

Legal Risks For Consumer Products Cos. In 2018: Part 2

By **Erin Bosman and Julie Park** (June 8, 2018, 3:07 PM EDT)

Developing and maintaining consumer trust is central to operating a successful consumer products company. Product recalls, contamination issues, product defects, privacy violations and data breaches can all undermine consumer trust in a company and its products.

These risks, and the risks of related litigation, only increase when products are connected to the internet, contain sensitive consumer information or operate autonomously. Rapidly evolving technologies, an uncertain economy and changing government regulations may further complicate the already challenging task of navigating legal issues.

Modern companies cannot anticipate all problems or guard against all risks, but should be mindful of common industry pitfalls. We have written this two-part analysis, based on a recent survey that our firm commissioned, to raise awareness of some of these risks — which may be the first step to avoiding unnecessary liability.

Morrison & Foerster commissioned Oxford Analytica[1] to evaluate the legal landscape for consumer products companies in the United States and to provide analysis of relevant trends and areas of concern. Oxford Analytica used data from sources including interviews with Morrison & Foerster clients and partners, interviews with law professors and surveys of in-house counsel conducted by the market research company YouGov.[2]

The first installment of this article discussed what the survey suggests are the greatest drivers of business change and the evolving risk environment in 2018. In this second installment, we look in detail at caseloads and issues of concern, the growing influence of the FTC and trends in corporate legal departments' budgeting.

Caseload Trends and Issues for 2018

Product liability, data privacy and regulatory/compliance are expected to be the three biggest sources of new case activity in 2018, according to survey respondents. Those top three sources were cited two to four times more than other sources.



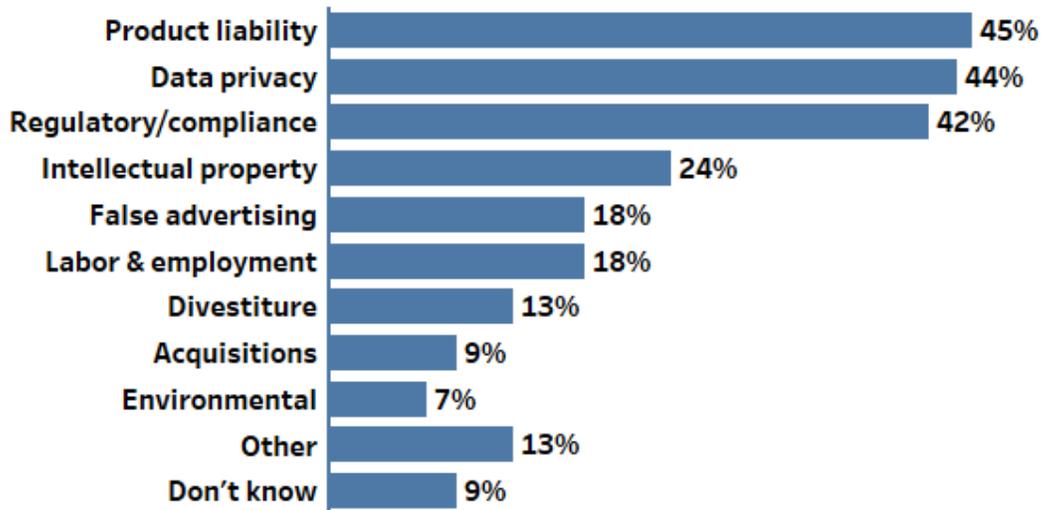
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CASELOAD TRENDS AND ISSUES FOR 2018

Respondents identified the following as the biggest expected sources of new case activity in 2018.



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The expectation of new cases driven by product liability, data privacy and regulatory/compliance tracks the articulated concerns of in-house legal departments. These three categories were ranked among the top five areas of concern, alongside litigation and protection of brand equity.

Below are some details about what is driving new cases in the product liability, data privacy and regulatory/compliance areas.

Product Liability

Product liability is not a new concern for consumer products companies, but the growth of the internet of things has changed the game. As internet of things innovations proliferate, manufacturers will design new gizmos, gadgets and contraptions for their products.

Inevitably, new features will lead to new problems. Manufacturers should anticipate potential failures of connected devices and analyze how those failures may be dealt with under traditional product liability legal standards.

In light of the current technology landscape, including the explosion of connected and autonomous devices, no one can know the specific product liability exposure that awaits consumer products companies. For example, one major unanswered question is: How will regulators treat a product that is considered both software and hardware?

