

## CPSC Definitely Not Zen About High-Powered Magnets

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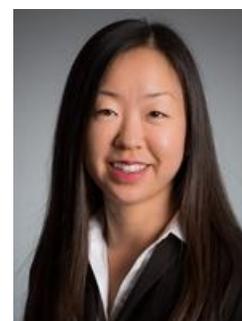
The last weeks of March brought us two interesting and seemingly contradictory opinions that show the many tools the U.S. Consumer Product Safety Commission has at its disposal to enforce its own regulations. These orders also demonstrate that CPSC will not hesitate to deploy resources and engage in simultaneous avenues of enforcement when it views violations as particularly egregious. In the ongoing saga of high-powered, small, rare earth magnet sets (SREMS), CPSC showed its resolve by pursuing an offensive enforcement campaign in both litigation and administrative forums.

In most instances, CPSC threatens administrative action or litigation to leverage consumer products distributors and manufacturers into corrective action plans. CPSC will, at times, act on its threats, but rarely has it had occasion to use this type of multifaceted approach to enforcement. As one would expect, CPSC most commonly enforces its regulations against products that present a danger to consumers, but a product that may pose a risk to consumers can often be made safer with proper warnings. The SREMS saga demonstrates that, even if proper warnings can mitigate a safety issue such that a product does not legally pose a substantial product hazard, CPSC may still be able to force companies into compliance with its demands if it believes the product is dangerous.

SREMS usually come in the form of tiny balls, approximately the size of a water droplet, and exhibit powerful magnetic forces that allow the balls to bind into interesting shapes and strings. They are also sold in the form of stackable discs. SREMS have many uses, including as functional parts of headphones, hard drives and various engines and turbines. Due to their small size and powerful magnetism, SREMS also appeal to consumers as educational tools and entertaining desk accessories. These tiny magnets, however, have also been the cause of serious injury. The individual magnets in SREMS are small enough for children to ingest and “so powerful that if ingested, they will cut through stomach and intestine to be reunited with each other.” *Jordan v. Maxfield & Oberton Holdings LLC*, No. 3:15-CV-220-CWR-LRA, (N.D. Miss. 2016).



Erin M. Bosman



Julie Y. Park



Dean S. Atyia

## **Zen Magnets Plays a Dangerous Game**

Star Networks USA LLC and Zen Magnets LLC are key players in the SREMS saga. In 2012, CPSC commenced administrative litigation against multiple SREMS companies, including Zen and Star. Both companies refused to recall the SREMS, which CPSC had preliminarily determined to be defective due to the injury they can cause when ingested. In August 2014, Star settled the administrative litigation by voluntarily recalling its SREMS.

Zen took a wholly different route. Rather than participate in settlement negotiations, Zen purchased a substantial amount of Star's inventory (917,000 total units) at a significant discount while CPSC was negotiating with Star. Zen paid only \$5,500 for Star's inventory that normally retailed for \$45,850. Zen then repackaged as its own inventory the exact same magnets that Star voluntarily recalled.

Pursuant to the Consumer Product Safety Act (CPSA), CPSC is authorized to bring administrative actions and promulgate rules to enforce the statute. The CPSA also imparts jurisdiction upon federal district courts to enjoin violations of the statute. CPSC initially sought a preliminary injunction in 2015 from the Colorado District Court to immediately prevent Zen from selling or distributing Star's voluntarily recalled magnets. Following the court's grant of the preliminary injunction, CPSC filed a motion for summary judgment, seeking permanent injunctive relief as well as a determination that Zen "knowingly" violated the statute, which would subject the company to civil penalties.

The CPSA prohibits the sale or distribution of any product subject to voluntary corrective action, like the recalled Star magnets. Therefore, CPSC contended that Zen violated the CPSA by repackaging Star's inventory. Zen intermixed the Star magnets with its own, such that sales of the Star magnets were indistinguishable from sales of the Zen magnets. The court agreed and found that there was no genuine issue of material fact as to Zen's violation of the statute.

The court issued an injunction ordering Zen to, among other things, (1) conduct a recall of all products incorporating Star's recalled magnets, (2) provide notification to customers, (3) post the court's order on its website for two years and announce the notice on social media accounts maintained by Zen including Facebook and Twitter, (4) notify current and future business associates of the order and (5) destroy or dispose of all recalled products in Zen's inventory or supply chain. The court also granted summary judgment on CPSC's claim that Zen "knowingly" violated the CPSA. This ruling allows the CPSC to impose further civil penalties.

Commenting on the ruling, CPSC Chairman Elliot Kaye said "The court's order to stop the ongoing sale of these recalled high-powered magnets is a big victory for the safety of children. Along with the U.S. Department of Justice, we will continue to move aggressively to enforce the law and protect consumers from the sale of recalled products, especially those that put children at risk."

## **Saved by the ALJ**

The Colorado District Court delivered its opinion on March 22. On March 25, an administrative law judge presiding over CPSC's related administrative action against Zen issued his own decision. The related administrative action took place pursuant to Section 15 of the CPSA, which allows the commission to seek an administrative determination that a product is a substantial hazard and presents a risk of injury to consumers. The ALJ found that SREMS are not substantial product hazards and do not present a substantial risk of injury to consumers when used as intended.

Considering all the litigation and reports of injury associated with SREMS, the ALJ's decision demonstrates the high burden of proof that CPSC must meet to obtain a finding of substantial product hazard. Administrative law judge Dean C. Metry concluded that CPSC did not meet its burden. The crux of the opinion was that, although the magnets are dangerous when ingested, (1) there is no danger of ingestion during the normal operation and use of the product; (2) they are not marketed to children under the age of 14 who may not be able to appreciate the dangers associated with abnormal operation and use, specifically ingestion; (3) the warnings affixed to the magnets that identify the danger of ingestion are not defective; and (4) the utility of the magnets as artistic and instructional tools outweighs their risk when used as directed such that the magnets are not inherently defective.

ALJ Metry ultimately concluded that SREMS are not product hazards when sold with appropriate warnings that include proper age recommendations.

## **Conclusion**

This pair of opinions shows the varied tools that CPSC has at its disposal, even if it cannot meet its burden to prove that a product is a substantial product hazard. The ALJ ultimately determined that the magnets Zen bought from Star were not substantial product hazards, but that finding had no bearing on the district court's determination that Zen was liable for violating CPSC regulations against selling recalled products.

What does this mean for Zen's magnets? As a result of the administrative decision, Zen must conduct a recall of any magnets sold without proper warnings (those sold before May 2010).

The Colorado District Court's order enjoins Zen from selling any of its magnets that were commingled with the indistinguishable Star magnets. And even though the ALJ decision might otherwise leave open the door for Zen to produce and market a new stock of magnets, these magnets have been subject to a federal ban that was imposed in April 2015 at CPSC's urging. Zen's website demonstrates Zen's pride in taking on the federal government: "The CPSC's war on magnets was the first time they took a two-pronged approach of conducting rulemaking simultaneously with administrative action. ... Right now, our biggest obstacle seems to be money to fund the battle." Zen bet the farm and seems ready to continue its fight. Its success in the administrative proceeding may embolden other consumer products companies to stand their ground and force CPSC to prove to an ALJ that there is a substantial product hazard.

—By Erin M. Bosman, Julie Y. Park and Dean S. Atyia, Morrison & Foerster LLP

*Erin Bosman is a partner and Julie Park and Dean Atyia are associates in Morrison & Foerster's San Diego office.*

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