BUCKYBALLS: AN ETHICS-BASED DISCUSSION OF PRODUCT LIABILITY AND THE RESPONSIBLE CORPORATE OFFICER DOCTRINE

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The Magnet Magnate

Ohio native Craig Zucker caught lightning in a bottle in 2009 when his magnetic office toy became an internet sensation. At age 34, Zucker was a veteran of small entrepreneurial ventures. Previously, he had founded Small Wonder, a company that sold small plastic novelty bracelets, disposable watches and other knick-knacks. Following a failed bottled water venture, he saw a YouTube video about small, powerful rare-earth magnets. Far stronger than typical magnets, the tiny rare-earth magnets could be stacked, sorted and rearranged in limitless shapes. Zucker had found what he thought was the next big thing—the powerful magnets only needed the right packaging and marketing to become a classic toy.

Zucker purchased a small quantity of the magnets from China, repackaged them and marketed them as Buckyballs. Named for futurist Richard Buckminster "Bucky" Fuller (an American neo-futuristic architect, systems theorist, author, design, and inventor), the magnets were sold in packages of 10 up to 216 magnets with a carrying case and retailed between $19.95 and $100.00 (see Figures 1 and 2).

Product Promotion

Following a 2009 demonstration at the New York Gift Show, Buckyballs found their way to desks and office waiting rooms across the county via a retail and distribution network that included popular retailers such as Urban Outfitters and Brookstone. Buckyballs were lauded as hip gifts by pop culture magazines such as Esquire ("there's no better desk toy"), Real Simple ("much more satisfying than a simple stress ball"), Rolling Stone ("toy of the year"), Maxim ("modern art") and People ("addictive") (Buckyballs, 2011). Ultimately more than 2,000,000 Buckyballs were sold in the United States. Zucker's magnet company, Maxfield and Oberton Holdings, LLC (M&O), grew to approximately $18 million in annual sales and boasted a presence in some 5,000 retailers by the end of 2011.

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Figure 1: Buckyballs Example 1.
https://distantoutpost.files.wordpress.com/2012/08/buckyballs.jpg

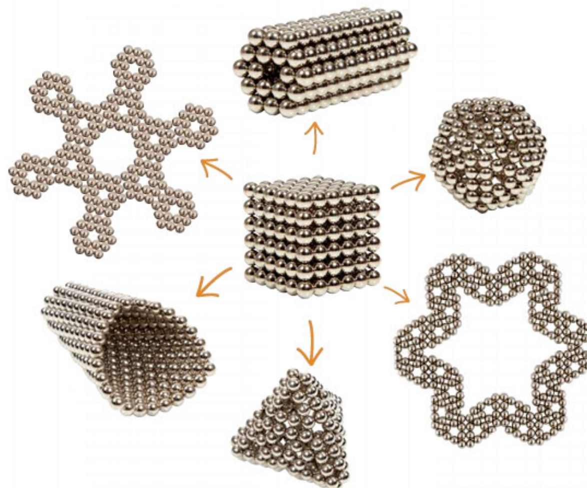

Figure 2: Buckyballs Example 2.
http://internet-entrepreneurship.com/buckyballs-are-amazing/

Warning

As the sales of magnets increased, so did an undercurrent of complaints about the safety of the product. Most of the complaints involved children who ingested the magnets. Because of the

magnets' strong magnetic pull, consuming multiple magnets led to serious internal injuries. From March 2009 until March 2010, Buckyballs were initially sold with the following warning label:

> Warning: Not intended for children. Swallowing of magnets may cause serious injury and require immediate medical care. Ages 13+.

Zucker felt that the warning complied with The Restatement of Torts, the lodestone for products liability law. The Restatement (Third) and an increasing number of state courts have adopted a reasonableness standard for product warnings. The Restatement provides its standard for warning claims at section 10(b):

A reasonable person in the seller's position would provide a warning after the time of sale if:

> (1) the seller knows or reasonably should know that the product poses a substantial risk of harm to persons or property; and
>
> (2) those to whom a warning might be provided can be identified and can reasonably be assumed to be unaware of the risk of harm; and
>
> (3) a warning can be effectively communicated to and acted on by those to whom a warning might be provided; and
>
> (4) the risk of harm is sufficiently great to justify the burden of providing a warning.

In short, manufacturers have a duty to warn about product dangers, so that a reasonable person can use the product safely. As more and more Buckyballs were sold, anecdotal reports began to circulate about the magnets causing injuries to children. As publicity grew, so did attention from federal regulators.

