



LEGAL RISKS TO CONSUMER PRODUCTS COMPANIES

2018

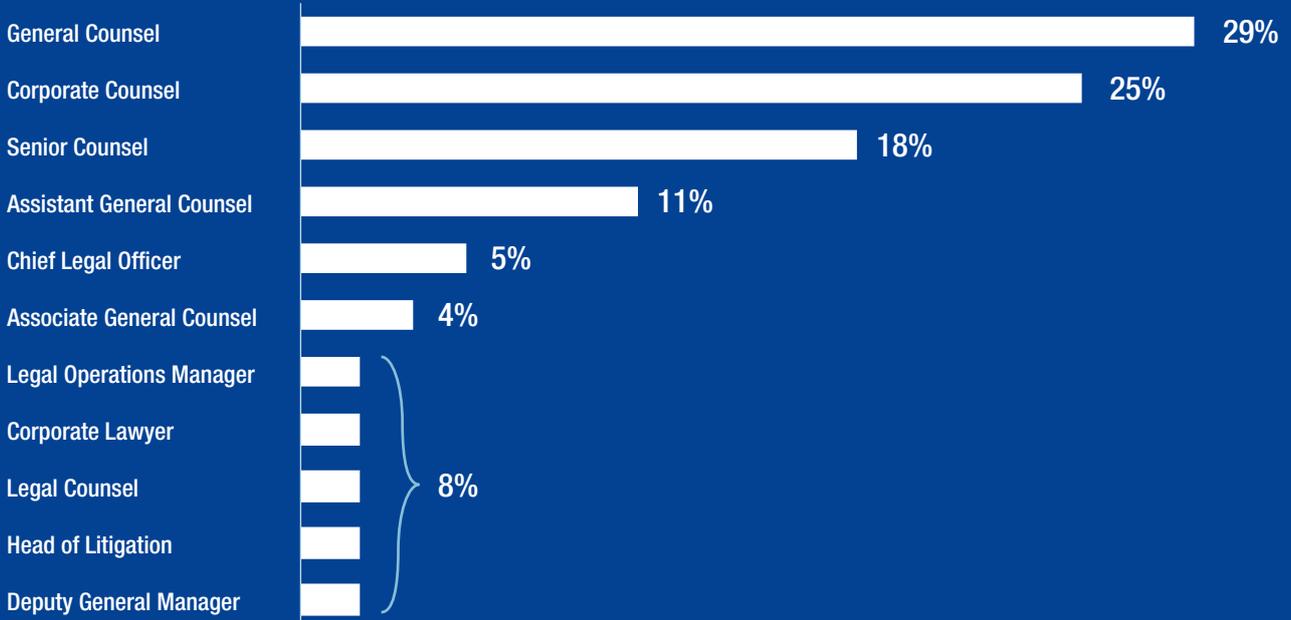
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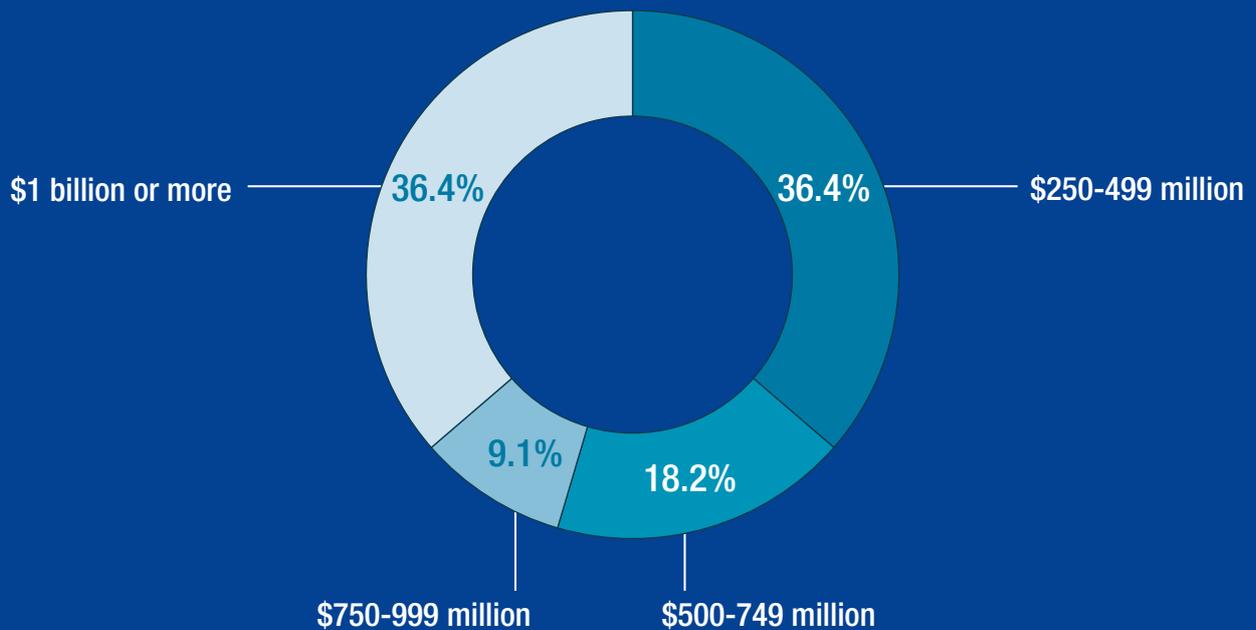
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FIGURE 1: SURVEY BREAKDOWN

