

## CLIENT ALERT

### CPSC Seeks Civil Penalties Against National Retail Chain

April 2015

In a rare move, the U.S. Department of Justice filed suit on April 21st in the Northern District of Texas on behalf of the Consumer Product Safety Commission (CPSC or Commission) seeking civil penalties and injunctive relief against Michaels Stores Inc. (Michaels). The complaint alleges that Michaels knowingly imported and sold glass vases between 2006 and 2010 that were too thin to withstand normal handling and prone to shattering in consumers' hands. The complaint also alleges that, despite numerous injury reports, Michaels failed to immediately notify the CPSC of this substantial product hazard, and instead waited more than two years. According to the CPSC, when Michaels finally reported the hazard, its statements regarding Michaels' role in importing the vases as well as the defects were intentionally misleading.

Michaels sourced the defective vases from an unaffiliated Chinese manufacturer through a procurement company. Michaels then imported the vases under its own importer of record number before selling the vases in its stores or online. The complaint alleges that Michaels began to receive consumer reports as early as 2007 about the fragility of the vases and customer injuries caused by their breakage. However, despite the nine incidents identified in the complaint, Michaels did not submit any information to the CPSC until February of 2010.

Finally, the complaint alleges that Michaels sought to mislead CPSC as to its role in importing the defective vases. That is, the Consumer Product Safety Act (CPSA) distinguishes between "retailers" and "manufacturers" – both have reporting responsibilities under the CPSA, but the reporting requirements for "manufacturers" are broader. *See* 16 C.F.R. § 1115.13. Importantly, the CPSA specifically defines "manufacturer" to include any party that imports a product into the U.S. *See* 15 U.S.C. § 2052(a). According to the Commission, Michaels' reports allegedly implied that Michaels was only a "retailer" and not the "manufacturer," which in turn meant that its reports failed to include significant additional information required of a "manufacturer" under the CPSA.

This complaint offers several immediate lessons for importers, manufacturers, and retailers:

- **Develop and maintain a formal compliance program** – The CPSC cited Michaels' lack of a formal compliance program or internal controls as grounds for establishing a permanent injunction. According to the CPSC, Michaels had not "adopted appropriate internal controls to ensure and monitor compliance." Compl. at ¶ 38.
- **Set up a continuous improvement loop** – Companies should set up a continuous improvement loop that allows them to promptly address consumer complaints and make real-time changes to products accordingly. Retailers should be vigilant about potential design flaws throughout a product's retail life.
- **Report known defects "immediately"** – Under the Commission's regulations, once an entity has sufficient information to reasonably support the conclusion that a consumer product fails to comply with the applicable safety rule or standard, the entity is required to report "immediately," which is defined as within 24 hours. *See* 16 C.F.R. § 1115.14. According to the complaint, Michaels failed to file a report immediately; it knew of at least nine injuries beginning in 2007, but didn't file its Initial Report to the CPSC until 2010. Companies should develop a process for

evaluating and documenting product data, and determining when they have sufficient data to mandate a report to the CPSC, and ensuring that hazards and risks are reported to the CPSC within 24 hours of making that determination.

- **Be mindful of which entities have reporting obligations** – Importers are treated as manufacturers for CPSC reporting purposes. Although a third company procured the vases, Michaels was the importer of record and therefore the manufacturer as a matter of law for CPSC purposes. As a result, CPSC alleged that Michaels "conveyed a false impression" by identifying the procuring company as the importer of the vases. Michaels, as the importer, was ultimately responsible for reporting potential product hazards.

As this case represents an uncommon action by the Commission, importers, manufacturers, and retailers should continue to watch this case closely.

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