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Client Alert

CPSC Approves Publication of Proposed Voluntary Recall Rule

November 21, 2013

On November 13, 2013, the U.S. Consumer Product Safety Commission (CPSC) voted 3-1 to publish notice of a proposed interpretive rule that would establish standards for voluntary product recalls, revising 16 CFR part 1115. As approved, the proposed rule, which originally focused on the form and content of recall notice, incorporates several substantive amendments introduced by Commissioner Robert Adler during the November 13 meeting. These amendments would eliminate the option to engage in a voluntary recall without entering into a legally binding agreement and would allow the Commission to seek compliance terms as part of a firm's binding corrective action plan governing the conduct of the recall. Notice of the proposed rulemaking was published in the *Federal Register* on November 21, 2013. 78 Fed. Reg. 69,793 (Nov. 21, 2013).

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- CPSC Approves Publication of Proposed Voluntary Recall Rule
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The amendments have garnered significant attention, for good reason. Voluntary recalls are one thing; binding agreements with a federal enforcer something else altogether. This represents a sea change in Commission direction. Regulated entities who today delegate authority for voluntary recalls to non-lawyer compliance managers may well require additional process and in-house review and approval given that their recall decisions have the force of law. Entities previously inclined to err on the side of corrective action may think twice knowing that their recall terms and conditions are contractual and enforceable in nature. Moreover, the proposed rule's fixation on compliance programs fails to appreciate just how tough it can be to decide whether consumer complaints truly reflect a product defect. Even with a first-class compliance program, engineers wrestle with whether incomplete consumer call center records or warranty and return data override testing results that show compliance with rigorous industry standards, particularly where additional testing does not indicate that the product is defective. A compliance program is just one safeguard against potential product failures but cannot guarantee their safety.

Here, we review the current regulatory framework for voluntary recalls, how the proposal changes the process, and the issues raised by the amended proposal released for public comment.

Voluntary Recall Regulatory Framework

Nearly all recalls conducted with the CPSC are voluntary, with most firms agreeing to cooperate with the Commission to recall and address potential product hazards. Indeed, the Commission's Fast Track program, which won an innovation in government award, provides an abbreviated twenty-day process for negotiating a recall, incentivizing companies to cooperate with the government without fear of an adverse determination regarding the safety of their product. Relying for years on informal cooperation to recall products, the Commission has only recently filed its first actions seeking mandatory recalls in over a decade.

The CPSC has individually negotiated voluntary recalls for over thirty years and, in doing so, has built trust with firms and created common practices that have been incorporated into the mandatory recall notices rule. Similar guidance has already been provided by the Commission in its comprehensive Recall Handbook.

The new rule as proposed substantially modifies established practice and may have unintended consequences.

Proposed Voluntary Recall Process in the Amended Proposal

The draft rule as amended by the Commission vote proposes two significant revisions to 16 CFR § 1115.20, and adds a new subpart D to the rule.

1) Voluntary Corrective Action Plans Become Legally Binding.

Under the current regime, corrective action plans are expressly not legally binding. 16 CFR § 1115.20(a). The lone exception, to date, has been a legally binding voluntary agreement containing a corrective action plan in the form of a consent order. 16 CFR § 1115.20(b).

The original voluntary recall rule promulgated in 1975 distinguished between the voluntary, non-binding corrective action plan and the binding consent agreement, explaining that the consent agreement should only be used where there was "a lack of full confidence that the company would comply with a non-binding Corrective Action Plan" based on the staff's prior experience with the firm. 40 Fed. Reg. 30,938 (July 24, 1975). The non-binding corrective action plan was established specifically "as an expeditious means of protecting the public from a substantial product hazard," in contrast to having to take time to go through the process of securing a consent order. *Id*. at 30,937; *see* 16 CFR § 1115.20(b). The regulations were revised in 1977 to include criteria for the staff to use in determining whether it is appropriate to pursue a non-binding corrective action plan or consent agreement. 42 Fed. Reg. 46,721 (Sept. 16, 1977); *see* 16 CFR § 115.20(a)(2). As recently as 2010, the CPSC elected to exercise its power to seek a legally binding corrective action with the Daiso consent decree.

The Commission's proposal to make corrective action plans legally binding would would represent a clear and dramatic turnabout: "once a firm voluntarily agrees to undertake a corrective action plan, the firm is legally bound to fulfill the terms of the agreement. 78 Fed. Reg. 69, 795, 69, 799. This change addresses concerns about "recalcitrant firm[s]" that "have deliberately and unnecessarily delayed the timely implementation of

the provisions of their corrective action plans." 78 Fed. Reg. 69, 795. This is a marked departure from the original intent of the rule, whereby a mandatory recall proceeding should be pursued if a firm violated a voluntary corrective action plan. *See* 40 Fed. Reg. 30,937. At the November 13 meeting, Commissioner Ann Marie Buerkle challenged whether this provision was even necessary, explaining that this has not been an issue in most cases, that most firms do comply with voluntary corrective action plans.