Can you please tell me what your job title is?



What was the revenue of your company in the last financial year?



INTRODUCTION

Running a successful consumer products company has never been easy. Rapidly evolving technologies, an uncertain economy, and changing government regulations appear primed to complicate the already challenging task of navigating legal issues. If you are concerned (or even curious) about what the legal landscape for your company in 2018 looks like, this report is for you.

Developing and maintaining consumer trust is central to operating a successful consumer products company. Product recalls, contaminations, 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.

Modern companies cannot anticipate all problems or guard against all risks, but should be mindful of common industry pitfalls. We are providing this report to raise awareness of some of these risks, which may be the first step to avoiding unnecessary liability.

Layered on top of these concerns is the need to deal with an expanding list of regulatory agencies, which circle the globe and often have overlapping jurisdictions and competing enforcement priorities. This complex products landscape will test the existing legal framework and force companies to anticipate and plan for previously unknown risks.

This report identifies some of the notable emerging risks that consumer companies may face in the coming year.

SURVEY METHODOLOGY

Morrison & Foerster commissioned Oxford Analytica¹ to evaluate the legal landscape for consumer products companies in the United States and to provide analysis of relevant trends and areas of concern. Operating as an independent third party, Oxford Analytica relied on data from numerous 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.

The surveys of in-house counsel were conducted telephonically between November 13 and December 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.

EXECUTIVE OVERVIEW

Although much uncertainty exists in the consumer products space, many survey respondents identified similar industry drivers and areas of concern. Several companies polled believed their legal endeavors (and related costs) will increase in 2018.

- The most important drivers of change for consumer products companies in 2018 will be: the economy (78%), government regulatory change (71%), and technological advancements (59%).
- One out of three legal matters in 2017 was high risk or complex, with one out of five in-house counsel expecting more high-risk products lawsuits in 2018.
- The following areas are expected to give rise to the most new case activity in 2018: product liability (45%), data privacy (44%), and regulatory/compliance (42%).
- The biggest concerns within legal departments are: litigation (69%), protection of brand equity (60%), privacy and data security (56%), regulatory issues/government enforcement (49%), and product liability (44%).
- Approximately two out of five legal departments expect their litigation costs to increase in 2018.

¹ Oxford Analytica is an international consulting firm that provides strategic analysis of world events and industries. More information about the firm can be found [here](#).

2018 DRIVERS OF BUSINESS CHANGE

In-house counsel at consumer products companies expect the economy, government regulatory changes, and technological advancements to be the top drivers of change for their businesses in 2018. Below we provide additional information about each of these categories and how we expect them to affect the consumer products industry.

THE ECONOMY

Unsurprisingly, industry leaders anticipate the economy will generally drive developments in the consumer products industry. With U.S. unemployment at its lowest level in 17 years, and wages expected to grow approximately 3%, consumers should have more disposable income and confidence in 2018. But this growth may be short-lived: consumers are also dipping heavily into their savings, which have fallen to their lowest level since the Great Recession of 2007. This could limit future spending, especially if combined with faster-than-expected increases in inflation or interest rates as the Federal Reserve revises its monetary policy.

If the U.S. economy is healthy, or at least stable, in the coming year, consumer products companies will be more willing to invest in new and emerging markets to drive growth. In addition, consumer products companies will continue to respond to changes in the U.S. population, focusing on brands intended to appeal to growing demographic groups, including Hispanics, baby boomers, and millennials. This sharpening focus on specialized brands, along with relatively low interest rates and stiff competition, is expected to spur merger and acquisition activity beyond the 2017 benchmark of \$311.6 billion in deals reported in the consumer products sector. Concurrently, consumer products companies will likely spin off secondary brands to maintain traditional product lines to account for decreased consumer spending in the near future.

