” (par. 9) The E.coli was linked back to Jack in the Box for its use of burners that did not cook hamburger meat at high enough temperatures to fully kill the contaminant. (Court, par. 11) Monthly sales
fell 35% from a year in January and the negative effect lasted long beyond 1995 with sales 20% lower than in 1993. (par. 12) Avoiding responsibility and shifting blame did not change the customer’s problem that the food was making people sick.

A comparison to Jack in the Box’s response to its own food safety incident can provide a useful benchmark in judging McDonald’s actions. After the incident the company apologized early and often as well as detailing internal changes the company was making in its own advertising. (Court, par. 35) These changes included replacing its meat processor, finding new suppliers, developed a company-wide microbe testing from suppliers, and stricter restaurant cooking and preparation standards. The company published advertisements in Washington newspapers with toll-free numbers for customers to learn about the company’s cleanup efforts. Furthermore, President Nugent apologized on televised commercials and the company later offered to pay affected customers’ medical costs. (par. 36) Jack in the Box, after its earlier face saving avoidance and denial approach, admitted responsibility and accepted the costly responsibility of legal fees and internal restructuring. To underline its commitment to food safety Jack in the Box sought to assure the public that the company had gone above and beyond what compliance and rules required by food safety regulators.

An Evaluation of McDonald’s Response

McDonald’s public and emphatic assurances to its Chinese consumers sought to fix the gap in monitoring that had been exposed by the Dragon News reporting. McDonald’s provided both external modifications to its business practices, for example opening company documents to public view, modifying store design, and repeated apologies and advertisements highlighting
internal changes the company implemented. Internally the company appointed new heads of departments, increased lines of communication, and increased monitoring mechanisms. These measures were all deemed necessary so as to remain a competitive and attractive restaurant in the Chinese market as well as to maintain the company’s global brand image. An incident highlighting the company’s food safety failings threatens not only the local business operations but also risks contamination of the company’s global brand image. From the Chinese consumer’s perspective McDonald’s had taken the necessary steps to make assurances of the company’s food safety after the incident had concluded. More than a year later the company sales had recovered worldwide rising 8.9% in Q3 of 2015. (Gensler, par. 5)

Recommendations for Improvements for Monitoring Agents

Outside observers to McDonald’s may feel powerless to change the company’s corporate behaviors. However, the fallout from the Dragon News investigative footage indeed spurred McDonald’s and other restaurant chains in China to take significant and public actions to re-establish their reputations. McDonald’s in China has taken the path towards greater transparency in reporting on its supply chain and suppliers. Effective transparency measures take time to be credibly received and must be consistently applied. Monitors such as food safety reporters and government auditors should press to increase their access to the company’s facilities to ensure continued compliance. Certainly more compliance issues will be discovered as health and hygiene standards must continuously filter from management to staff. Paradoxically greater visibility of the McDonald’s operations, however, has another consequence: while viewers see that no illicit substances have been added or that the meat has not been tampered with, viewing
the processing large amounts of dead animals can still be unsettling. (New, par. 9; See Appendix 3)

Government and 3\textsuperscript{rd} party monitors of McDonald’s food safety should continue to probe the company on its aim to promote global standards at its worldwide operations. Operating globally without proper implementation strategies threatens companies and their affiliates to risks of rule non-compliance as OSI Group found. Monitors of McDonald’s food safety should investigate its new operations in different countries to determine if the company is indeed implementing an adaptive strategy which considers risks and threats within the new environment.

For McDonald’s own monitors the company should continue to share information related to its suppliers and how the company handles its food. McDonald’s in China lost its reputation for food safety because of an inadequate application of its monitoring mechanisms. For the foreseeable future, the company will need to provide constant factual assurances of the safety of its food or risk losing revenues to competitors and lower restaurant attendance.

\textbf{Conclusion}

In the competitive fast food industry in China, loss of market share and a lowered reputation in the eyes of consumers could severely disadvantage the company while driving consumers to rival restaurants. 3\textsuperscript{rd} party monitors such as the Dragon News’ investigative reporter can spur large companies like McDonald’s to change business operations by exposing non-compliant activity. The 3\textsuperscript{rd} party monitor was sufficiently empowered by having their story carried on a major news provider. Though McDonalds did not swiftly distance itself from OSI Group, it took credible steps such as improving its internal operations and auditing procedures as
well as making public the company’s internal operations for consumers to view. With future revenues and its reputation at stake in the country, McDonald’s saw the cost of these food safety compliance improvements as a necessary component for doing business in China. Furthermore, as a global brand, failure to fully commit to changes in China would threaten the company’s reputation as a safe food provider in other countries.

Works Cited


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<http://www.aboutmcdonalds.com/content/dam/AboutMcDonalds/Sustainability/Library/


Appendix 1: McDonald’s Chinese Website Inspection and Business License information (translated)

<table>
<thead>
<tr>
<th>Product</th>
<th>Product Performance Standards</th>
<th>Supplier</th>
<th>Profile Name</th>
<th>Operating</th>
</tr>
</thead>
<tbody>
<tr>
<td>Burgers</td>
<td>Q / SMK00065-2014 (enterprise standard record number: 4418755-2014)</td>
<td>Ming-Food Co., Ltd.</td>
<td>Business license</td>
<td></td>
</tr>
<tr>
<td>Burgers</td>
<td>Q / SMK00065-2014 (enterprise standard record number: 4418755-2014)</td>
<td>Ming-Food Co., Ltd.</td>
<td>Testimonials</td>
<td></td>
</tr>
<tr>
<td>Burgers</td>
<td>Q / SMK00065-2014 (enterprise standard record number: 4418755-2014)</td>
<td>Ming-Food Co., Ltd.</td>
<td>Each delivery inspection reports</td>
<td></td>
</tr>
</tbody>
</table>
(Excerpt: E.Coli O157: None Detected: Result: Passed)
Appendix 3: YouTube: Grant Imahara appears in McDonald’s Food Safety Assurance video (US): Our Food Your Questions