

Buckyballs Case Shows What An Uncooperative CPSC Can Do



Law360, New York (June 24, 2014, 10:41 AM ET) -- The U.S. Consumer Product Safety Commission settlement of the Buckyballs litigation provides a cautionary tale for consumer product makers and sellers. It involved a startup business that sold only one product: desktop magnet sets marketed exclusively to adults.

In this case, the CPSC instructed the company to cease selling the magnet sets, even though the company provided clear safety warnings and the product did not cause harm when used as intended. When the company refused to put itself out of business, the agency — before taking any legal action — pressured retailers to stop selling the product. Without any major outlets for its products, the company had to throw in the towel and dissolved. At this point, agency staff, without a commission vote, stretched the law in an attempt to require the company's former CEO to personally conduct a recall and provide refunds out of his personal assets to any consumer who purchased the product.

The settlement, which was reached on May 9, ends the CPSC's administrative action against the CEO, Craig Zucker, as well as a civil action he filed in federal court to enjoin the commission from pursuing him. Because the claims never reached a decision, the main question remains unanswered: Did the CPSC have the authority to impose personal liability on the company's former CEO?

While it seems unlikely that this case will be a harbinger of routinely aggressive enforcement against individuals for their company's activities, the CPSC has preserved that threat. The CPSC's action also sends a clear signal that it is willing to abandon its traditional cooperative approach to resolving safety concerns when a company resists a "suggested" voluntary recall. If the CPSC pursues its recent proposal that would result in a more onerous "voluntary" recall process with higher stakes, more companies may consider resisting such "suggestions" in the future. They should heed the lessons of Buckyballs.

Rise of Buckyballs

Buckyballs and Buckycubes were high-strength magnet sets marketed to adults as desktop toys by a

company called Maxfield & Oberton Holdings LLC. The high-power magnets, which can be stacked and stretched into shapes, became something of a sensation between 2009 and 2011. People Magazine called Buckyballs one of the five hottest trends of 2011, declaring that “this year’s go-to workplace distraction came in the form of these impossible-to-put-down, shape-shifting magnetic balls.”[1] In 2012, they appeared on the cover of the Brookstone catalog. Approximately 2.5 million sets were sold online and through major retailers.

Safety Concerns Emerge

Reports emerged that children who got their hands on Buckyballs swallowed them and that the magnets can join together internally, leading to serious injuries. In response, Maxfield worked with the CPSC in 2010 to develop a comprehensive safety program. The company enhanced product warnings, which read “Keep away from all children!” and cautioned, “Do not put in nose or mouth. Swallowed magnets can stick to intestines causing serious injury or death. Seek immediate medical attention if magnets are swallowed or inhaled.”

The company not only placed warnings on the inside and outside of the packages, it did not permit sales to stores that primarily sell children’s products and required retailers to complete a safety questionnaire and agreement.[2] In coordination with the agency, the company also distributed press and video releases on safe magnet set use. In early 2012, Maxfield established a dedicated magnet safety website and distributed point-of-sale safety signage to retailers for display with the product.

CPSC Files Administrative Complaint and Publishes Proposed Rule

CPSC staff, however, concluded that no warning would be enough to protect children from swallowing the magnets. The commission’s staff urged the company to undertake a voluntary recall, file a “corrective action plan” and remove the products from the market. That recall would put Maxfield out of business.

The company did something almost unheard of: It refused.

The Buckyballs maker viewed its safety efforts as addressing safety concerns. Only when parents improperly left the product accessible to children or it was used by them as toys, contrary to the product’s labeling, could it cause harm. The company’s perspective was that many common products pose a serious risk of injury and many present a much higher risk than its products, yet remain for sale with warning labels. Examples include balloons, button batteries, ATVs, fireworks, drain cleaners and detergent pods.

When negotiations broke down, the CPSC pushed the company’s retail partners to stop selling Buckyballs due to “the severity of the risk of injury and death possibly posed by” the product.[3] About eight major retailers stopped selling the product.