Giving corrective action plans binding force marks a fundamental shift in the way that voluntary recalls are handled by the CPSC. Consequences may include:

- Imposing potentially significant delay in the voluntary recall process so that terms can be negotiated, vetted, and finalized, thereby gutting the streamlining benefits of the Fast Track program;
- Shifting CPSC resources away from getting unsafe products out of the hands of consumers toward negotiating and enforcing corrective action plan agreements; and
- Causing firms to reevaluate their *uber*-cooperation orientation toward the Commission given –
    - the potential for future litigation with the CPSC over enforcement of corrective action agreements;
    - the need for publicly traded companies to approve the terms of a binding agreement and ensure compliance with such an agreement to meet duties owned to their shareholders; and
    - the effect corrective action plan agreements might have if introduced as evidence in product liability litigation.

The binding corrective action plan proposed may prove tantamount to extracting a consent decree without jumping through consent degree protections and formalities. Commission staff seemingly would no longer have to provide the firm with a draft complaint outlining its case. *See* 16 CFR § 1115.20(b). There would be no requirement that the corrective action plan be published in the *Federal Register* for comment or that the Commission formally consider any objections it received. *Id*. at § 1115.20(b)(4), (5). The CPSC would not settle its charges against the firm, which is mandatory for a consent order. *Id*. at § 1115.20(b)(1)(iii).

Compunding matters, it is not clear that the Commission even has the power to enforce a voluntary corrective action plan as binding, and the proposed rule does not cite to any authority that would enable it to do so. This may explain in part why the two-tiered system was established in the first place, because the only way for the CPSC to enforce a voluntary corrective action plan is through a consent order. Noncompliance with a voluntary corrective action plan does not fall within any of the prohibited acts in Section 19 of the CPSA (15 U.S.C. § 2068), and there is no other provision in the statute authorizing the Commission to otherwise enforce a voluntary corrective action plan. Neither should a voluntary corrective action plan, as proposed in the rule, be enforceable as a contract because the Commission is not a signatory to the plan and does not exchange anything in consideration for the firm's agreeing to the corrective action plan, as it does in a consent order. *See* 16 CFR § 1115.20(b)(1)(iii).

2) Compliance Programs May Be Included in Corrective Action Plans.

The proposed rule contemplates including compliance programs in corrective action plans as a matter of course. In particular, plans would set forth elements of a compliance program similar in substance to those featured in the recent Kolcraft and Williams-Sonoma civil penalty settlements. *See* 78 Fed. Reg. 69,795, 69,799. The terms describe only vaguely what a firm must do to conform, affording the Commission discretion in evaluating a firm's compliance program but also potentially complicating efforts of parties and a reviewing court to enforce terms crafted so generically.

The Commission may have deliberately drafted the rule broadly to retain the discretion to apply more specific terms in individual cases as needed. In operation, however, the terms will likely need to be surgically precise to ensure that a recalling company understands its ongoing obligations. It is unclear whether the CPSC will have the drive, or the wherewithal, to monitor the effectiveness of compliance programs and seek enforcement where firms fall short.

The proposed rule – while nowhere identifying the legal authority for what the Commission proposes – indicates that a compliance program may be appropriate where there have been "[m]ultiple previous recalls," a failure to timely report under Section 15(b) in the past, or actual "[e]vidence of insufficient or ineffectual procedures and controls . . . ," though is clear that "[t]he Commission always retains broad discretion to seek a voluntary compliance program agreement." 78 Fed. Reg. 69,799. Of course, the mere frequency of prior voluntary recalls are not necessarily indicative of a need for a compliance program, but may instead reflect the existence of a robust program designed to catch and act upon product issues before they become a problem. Forcing compliance terms during a voluntary recall process may discourage firms from cooperating with the CPSC on voluntary recalls, as former Commissioner Nancy Nord noted in connection with the recent William-Sonoma settlement.

As a practical matter, entities regulated by the CPSC either have a compliance program or should have one. A robust compliance program can at times mitigate a penalty assessment in the event that a problem with a product arises and is not recognized as a reportable safety issue right away. So, proponents of the rule might say, what's the big deal in encouraging staff to include compliance programs by agreement in certain voluntary corrective action plans? The answer is the not-so-subtle implication that recalls reflect a failure in the existing corporate compliance programs, when very often that is not the case. Class action litigants might point to the need for such terms in an agreement with the Commission as a suggestion of negligence or worse, when in reality a recall may actually vindicate compliance programs as functioning exactly as it should.