TECHNOLOGICAL ADVANCEMENTS

The Internet of Things (IoT) may prove to be the most significant technological development for consumer products companies in this decade. Connecting devices and harnessing the power of data provides immense opportunities for industry players but can also give rise to potential liabilities.

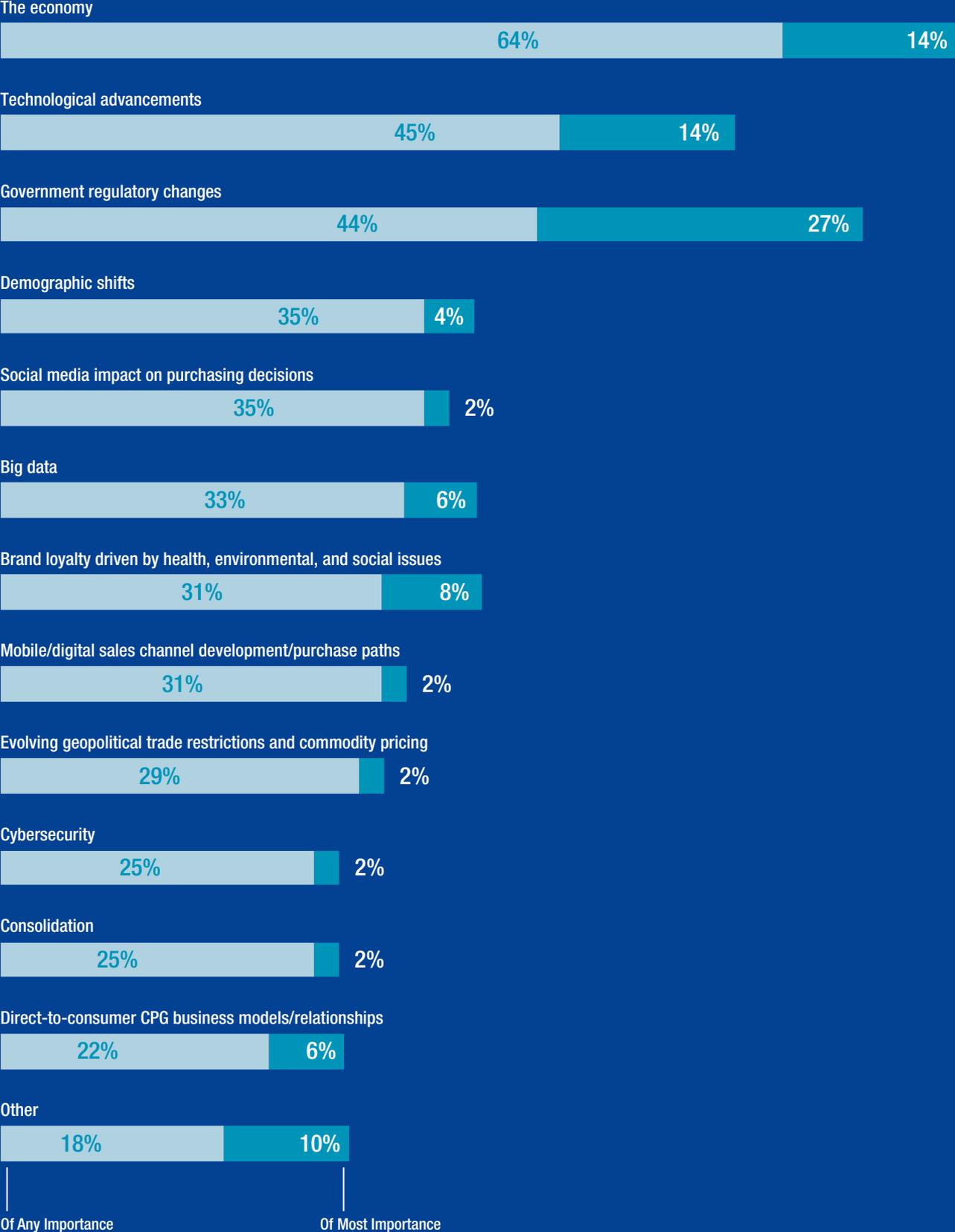
Consumer products companies embracing IoT, particularly those offering healthcare-related products and home devices, will face a myriad of legal, regulatory, and reputational complications. For example, concerns about privacy and security may lead to increased government scrutiny. Accordingly, companies should develop safeguards and systems designed to ensure compliance with relevant standards. Such efforts, in turn, need to be evaluated through both legal and business lenses. Many questions, including how traditional legal standards guiding the product liability industry will apply to novel products, remain unanswered, setting the stage for complicated legal proceedings to determine consumers' and companies' rights in the digital age.