The CPSC’s Office of Compliance issued a preliminary determination on July 10, 2012, finding that

Maxfield's products presented a substantial product hazard. Two weeks later, the CPSC voted 3-1 to file a complaint against the company — its first administrative action seeking a mandatory recall in over a decade. The agency issued a press release citing “more than two dozen ingestion incidents, with at least one dozen involving Buckyballs” since 2009.[4] The agency announced that it sued the company “[i]n an effort to prevent children from suffering further harm ...”[5]

Although the agency could have first filed a complaint against the company and asked a judge to impose stop sales during the action, the CPSC effectively put the company out of business, and only then filed its complaint.[6]

The company responded with an aggressive public relations campaign, noting that under the CPSC's reasoning, the federal agency could selectively ban nearly any product that results in injuries, regardless of whether the product displayed absolutely clear warnings. Maxfield's advocacy efforts included a full-page ad and publishing an Open Letter to President Obama in the Washington Post and similar ads in Politico, Roll Call and The Hill in August 2012.[7] In a series of posts between September and October of 2012, the company's blog satirized the CPSC's action, asking “What will the CPSC ban next?” — hippos, hot dogs, stairs, beds or coconuts, noting that each is responsible for hundreds or thousands of injuries or fatalities each year that warnings cannot effectively prevent.[8]

Meanwhile, the CPSC published a proposed safety standard designed to ban all small magnet desk sets in September 2012.[9]

In the midst of a recall action, facing a proposed regulation that would ban its products and a cut off from major retailers, Maxfield filed a Certificate of Cancellation with Delaware's Secretary of State on Dec. 27, 2012. By doing so, the company ceased to exist pursuant to applicable Delaware law.

The company reportedly established a liquidating trust with \$262,000 to pay for certain claims against the company,[10] an amount the CPSC considered “obviously insufficient” to compensate consumers through a recall program in light of the number of products sold.[11] Then, Zucker reportedly left with his girlfriend for a six-week vacation in Thailand.[12]

CPSC Names Zucker as a Respondent

In an unprecedented action, CPSC staff, without a commission vote, filed a motion to amend its complaint against the defunct company to name Zucker individually as a respondent in February 2013. The action sought to place the responsibility for conducting the recall, providing refunds to customers and reimbursing retailers personally on the company's co-founder. If each and every product sold was returned for a full refund, the recall would cost approximately \$57 million.

The CPSC invoked the “responsible corporate officer” doctrine, a seldom-used theory, as a basis for imposing personal liability on Zucker. The doctrine originated as a response to the shipment of misbranded and adulterated drugs or food, where federal law provided that “[a]ny person” violating this provision is “guilty of a misdemeanor.”[13] Under the Food, Drug, and Cosmetic Act, the U.S. Supreme

Court ruled that a corporate executive who is in a “responsible relationship” in a company has a duty to seek out and remedy criminal violations when they occur and implement measures to ensure violations will not occur.[14]

In May 2013, Administrative Law Judge Dean C. Metry granted a motion to amend the complaint, permitting the CPSC to move forward against Zucker. Judge Metry noted that “at the start of the instant litigation there existed a responsible corporation in Maxfield. However, for reasons unknown, the corporation apparently opted to dissolve after the CPSC filed its complaint.” Judge Metry reasoned that “this is not a case of individual and corporate liability, but rather a case of individual liability in the face of a voluntary corporate dissolution after said corporation has been charged with introducing hazardous products into the stream of commerce.”[15]

Judge Metry later, however, precluded the agency from obtaining Zucker’s personal financial records, finding that information such as his 401K or life insurance had no link to the company or its products.[16]

Zucker responded by establishing a new website, “United We Ball,” which continued to criticize the CPSC, and a new entity that sold large desktop magnets called “Liberty Balls” and “Ball of Rights” to raise money for his legal defense.[17]

He retained attorneys with a government accountability group called Cause of Action, which sought an injunction in federal district court in Maryland against the CPSC on the basis that it had overstepped its authority by naming Zucker as a respondent.[18] Zucker also alleged that the “CPSC singled him out for selective administrative adjudication to deter him and other corporate officers from exercising their freedom of speech and their right to petition government officials for redress, and/or wrongly predetermined the outcome of the administrative adjudicatory process, all in violation of the First and Fifth Amendments of the United States Constitution.”[19]

Settlement

In May, the CPSC and Zucker settled both the administrative action and federal litigation.[20] Zucker agreed to pay \$375,000, in several installments, into a “recall trust” that will provide consumers with refunds if they turn in their Buckyballs to the agency. The commission approved the settlement by a vote of 2-1, with Acting Chair Robert Adler voting in opposition.