Will some upcoming recall be used as evidence to sue to enforce the terms of a legally mandated compliance program? If a corrective action plan is legally binding, the compliance program itself would arguably be subject to enforcement in federal court despite the fact that it does not have the formality and specificity required of a consent decree.

3) The Proposed Rule Details Requirements for Voluntary Recall Notices.

The proposed rule finally lists mandatory elements for voluntary recall notices, some of which are consistent with current practice and others that are new.

- **Direct notice, provided directly to consumers who purchased the recalled product, will be required where that information is "reasonably obtainable" from the firm or third parties. 78 Fed. Reg. 69,796, 69,800. The CPSC does not however address how firms may deal with privacy concerns that could arise in the collection, storage, or use of identifying consumer information, which is a growing priority for state and federal regulators. The Commission has not addressed the cost of such a requirement, which can be quite high given that some firms charge for the use of such customer information in order to maintain control over the data and protect their customer's privacy. In fact, there has been no cost-benefit analysis presented in connection with the proposed rule.**

- **Where consumer information is not available, notices will need to be done by press release or recall alert, posted in-store and on the firm's website, and publicized by two additional methods, drawing from a list provided in the rule. 78 Fed. Reg. 69,796, 69,800.Those other forms of notice include traditional means such as video, radio, and newspaper announcements as well as electronic means, using blogs and social media such as Facebook, Twitter, and Instagram.**

- **The term "recall" will be required to appear in both in the headline and text of voluntary recall notices. 78 Fed. Reg. 69,797, 69,801. Though consistent with existing practice, there remains concern that the term "recall" is often inaccurate given the wide range of corrective action types, and mandating its use can mislead and confuse the very consumer audience designed to be reached.**

- **The notice will need to state "that the hazard '*can*' occur" where there have been incidents. 78 Fed. Reg. 69,801 (emphasis added). The Commission explains "that the words 'could,' 'may,' or 'potential' should not be used . . . ." 78 Fed. Reg. 69,801. Once again, the Commission, by adopting a wooden approach in place of latitude in negotiating, is in effect directing recalling entities to mislead consumers. In fact, it is often far from clear that hazard "can" occur, at least with any reasonable degree of likelihood. Strong, unequivocal language might also be used against a recalling firm in product liability suits. The draft rule does not provide for the use of a liability disclaimer on the notice either, which may affect the admissibility of a voluntary recall notice in litigation.**

- **Notices for recalled products that are manufactured in another country and imported will have to identify both the U.S. importer and the foreign manufacturer. The notice will need to provide the legal name of the manufacturer and the city and country of its headquarters. 78 Fed. Reg. 69,801. Though the Commission is aware that many firms regard the identities and locations of foreign manufacturers as proprietary business information and do not publicly disclose those details, the draft does not account for those issues.**

- **"Significant retailers" of the product will be named in notices. Retailers that exclusively sold or imported the recalled product, have multiple stores across the country or regionally, or sold a large**

portion of the products are considered significant. 78 Fed. Reg. 69,797-98, 69,801. The Commission also reserves the right to identify a retailer in the notice if it "is in the public interest." 78 Fed. Reg. 69,801.Exclusive retailers will also be identified in the headline of the recall notice. *Id*. Though this is common practice today, the draft rule does not appear to afford any discretion for circumstances where it may not be useful or warranted to name the retailer.If there have been fatalities associated with the recalled product, the notice "should provide the age and state of residence of all persons killed." 78 Fed. Reg. 69,802.

- **Compliance programs may be publicized in voluntary recall notices. 78 Fed. Reg. 69,802. It is unclear, though, how mention of a compliance program in a notice would serve to motivate "consumers and other persons to identify the product ant its actual or potential hazards, and to respond . . . ," in line with the CPSC's stated guiding principle for this rule. 78 Fed. Reg. 69,800.**

The proposed rule marks a significant change in the Commission's approach to voluntary recalls, and is yet another example of the CPSC's continued aggressive demonstration of intent to use its authority to the fullest. Yet, in attempting to alter the system that has been in place and working for decades, the Commission may be jeopardizing its ability to effectively respond to product safety issues. The CPSC has limited resources. It needs firms to cooperate in order to recall products. The proposed rule risks alienating those valuable agency-entity partnerships and imposing higher costs on the Commission to enforce its strict regulations. Individual commissioners have stated that they perceive the proposed rule as a simple "tweak" to the voluntary recall process. The rule's terms suggest otherwise. Time will tell. Meantime, entities governed by CPSC would be wise to develop plans for addressing the bold and bracing new world foreshadowed by the Commission's sweeping proposal.

Comments to the proposed rule must be submitted by February 4, 2014. To access the proposed rule, click here.

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