Many industry leaders believe the benefits of IoT outweigh its risks. In this vein, many consumer products companies are actively developing technology to efficiently and creatively optimize customer engagement and influence consumers' path to purchase. For example, while traditional brick-and-mortar retailers have suffered from declining foot traffic as consumers order products online, some have responded to the digital commerce era by offering increased customization and "buy online, pick up in-store" options. Companies harnessing IoT technologies are also likely to have more modes of communication with their customers, enabling timely delivery of warnings or firmware updates related to safety or customer satisfaction.

GOVERNMENT REGULATORY CHANGES

Politics play a role here. The perceived effect of government regulation is mixed because of the current political climate in the United States. On one hand, the current White House and Congress are unlikely to actively regulate consumer products companies, particularly in the areas of health, environmental, or labor issues. On the other hand, absent federal action, many state and local governments will look to fill that void and are likely to push through legislative and regulatory changes on a range of issues that will affect consumer products companies, including climate change, nutrition, privacy, and the minimum wage. This piecemeal approach may be representative of increasing divergence in regulations globally. Such varying legal standards will put more pressure on in-house counsel to ensure compliance across multiple jurisdictions.

FIGURE 2: MOST IMPORTANT DRIVERS OF CHANGE FOR BUSINESS IN 2018



EVOLVING RISK ENVIRONMENT

FIGURE 3: CLASSIFICATION OF CONSUMER PRODUCTS LEGAL MATTERS

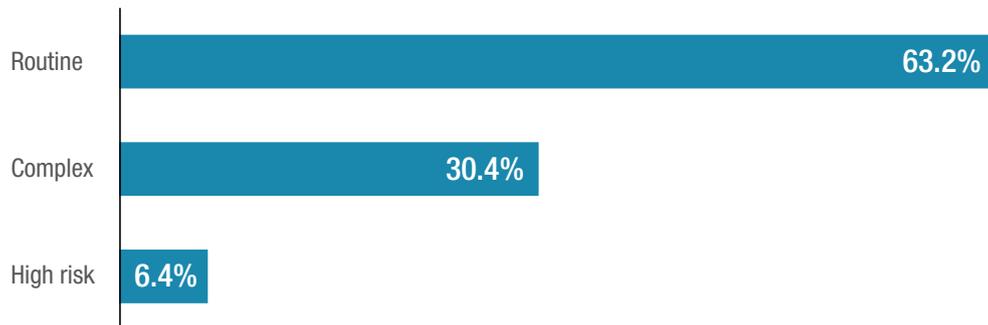


FIGURE 4: NUMBER OF HIGH-RISK CONSUMER PRODUCTS LAW SUITS 2018



Approximately one in three legal matters faced by consumer products companies in 2017 was considered high risk or complex. Although nearly one out of five respondents (18%) predicted an increase in high-risk cases in 2018, approximately the same number (20%) predicted a decrease. The majority of respondents (60%) predicted no change. These responses may reflect the disparate risk profiles among consumer products companies, with those in the IoT space facing more uncertainty than others. Even though consumer products companies generally do not expect growth in high-risk litigation, those that do likely have concerns about risks associated with regulation and technological advances. Gavin Grover, co-head of the global Corporate Finance Practice Group at Morrison & Foerster, commented: “Many traditional business models are undergoing massive change in the consumer area. These market forces capture the attention of top management.

Legal cases follow closely with disruptive changes in any industry and many cases are inevitably high stakes. Talent moves more frequently in times of rapid business evolution as new business models lure management teams. All these factors drive litigation and controversy practices across the spectrum. We always see spikes in high stakes litigation where industry forces are in flux. The San Francisco Bay Area in particular seems to capture an outsized share of disruptive new business models and the related cycle of controversy practices for growth companies.”

“MANY TRADITIONAL BUSINESS MODELS ARE UNDERGOING MASSIVE CHANGE IN THE CONSUMER AREA.”