According to the settlement, the CPSC will establish a recall trust, which will be administered by CPSC staff and a trustee acting on Zucker’s behalf. The trust will use an initial \$75,000 payment to establish a website and publicize the recall. The recall trust is expected to begin accepting claims within six months of publicizing the recall. Consumers who request a refund will need to provide proof of purchase, including a receipt and affidavit confirming purchase in the U.S., the place of purchase and the purchase price. Basically, those who return more than half the Buckyballs in a set, along with the required proof of purchase, will get a full refund. Those who return slightly less than half will receive a refund of 50 percent of the purchase price. The settlement specifies that the \$375,000 is considered a business

expense, not a fine or penalty.

Commissioner Adler “strongly disagree[d]” with a number of the settlement terms, which he viewed as inadequately to protect and compensate consumers. He objected to the short time frame it provides consumers to request a refund and because he views the amount of the settlement as “minuscule” given the 2.5 million products sold. Although the Acting Chair acknowledged the possibility that the CPSC might not be able to collect more from Zucker, Commissioner Adler would not have agreed to return any unclaimed funds to Zucker after six months, as provided by the settlement terms, and would have given consumers five years to request a refund.[21]

Commissioner Ann Marie Buerkle voted to approve the settlement, but shared her own concerns with the manner in which the agency conducted the litigation. She observed that the question of “when, if ever, an individual officer or director of a corporation can properly be made a respondent in a contested recall case is one of enormous consequence for consumers and manufacturers alike.” She found the agency’s addition of Zucker as a respondent to the complaint, without a commission vote, “troubling.” If the CPSC staff lawyers “can alter our fundamental policy judgments about whom to sue and why, by amending the complaint,” she said, the regulation reserving this power to the commission “is virtually meaningless.”[22]

Zucker declared the settlement a victory. “After nearly two years of fighting, it’s good to finally have this case behind me,” he said. “My life has been consumed with defending both an overreaching lawsuit and the rights of small-business owners. At this point, I have spent more on legal fees than I will on the settlement. The law does not support an individual being named in a case like this and I hope that this settlement will discourage the CPSC from wrongfully pursuing individual officers and entrepreneurs again in the future.”[23]

In response to news of the settlement, Karen Harned, Executive Director of National Federation of Independent Business' Small Business Legal Center, observed that “there’s a bold line between regulatory enforcement and regulatory abuse, and in this case the federal government crossed it without ever slowing down.”[24]

What Does the Buckyballs Litigation Mean for the Future?

The Buckyballs saga shows that the CPSC is willing to take an aggressive approach to regulation and enforcement, even if it means climbing out on a legal limb.

From the Commission’s perspective, the settlement achieved its goal of implementing a voluntary recall, making it illegal for anyone to sell Buckyballs in the future. And, while consumers who harmlessly have Buckyballs on their desks at workplaces, as intended, can continue to use them, those who have concern that their products could fall in the reach of children at home have the option of returning them for a refund.

The settlement terms suggest, however, that the commissioners and agency staff recognized that, in

invoking the responsible corporate officer doctrine and attempting to pierce the corporate veil, the CPSC was on shaky legal ground. The amount of the settlement was a fraction of that which it originally sought, only slightly more than the amount the dissolved company placed in a liquidating trust at the outset and may be less than the company and its CEO spent defending itself.

By settling the matter, the CPSC avoided the potential for an unfavorable ruling finding that it did not have the authority to sue Zucker personally. Section 15 of the Consumer Product Safety Act authorizes the CPSC to “order the manufacturer or any distributor or retailer” of a consumer product to conduct a recall when it finds that a product distributed in commerce presents a substantial product hazard.[25] It does not authorize actions against individual corporate officers. Piercing the corporate veil is a rare action, typically reserved for situations where an individual is viewed as an “alter-ego” of a company and fails to observe corporate formalities. The responsible corporate officer doctrine allows for personal liability, but in response to a criminal violation of a particular federal statute. In the Buckyballs case, there was no violation at all — civil or criminal — as the CPSC had merely made a preliminary determination necessary to begin civil administrative proceedings and no regulation prohibited sale of the products.