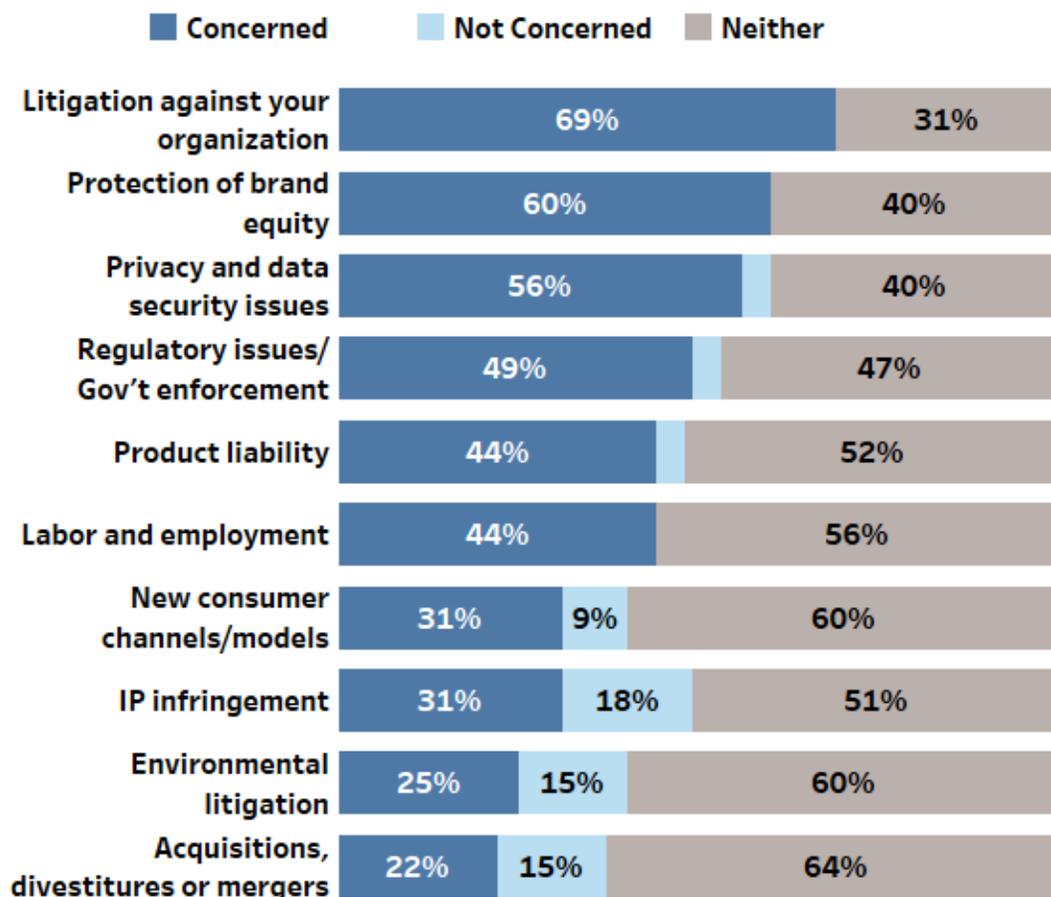
Historically, software hasn't been subject to product liability claims. But as the internet of things becomes more pervasive, courts may determine that software integrated into a connected product should be. Courts may also find that connected devices expand the manufacturer's duty to warn users about potential safety issues. Legal counsel must anticipate the most likely outcome of future judicial decisions, to help minimize potential exposure.

Data Security and Privacy

As products and companies gather more information through use of novel systems and products, concerns about data security and privacy will only continue to grow. Survey respondents made it clear that consumer products companies are concerned with the liabilities that accompany storage, use, transfer and analysis of sensitive information.

CASELOAD TRENDS AND ISSUES FOR 2018

Respondents identified their most pressing business concerns.



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Data Security

Many consumer products companies now gather large amounts of data regarding consumers, including their behaviors. In many cases this is intentional, but sometimes companies (or companies' products) may inadvertently harvest or collect information.

This data can be a tremendous asset, allowing companies to refine the next version of a product based on customer feedback and usage, or targeting favorable user demographics. Data can also be a product

or service itself, such as when companies attempt to monetize it in other ways beyond companies using data for their own internal purposes.

However, collecting data comes with risks — for example, a company may expand the scope of regulation by collecting certain types of data, as well as face potential liability if the company misuses the data or suffers a data breach.

Data Privacy

Data privacy is an issue that focuses on the collection, protection, processing and deletion of data regarding an individual. It is an issue that is front and center for many companies, and it is increasingly considered in the product liability context and, as such, poses new challenges for consumer products companies.