GAVIN GROVER

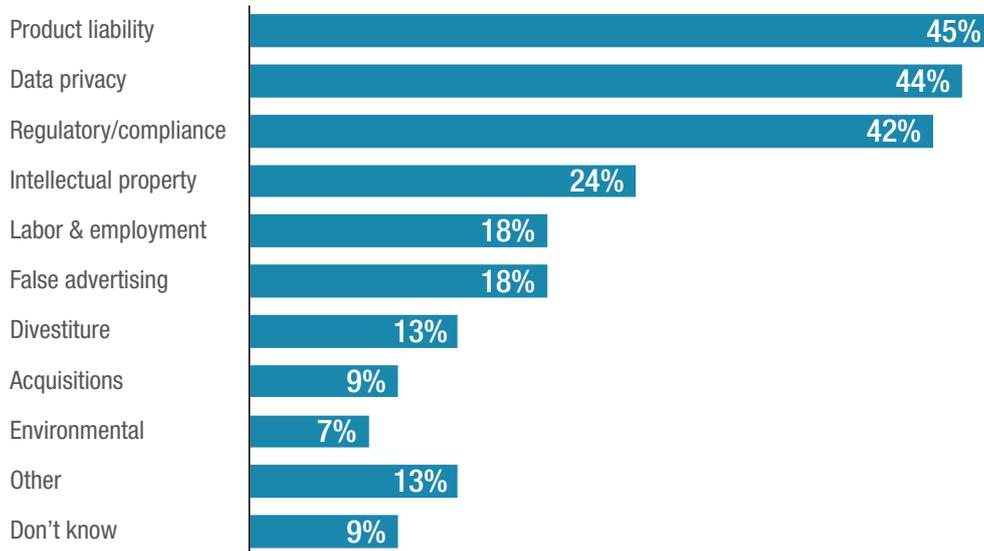
Co-Head Morrison & Foerster Corporate Finance; Consumer Products and Retail Group

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.

FIGURE 5: SOURCES OF NEW CASES

Which, if any, of the following are the biggest expected sources of new case activity in 2018?



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 IoT has changed the game. As IoT 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 IoT and autonomous devices, no one can know the specific product liability exposure that awaits consumer products companies,” states Erin Bosman, chair of Morrison & Foerster’s Product Liability and Counseling Practice Group. 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 IoT becomes more prevalent, courts may determine that software integrated into a connected product should be. Courts may also find that IoT devices expand the manufacturer’s duty to warn users about potential safety issues. “As lawyers, our job is to anticipate the most likely outcome of future judicial decisions so we can help minimize potential exposure,” explains Bosman.

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.

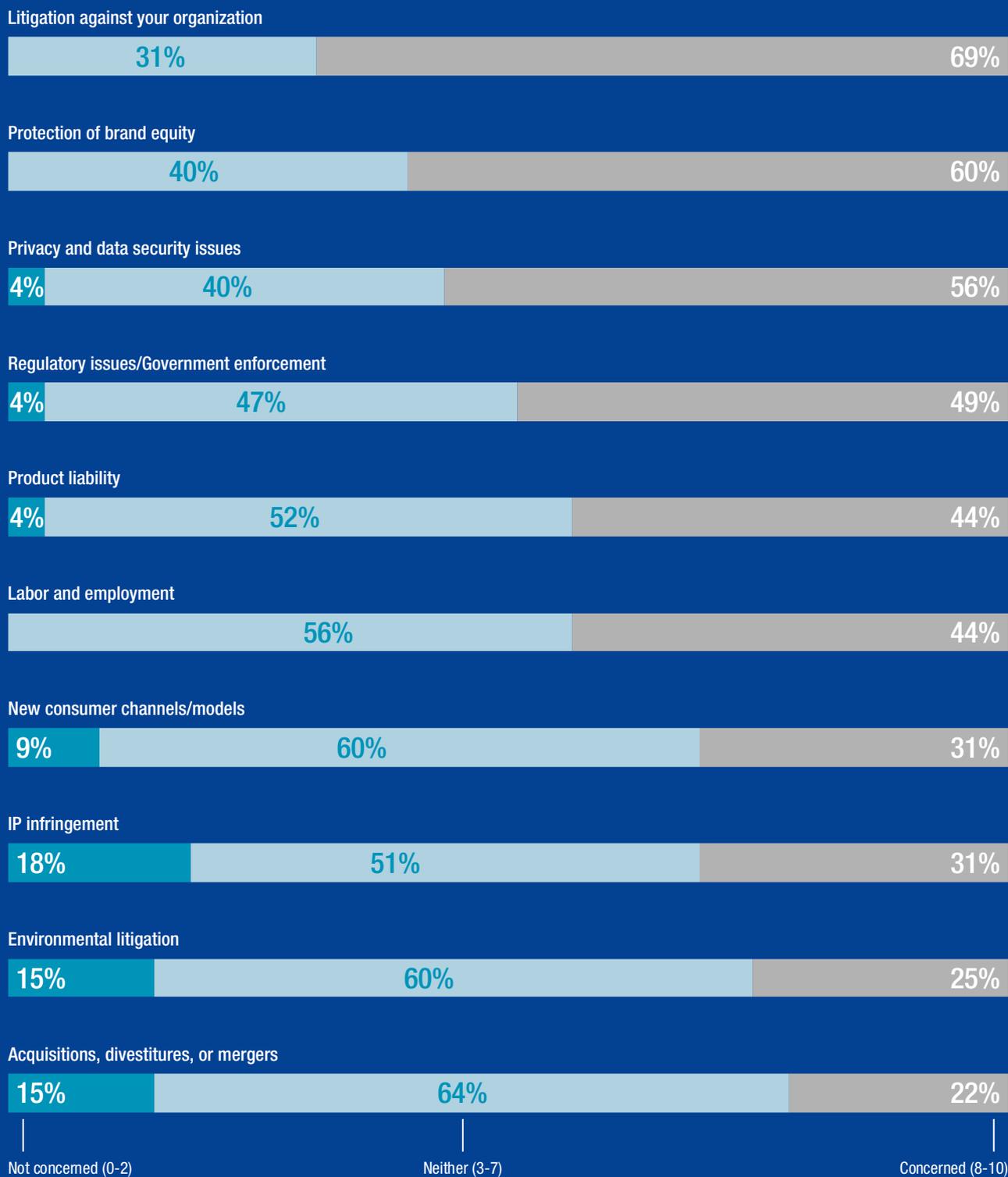
“ DATA PRIVACY IS INCREASINGLY OVERLAYING PRODUCT LIABILITY AND COMPANIES NEED TO BE PREPARING FOR NEW AND UNIQUE CLAIMS.