Although the CPSC has preserved the powerful threat of personal liability, it is unlikely that the CPSC will routinely name corporate officers as respondents in recall actions. The CPSC found itself in an unusual situation — that of a company vanishing in the midst of a rare administrative action seeking to impose a mandatory recall. Dissolution made Zucker “a man without a company.” The outcome suggests that a company that finds itself subject to pressure from the CPSC to conduct a recall that it cannot undertake, or believes is unwarranted, it should consider alternatives to dissolution.

For example, in another recent case, four major retailers, at the behest of the CPSC, took the unusual step of conducting the recall themselves and offering consumers refunds after the maker of an infant recliner initially refused to voluntarily do so.[26] The small business that made Nap Nanny had earlier worked with the CPSC to address concerns that parents improperly placed the product on table or in cribs, through both improved warnings and design changes. After the agency filed an administrative complaint, the company — which was then out of business, but had not dissolved — settled with the CPSC and undertook the recall.[27]

The CPSC’s actions in both cases also indicate that the agency may find that warnings, however strong, are not enough to address safety concerns. The CPSC may look to whether a hazard can be eliminated through a design change and, if not, weigh the utility of the product against its potential harm. The commission's staff may attempt to completely ban products through the voluntary recall process, even before promulgating a safety standard that is subject to notice and comment rulemaking.

The cases show that the CPSC has significant tools at its disposal to pressure companies to remove products it believes are unsafe from the market. The Consumer Product Safety Act’s reporting and recall obligations fall not only on manufacturers, but also on retailers and distributors. The vast majority of recalls are conducted by manufacturers. If a manufacturer is unwilling or unable to conduct a voluntary recall, however, the CPSC has shown that it will go directly to retailers and ask them to stop selling the

product.

Such impasses could become more common if the CPSC approves a proposed rule that would significantly alter the voluntary recall process. The rule would make voluntarily-entered corrective action plans legally binding, eliminate the ability of businesses to disclaim a product hazard when proactively conducting a recall, and permit the CPSC to mandate adoption of compliance plans.[28] As a result, entering a voluntary recall would likely require more lawyers (and cost), expose the company to greater product liability and present a risk of federal agency intervention in a company's internal operations. With such higher stakes, companies may more frequently resist overtures from CPSC staff to voluntarily conduct a recall that the company views as unnecessary.

The Buckyball and Nap Nanny outcomes also convey to major retailers that, if they take the chance on marketing an innovative, high-demand product developed by a small business, they could be left holding the bag if the CPSC believes there is a safety issue. That message could hurt small businesses and reduce consumer choice.

Have we heard the last of Buckyballs? Probably not. Cause of Action is pursuing litigation against the CPSC to obtain documents through a Freedom of Information Act request indicating how agency staff reached its decision to pursue Zucker personally and whether retaliation played a part. Meanwhile, the CPSC continues to pursue an action against Zen Magnets and Star Networks, two other magnet brands. The proposed rule designed to ban all small magnet desk remains pending.

—By Cary Silverman, Shook Hardy & Bacon LLP

Cary Silverman is a partner in Shook Hardy & Bacon's Washington, D.C., office, where he is a member of the firm's public policy practice group. Silverman filed a motion on behalf of the National Federation for Independent Business in support of Craig Zucker's action seeking an injunction against the Consumer Product Safety Commission in federal district court in Maryland.

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[1] Trends of 2011, People Magazine, v. 76, no. 26 (Dec. 11, 2011).

[2] Sohrab Ahmari, Craig Zucker: What Happens When a Man Takes on the Fed, Wall St. J., Aug. 30, 2013.

[3] Id.

[4] See U.S. Consumer Prod. Safety Comm'n, News Release, CPSC Sues Maxfield & Oberton Over Hazardous Buckyballs® and Buckycube™ Desk Toys Action Prompted by Ongoing Harm to Children From Ingested Magnets, No. 12-234, July 25, 2012.

[5] *Id.*

[6] Former Commissioner Nancy Nord (who voted for filing the complaint) and former Commissioner Anne Northup (who voted against filing the complaint) agree that the CPSC should have sought an order from an Administrative Law Judge to stop the sale of the products, rather than going directly to retail outlets before filing a complaint. They also agreed that they would not have authorized proceeding against Zucker personally after his business folded. See Anne M. Northup, *The Rest of the Buckyballs Story*, *The Hill*, June 6, 2014; Nancy A. Nord, *Fielding Differences*, *Conversations With Consumers*, June 19, 2014.