The amount of information that is being collected about consumers is growing exponentially. The increase in the amount of data collected and the continuing trend of consumers asserting privacy rights gives credence to the statement by Daniel Hemel, assistant professor of law at the University of Chicago Law School, that “[d]ata privacy is the new product liability.”

European lawmakers have recently passed a law that increases the protection for consumers, the General Data Protection Regulation, which became effective on May 25, 2018. It is intended to strengthen protection in the European Union, but it can apply both to companies within the EU and to companies in other parts of the world, depending on the circumstances. GDPR is part of a continuing, and growing, trend for increased regulation of personal information globally.

Failing to protect consumers’ privacy poses two major issues for consumer products companies.

- Major reputational damage and loss of brand equity: This is a primary business concern among survey respondents. A brand that is seen to be intrusive into its customers’ lives or unable to protect personal information is likely to fail. This is particularly true if competitors’ products can easily replace the intrusive devices.
- Increased litigation pertaining to privacy issues: The California Invasion of Privacy Act, for example, has been cited in recent class-action suits regarding communication between businesses and customers. GDPR increases the legal requirements on companies, as well.

Regulatory/Compliance

Uncertainties in Washington, D.C., will impact the consumer products industry. Although regulatory innovation is unlikely to come from the current U.S. administration, regulatory agencies like the U.S. Consumer Product Safety Commission and the U.S. Food and Drug Administration will continue to operate and to modify requirements placed on consumer products companies.

Perhaps more importantly, individual states are likely to try and fill the void and be active in legislating or regulating many consumer-related issues. California, New York, Illinois, Massachusetts and Connecticut are among the states most likely to create new laws around data security, privacy and product safety, and we see that California has recently proposed new legislation regarding data privacy.

State legislators and attorneys general in these states have all signaled their interest in doing so. These five states alone produce about 30 percent of U.S. gross domestic product, which means that legislative or regulatory change in these states will have a significant impact on consumer products companies.

Balkanized Consumers

Increased localization of data regulation may also pose major challenges for consumer products companies. Consider, for example, if different countries promulgate different standards for data collection, transfer and storage (e.g., what is allowed in Country A may not be allowed in Country B).

Tailoring corporate handling of that data to comply with both countries' requirements may be difficult or, in some instances, impossible, particularly where there are requirements that conflict and are not just inconsistent.

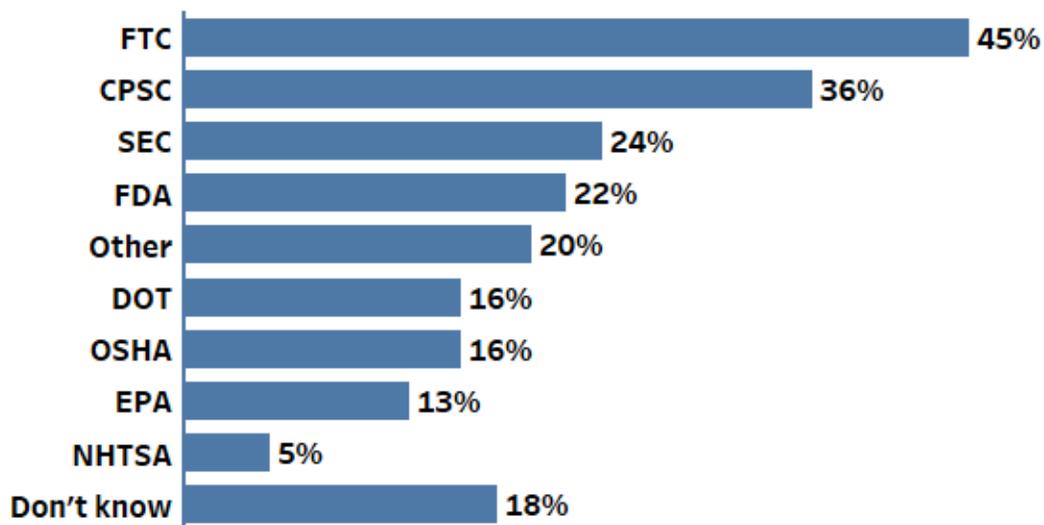
Accordingly, companies operating internationally need to not only determine how to comply with the relevant privacy standards in varying jurisdictions, but also to anticipate how changes to those standards may affect their logistics and business operations.

FTC's Growing Influence

Relevant regulations come from a variety of sources. Although the current presidential administration and Republican-controlled Congress are unlikely to push for increased regulation and enforcement, there are agencies in the United States responsible for enforcing privacy laws and regulations. Survey respondents identified a number of federal agencies they believe will have the most impact on their businesses.