ERIN BOSMAN

Chair, Morrison & Foerster Product Liability and Counseling Practice; Consumer Products and Retail Group

FIGURE 6: LEGAL DEPARTMENT BUSINESS CONCERNS

At this point in time how concerned, if at all, is your legal department about each of the following issues for your organization (on a scale from 1-10)?



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, 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.

**“ IF I DON'T TRUST YOU
WITH MY DATA, I DON'T
TRUST YOU. PRIVACY IS TRUST.”**

ANDREW SERWIN

Co-Chair, Morrison & Foerster
Privacy and Data Security; Consumer
Products and Retail Group

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 assistant professor of law at the University of Chicago Law School Daniel Hemel's statement that “[d]ata privacy is the new product liability.”

European lawmakers have recently passed a law that increases the protection for consumers. Specifically, the General Data Protection Regulation (GDPR) will become effective on May 25, 2018, and it is intended to strengthen protection in the European Union (EU). It can apply to companies both within the EU, as well as companies in other parts of the world, depending on the circumstances. Andrew Serwin, partner and co-chair of the Privacy and Data Security Group at Morrison & Foerster, says that GDPR is part of a continuing, but growing, trend for increased regulation of personal information globally.

Failing to protect consumers' privacy poses two major issues for consumer products companies:

1. Major reputational damage and loss of brand equity 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.

2. 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 Consumer Product Safety Commission (CPSC) and the Food and Drug Administration (FDA) 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.

According to Andrew Serwin, 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% 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.

“ THE INCREASING ‘FEDERALIZATION’ OF PRODUCTS LIABILITY HIGHLIGHTS THE NEED FOR ADMINISTRATIVE LAW SOPHISTICATION AND EXPERTISE TO ADDRESS LIABILITY ISSUES.

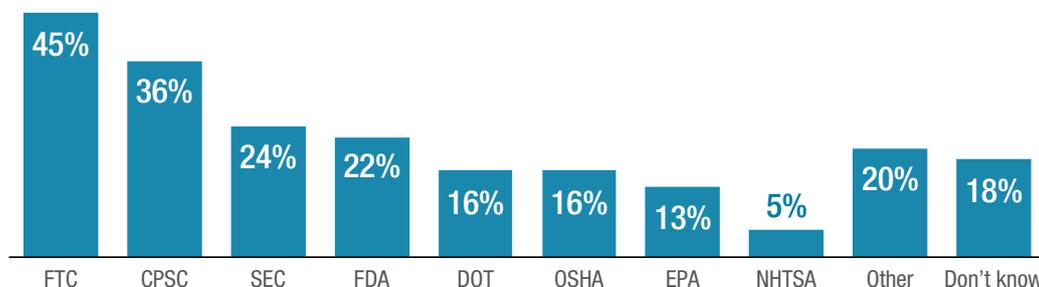
CATHERINE SHARKEY
Professor of Law, New York
University School of Law

FTC'S GROWING INFLUENCE

Relevant regulations come from a variety of sources. Although the current political 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.