[7] See Buckyballs Blog, at <http://www.getbuckyballs.com/blog/2012/08/open-letter-to-president-obama/> (last visited June 17, 2014).

[8] See Buckyballs Blog, at <http://www.getbuckyballs.com/blog/tag/consumer-product-safety-commission/> (last visited June 17, 2014).

[9] See Notice of Proposed Rulemaking, *Safety Standard for Magnet Sets*, 77 Fed. Reg. 53,781 (Sept. 4, 2012). The proposed rule would mandate that magnets that have “small parts” have small parts are low strength (a “flux index” of 50 or less). See *id.*

[10] Josh Hicks, *Federal Regulators Suing Buckyballs Founder In Rare Product-Recall Case*, *Wash. Post*, Jan. 7, 2014.

[11] Letter from Mary B. Murphy, Assistant General Counsel, CPSC, to Julie Beth Teicher, Trustee, MOH Liquidating Trust, Feb. 5, 2013.

[12] Burt Helm, *Buckyballs vs. The United States of America*, *Inc. Magazine*, Mar. 2014.

[13] *United States v. Dotterweich*, 320 U.S. 277, 281 (1943) (citing 21 U.S.C. § 333).

[14] *United States v. Park*, 421 U.S. 658, 672 (1975).

[15] Order Granting Complaint Counsel’s Motion for Leave to File Second Amended Complaint in Docket Nos. 12-1 and 12-2, at 18, *In the Matter of Maxfield & Oberton Holdings LLC*, CPSC Docket Nos. 12-1 et seq. (May 3, 2013).

[16] See Order Granting in Part, Denying in Part, Respondent Craig Zucker’s Motion for a Protective Order, *In the Matter of Maxfield & Oberton Holdings LLC*, CPSC Docket Nos. 12-1 et seq. (Mar. 26, 2014).

[17] See <http://unitedweball.org/> (last visited June 16, 2014).

[18] Complaint, *Zucker v. U.S. Consumer Prod. Safety Comm’n*, No. 8:13-cv-03355-DKC (D. Md.) (filed

Nov. 12, 2013).

[19] *Id.*

[20] Consent Agreement, In the Matter of Maxfield & Oberton Holdings LLC, CPSC Docket Nos. 12-1 (May 9, 2014).

[21] See Statement of Commissioner Adler regarding the Dissenting Opinion on the Consent Agreement in the Matter of Maxfield and Oberton, LLC and Craig Zucker, individually and as an officer of Maxfield and Oberton, LLC, Respondents, May 14, 2014.

[22] Statement of Commissioner Buerkle on the Zucker Settlement Agreement, May 14, 2014.

[23] Press Release, A Settlement Agreement has been Reached in the Case CPSC v. Maxfield and Oberton Holdings, LLC. et al., May 12, 2014.

[24] National Federation of Independent Business, Press Release, NFIB: Buckyballs' Lawsuit Highlights Small Businesses Need for Legal Protection, May 13, 2014.

[25] 15 U.S.C. 2064(c)(1).

[26] Consumer Prod. Safety Comm'n, Press Release, Four Retailers Agree to Stop Sale and Voluntarily Recall Nap Nanny Recliners Due to Five Infant Deaths, No. 13-083, Dec. 27, 2012.

[27] Consumer Prod. Safety Comm'n, Press Release, Nap Nanny and Chill Infant Recliners Recalled by Baby Matters LLC After Five Infant Deaths; CPSC, Firm Settle Administrative Litigation, No. 13-216, June 14, 2013; see also Jayne O'Donnell, All Nap Nanny, Chill Recliners Recalled, USA Today, June 14, 2013.

[28] Consumer Prod. Safety Comm'n, Notice of Proposed Rulemaking, Voluntary Remedial Actions and Guidelines for Voluntary Recall Notices, 78 Fed. Reg. 69,793 (Nov. 21, 2013); see also Cary Silverman, CPSC Poised to Change Voluntary Recall Process: Will a More Efficient or a Slower, More Contentious Process Result?, LJM's Prod. Liab. Law & Strategy, vol. 32, no. 19, Mar. 2014.