FTC'S GROWING INFLUENCE

Respondents identified the federal agencies they believe will have the most impact on their businesses.



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The Federal Trade Commission was considered by nearly half of survey respondents to be the most

relevant regulatory agency. It was followed by the CPSC, the U.S. Securities and Exchange Commission and the FDA, respectively.

Each of these agencies, at least in part, monitors and regulates security, transfer and analysis of potentially sensitive information. In recognizing the impact these agencies may have, survey participants appear to have a finger on the pulse of the rising importance of privacy and data security issues to the industry.

Data Privacy Benchmark Cases

Recently, the FTC has levied and settled a number of claims against high-profile companies. In 2011, the FTC reached a settlement with Google Inc. over claims that it had breached privacy promises to consumers when launching its social network, Google Buzz. This settlement was one of the first privacy cases under Section 5 to require a comprehensive privacy program.

But not all companies capitulate to federal regulations. For example, LabMD Inc. challenged a 2016 FTC order requiring the company to implement a data security plan over the next 20 years, arguing that the FTC overstepped its authority. The FTC's initial complaint filed in 2013 alleged that LabMD failed to reasonably protect the security of consumers' personal data, including sensitive medical information. The company recently prevailed against the FTC in court. But it remains to be seen how much the outcome of this case will affect the scope of the FTC's future ability to enforce its power in matters of privacy and cybersecurity.

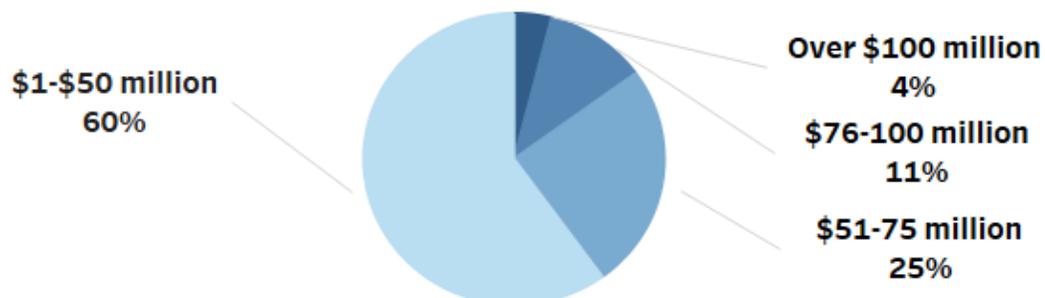
Legal Department Budgetary Considerations

Money matters

As discussed above, the economy is expected to be one of the most significant drivers of the consumer product industry in the next year. 60 percent of respondents reported budgeted dollar exposure for litigation in 2017 to be below \$50 million, while 15 percent reported spending \$76 million or more last year, 36 percent reported spending \$5 million or less on outside counsel and 31 percent reported spending over \$25 million annually.

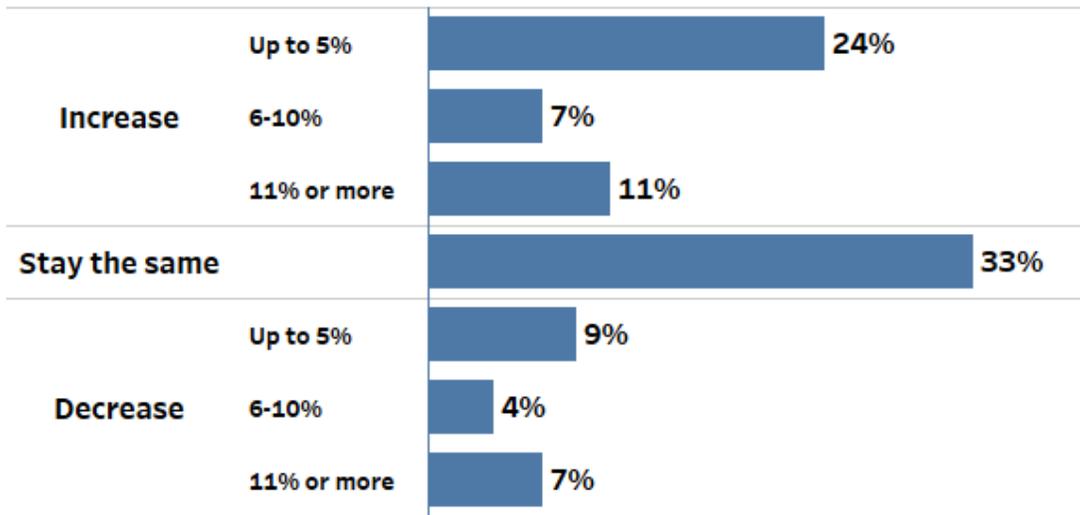
LITIGATION EXPOSURE

Respondents were asked to estimate the dollar exposure of their consumer products litigation matters in 2017.