FIGURE 7: RELEVANT REGULATORY AGENCIES

Which regulatory agencies, if any, are most relevant for your organization in terms of keeping up with regulatory developments or for potential enforcement actions?



The Federal Trade Commission (FTC) was considered by nearly half of survey respondents to be the most relevant regulatory agency. It was followed by the CPSC, the Securities and Exchange Commission (SEC), and the FDA, respectively. Each of these agencies, at least in part, monitor and regulate security, transfer, and analysis of potentially sensitive information. In recognizing the impact these agencies may have, survey participants appear to have a finger to the pulse of the rising importance of privacy and data security issues to the industry.

“ THE FEDERAL TRADE COMMISSION —THE CHIEF FEDERAL AGENCY ON PRIVACY POLICY—IS MORE RELEVANT TO LARGE U.S. CONSUMER GOODS COMPANIES THAN ANY OTHER AGENCY, REFLECTING THEIR FOCUS ON PRIVACY AND DATA SECURITY.

DANIEL HEMEL
Assistant Professor of Law,
University of Chicago Law School

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 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** is currently challenging a 2016 FTC order requiring the company to implement a data security plan over the next 20 years, arguing that the FTC has 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 outcome of the case **could define the scope of the FTC's 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. Sixty percent of respondents reported budgeted dollar exposure for litigation in 2017 to be below \$50 million, while 15% reported spending \$76 million or more last year, 36% reported spending \$5 million or less on outside counsel, and 31% reported spending over \$25 million annually.

FIGURE 8: LITIGATION EXPOSURE

What do you estimate the dollar exposure of your consumer products litigation matters was in 2017?

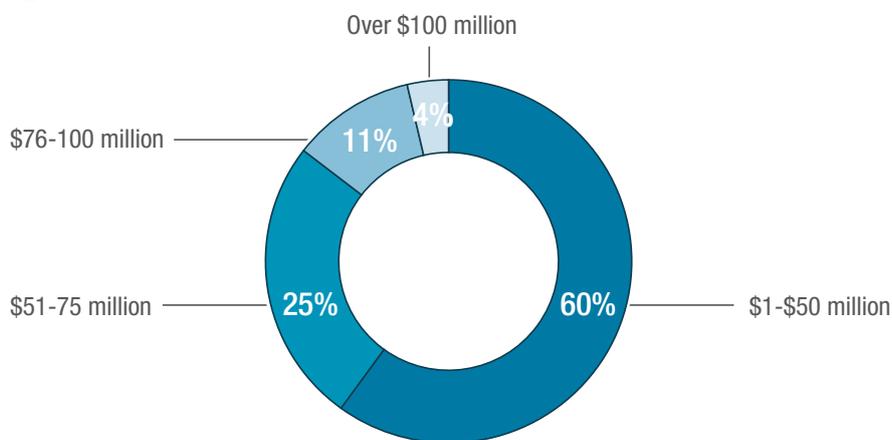
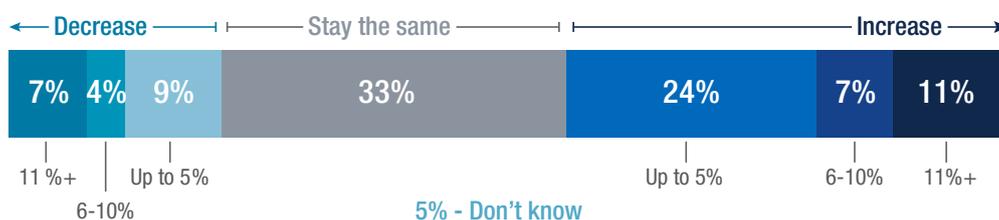