Government Response

The Consumer Products Safety Commission (CPSC), an independent administrative agency, was established by the 1972 Consumer Product Safety Act (CPSA) and charged with protecting the public from unreasonable risks of injury or death associated with the use of consumer products. The CPSC's jurisdiction covered a wide variety of consumer products, including those that posed a fire, electrical, mechanical or chemical hazard. Over the years, the CPSC had worked to coordinate recalls for all manner of dangerous items such as toys, cribs, power tools and household chemicals. In 2007-2008 the agency came under fire following several crib-deaths and massive recalls of Chinese-made toys containing lead paint. That publicity lead to enactment of the 2008 Consumer Product Safety Improvement Act (CPSIA), which gave the agency expanded recall power. Zucker's Buckyballs would prove the first test of these new powers.

In early 2010, the CPSC took an interest in Buckyballs after receiving a smattering of complaints. The toy industry had recently adopted a new standard that made a "toy," something intended for children under 14-years-old. In February 2010, the CPSC notified M&O of the new age standard. Simultaneously, the CPSC took the unprecedented step of directly reaching out to the biggest Buckyballs retailers. In letters sent directly to retailers, the CPSC urged them to voluntarily pull the product. Although the CPSC told retailers that selling Buckyballs was lawful, it warned them that the product carried a significant risk of injury or death. Few tort-conscious retailers were willing to continue sales. This effort was immediately effective and the number of Buckyballs retailers plummeted.

In March 2010, after learning about the communications the CPSC sent to its retailers, M&O voluntarily changed its warning label and issued a voluntary recall. Of the 175,000 Buckyballs sets sold, less than 50 were returned. The new warning label read:

> Keep away from all children! 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 also adopted a sales policy to keep its products out of children's toy retailers. For example, Toys "R" Us was dropped as a retailer and other stores were required to enter into responsible seller agreements. However, reports of injured children continued to mount.

Things Get Worse

From 2010 through 2011 a number of incidents sparked news coverage about the potential dangers Buckyballs posed to children. On January 28, 2010, a nine-year-old boy used Buckyballs to make tongue and lip rings. When he accidentally swallowed the magnets, he was sent to the emergency room. In December 2010, a three-year-old took eight Buckyballs off her refrigerator and ate them. The magnets became embedded in her trachea and esophagus, requiring surgery. In January 2011, a four-year-old mistook three Buckyballs for candy and suffered intestinal damage after eating them. In January 2012, a 10-year-old girl used two Buckyballs to mimic a tongue piercing. She swallowed the magnets and they became embedded in her large intestine, requiring an appendectomy.

The Centers for Disease Control and Prevention noted 33 cases where surgery was required and one instance where death resulted from magnet ingestion. During the first half of 2012, there were reports of 25 children injured by the magnets, nearly double that of the previous year. Subsequent government filings indicated a greater problem, alleging that some 1,700 children had been harmed by Buckyballs and similar powerful magnets.

Advocates for the company emphasized that the rate of injury was relatively low. Some statistics indicated only one injury per 100,000 sets of Buckyballs sold and less than one in 21.5 million per magnets in circulation (Federman, 2012). The company also highlighted their warning label and called for greater parental responsibility. In 2012, concern reached a fever-pitch at the CPSC. The agency contacted M&O and requested another recall, demanding that M&O generate

a plan to remedy the dangers of its product. M&O filed a proposed plan in late July 2012, but hours later the government filed a rare administrative law action, forcing an involuntary recall of the magnets.

Involuntary Recall

The vast majority of newsworthy product recalls are voluntary. Manufacturers often work with regulators to pull products from the market to prevent consumer exposure to unreasonably dangerous products. However, under the Consumer Product Safety Improvement Act (CPSIA) of 2008, the CPSC has the power, via an administrative law action, to compel a product to be pulled from sale and can seek assessment of the associated costs from the manufacturer. The action against M&O was one of the first uses of CPSC's expanded powers. Success in the administrative lawsuit would have effectively dissolved M&O, because it would have been required to cease selling its only product, pay for the costs of a recall (including the costs incurred by retailers and distributors in gathering and returning the products), offer refunds to all of its customers, and undertake expansive public notice and education measures.