LEGAL MATTER SPENDING FORECAST

Respondents were asked if spending on consumer products legal matters in 2018 will increase, decrease, or stay the same, compared to 2017.

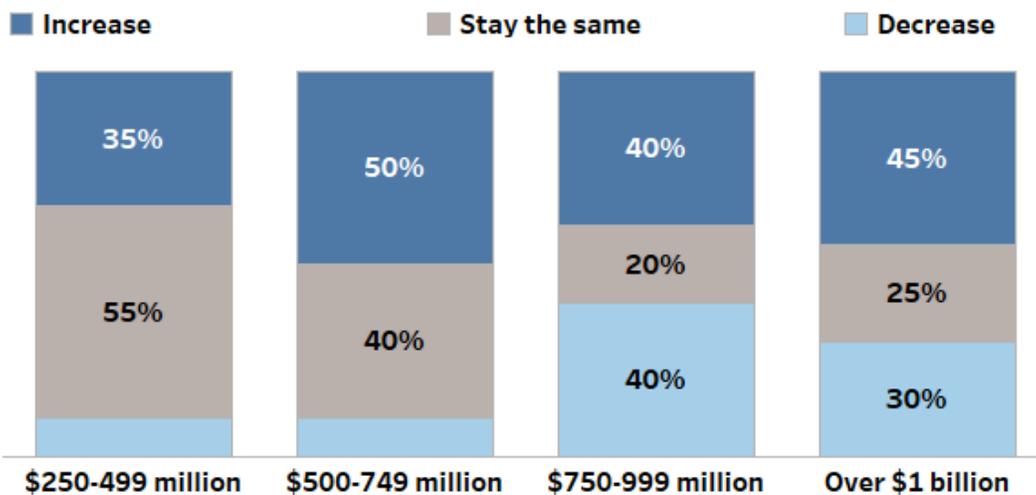


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42 percent of survey respondents forecast increased litigation costs for their companies in 2018. This may be due to a simple extrapolation of budgets and expected growth generally, or may reflect the expectation of more high-risk cases and the need to prepare for new and increased case activity centered on product liability, data privacy and regulatory compliance.

LEGAL MATTER SPENDING BY ANNUAL REVENUE

Respondents were asked how they expect spending on consumer legal protection to change compared to 2017, by annual revenue.



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Company size affects anticipated litigation costs. The percentage of companies expecting an increase in

litigation costs for 2018 varies by company size but doesn't increase linearly. For instance, 50 percent of companies with annual revenue between \$500 and \$750 million project an increase in spending, compared to 45 percent of companies with annual revenues over \$1 billion.

Notably, while only 10 percent of companies with revenues under \$750 million expect their legal costs to decrease, 40 percent of companies with at least \$1 billion in annual revenue also expect a decrease. This may reflect a greater ability of larger companies to leverage in-house counsel to decrease litigation costs.

Summary: Unknown Unknowns

Some risks are easier to anticipate than others, but there are also plenty of unknown unknowns — risks lurking around the corner and not yet identified. By paying close attention to the evolving regulatory, legal and technological environment, consumer products companies will be better prepared to address these risks. Savvy in-house counsel can protect their companies' interests by working with outside counsel to identify potential areas of concern.

Our survey results consistently indicated growing concerns about liabilities related to the protection, storage and use of consumer data. Survey results also lend support to an emerging "federalization" of product liability enforcement, which will, in turn, present new legal challenges. Further, consumer products companies are clearly concerned about how changes in demographics and consumer preferences could make their brands vulnerable to disruption.

The legal landscape for consumer products companies is rapidly changing. Our analysis provides some insight into those changes and the increased risks and benefits that they will bring. We look forward to helping our clients anticipate change and rise to the new challenges that await us in the coming year and beyond.

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[1] Oxford Analytica is an international consulting firm that provides strategic analysis of world events and industries.

[2] The surveys of in-house counsel were conducted telephonically between Nov. 13 and Dec. 17, 2017. In-house counsel across the United States at companies offering a range of consumer products participated in the survey. Approximately one-third of respondents are employed by companies with revenues over \$1 billion, nearly one-third are employed by companies with revenues of \$500 million to \$1 billion and the rest are employed by companies with revenues between \$250 and \$499 million.