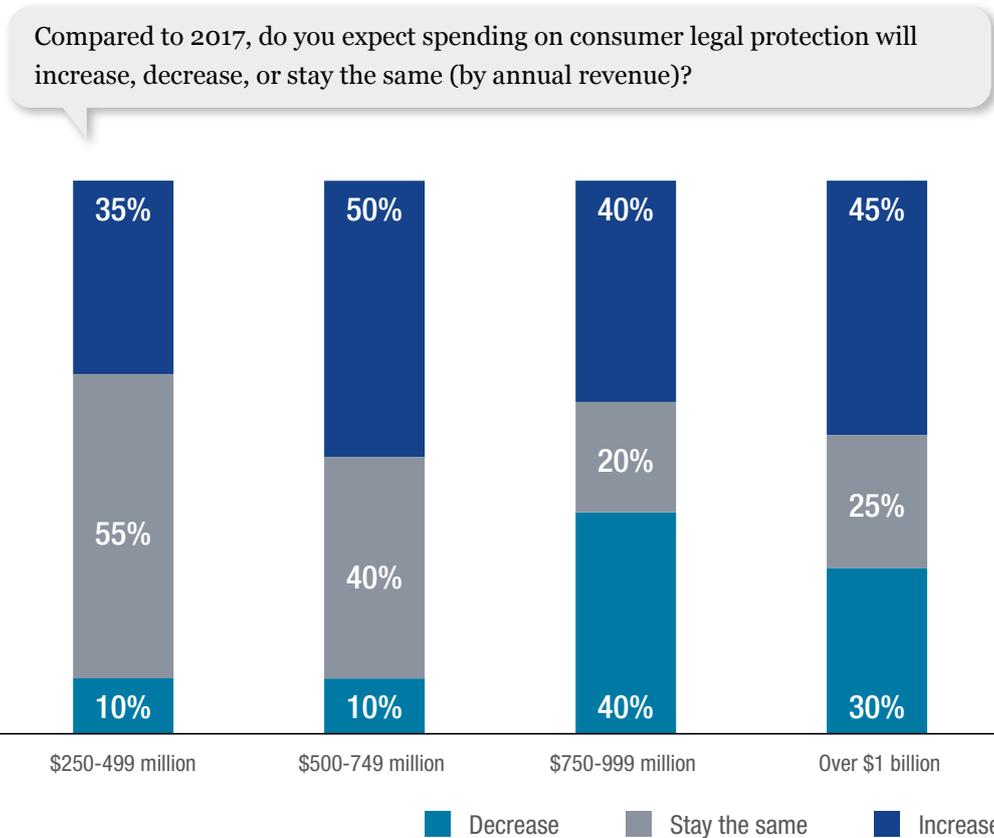
FIGURE 9: LEGAL MATTER SPENDING FORECAST

Compared to 2017, do you expect spending on consumer products legal matters in 2018 will increase, decrease, or stay the same?



Forty-two 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.

FIGURE 10: LEGAL MATTER SPENDING BY ANNUAL REVENUE



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% of companies with annual revenue between \$500 and \$750 million project an increase in spending, compared to 45% of companies with annual revenues over \$1 billion. Notably, while only 10% of companies with revenues under \$750 million expect their legal costs to decrease, 40% 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 UNKNOWNNS

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 report 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.

ABOUT OUR CONSUMER PRODUCTS AND RETAIL GROUP

Morrison & Foerster knows consumer products. Our clients span the consumer products spectrum, from prestige to mass market, electronics to baby products, chemicals to textiles. We provide full-spectrum legal services to some of the best-known household brands that trust us to guide them through their toughest strategic business decisions. With lawyers across the United States, Asia, and Europe, we're always there to help clients grow through corporate and transactional matters and defend them against high-stakes litigation. We are there at a moment's notice to manage safety crises and product recalls. And no matter what issues our clients face, we work with them to protect their reputation and brand integrity. Simply said, our lawyers have seen it all.

ABOUT MORRISON & FOERSTER

Morrison & Foerster is a global firm of exceptional credentials. Our clients include some of the largest financial institutions, investment banks, Fortune 100, and technology and life sciences companies. *The Financial Times* has named the firm to its lists of most innovative law firms in Northern America and Asia every year that it has published its Innovative Lawyers Reports in those regions. In the past few years, *Chambers USA* has honored Morrison & Foerster's Privacy and Data Security, Bankruptcy, and IP teams with Firm of the Year awards, the Corporate/M&A team with a client service award, and the firm as a whole as Global USA Firm of the Year. Our lawyers are committed to achieving innovative and business-minded results for our clients, while preserving the differences that make us stronger. The firm also has a long history of commitment to the community through providing pro bono legal services, including litigating for civil rights and civil liberties, improving public education for poor children, advocating for veterans, promoting international human rights, winning asylum for the persecuted, and safeguarding the environment.



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