The Battle Goes Public

While M&O lawyers developed a legal defense to the mandatory recall, Zucker launched a public campaign against what he viewed as an overreach by the government. Through the internet and social media, Zucker's "Save our Balls" campaign went viral (see Figure 3 for an example). By the fall of 2012, the battle over these tiny magnets was a cause célèbre among limited government activists.

Figure 3: "Save Our Balls" Campaign.
http://www.getbuckyballs.com/blog/tag/craig-zucker/

M&O Dissolution

Following the CPSC's mandatory recall lawsuit, retail sales for Buckyballs stalled and the company was facing significant legal bills for its defense. It also faced a number of product liability claims from injured parties. A company that was flush with cash in 2011, now faced a doubtful future. In November 2012, M&O ceased production of Buckyballs and on December 27, 2012, ceased all operations. The dissolution of the company essentially allowed Zucker to liquidate any remaining assets and walk away.

A liquidating trust was established under Delaware law. It worked similar to a bankruptcy, where claims against the defunct business would be administered by a trustee. The few remaining assets of M&O, which at this point consisted only of the company's now-worthless trademarks and inventory, would be liquidated to pay for any claims. Effectively, this meant that Zucker kept the profits he earned from the enterprise and left very little to pay toward any future claims brought by the injured children. Zucker's business was destroyed but he escaped personally unscathed. The dissolution of M&O, however, did not end the dispute. Rather, it left the CPSC seething and without a source of private funds to pay the recall costs. Unlikely to prevail in the administrative action (at least not without great cost), Zucker had seemingly beaten the CPSC at its own game by refusing to play.

The CPSC Strikes Back

In February 2013, the CPSC filed revisions to its administrative action, amending its complaint to add Zucker as an individual defendant. Rather than simply chase the assets of the now-defunct M&O, the agency sought to invoke the responsible corporate officer doctrine and hold Zucker personally liable for the costs of the recall and damages caused by his company's product. First recognized in the seminal case of *United States v. Park*, 421 U.S. 658 (1975), this doctrine set aside traditional ideas of limited corporate liability and holds individual corporate officers personally liable for the actions of their businesses.

United States v. Park arises from a Food and Drug Administration (FDA) enforcement action. Park was the CEO of Acme Markets, a national food chain. An FDA inspection of Acme's Baltimore warehouse discovered a rat infestation. After repeated warnings, Acme failed to fix the problem. The FDA pursued fines for violations, to which Acme pleaded guilty. However, the FDA also sought to hold Park personally liable for a misdemeanor violation of the federal safety law. The Supreme Court agreed with the FDA, holding that an individual officer could be held personally liable when the officer has a "responsible relationship to the issue." In Park's case, he admitted that as CEO he was ultimately responsible for compliance issues, although he was not specifically aware of the violation. Park thought "dependable subordinates" were addressing compliance. *United States v. Park* was one of the rare examples of "piercing the corporate veil" (i.e., a legal decision that treats the rights or duties of a corporation as the rights or liabilities of its shareholders).

For Zucker, application of the responsible corporate officer doctrine had potentially devastating consequences. The CPSC sought to make Zucker personally responsible for the recall costs,

which the agency estimated at a staggering $57 million. The CPSC only sought personal liability from Zucker, not any of the other M&O members or officers (or even the liquidating trust). Zucker considered the personal liability charges to be retaliation for his snarky ad campaign and defense of the initial recall. Complaints of government overreach turned into complaints of retaliation for daring to speak out against the CPSC. Zucker argued that seeking personal liability was intended to chill future speech against the CPSC and to punish him for his public campaign opposing the recall.

Decision Point

Buckyballs had become a test case for the CPSC's expanded recall power. Further, the Buckyballs case was the CPSC's most aggressive attempt at making a corporate officer personally liable for business-related mishaps. Zucker now realized that, he had become representative of business owners and corporate officers at large. If Zucker fought the charges and won, there would be legal precedent that corporate officers could continue to separate themselves from any harm to consumers caused by the business. This outcome would presumably favor economic productivity because business owners and corporate officers would be protected as they innovated and brought new products to market. The downside would be that businesses, and the corporate officers that ran them, would be able to bring out products with potential harm to the health and safety of consumers. If Zucker fought the charges and lost, there would be legal precedent that corporate officers could potentially be liable for business-related calamities. Another option for Zucker was to reach a settlement with the CPSC. Zucker did not have the $57 million the agency was demanding, but he could agree to pay a portion of this amount in order for the personal liability charges to be dropped.

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