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# STATEMENT OF COMMISSIONER ANNE M. NORTHUP ON THE FINAL RULE INTERPRETING CIVIL PENALTY FACTORS

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As part of the long-term strategic planning process currently taking place at this agency, we are considering how we want the public (especially consumers) and the industries we regulate to regard the Consumer Product Safety Commission in five years' time. I think that vision should guide the kind of long-range decision making entailed in our new civil penalties regulations. Today I voted against the proposed Final Rule Interpreting Civil Penalty Factors because it fails to take the agency where I believe it should arrive five years from now. Before delving into my specific concerns with the rule, I would like to share my own hopes for how others will regard this agency in the future.

For consumers, I would hope that they will view the agency warmly and trust it to intervene promptly and appropriately where genuine safety threats exist. Protecting consumers involves preventing dangerous products from getting to the market, removing effectively and efficiently those that do, and forewarning parents—in particular—of imminent but hidden dangers revealed by the agency's hard-won experience. The CPSC is doing a remarkable job of ramping up education, both by increasing its visibility in traditional channels and through the expanded (and clever) use of newer social media. All of those efforts pay off in attracting parents, child care professionals, and other consumers to take full advantage of the agency's valuable tools and put their faith in the agency as a reliable safety resource.

But I also hope that product suppliers can trust and utilize CPSC resources to confidently continue to bring new, useful and exciting goods to the market. Consumers demand a vibrant market that is able to evolve, allowing new and more creative start-ups into the market and encouraging current businesses in the market to expand and innovate in response to customer wishes. For example, buyers of children's products do not want to go to the toy store next Christmas and see only the same toys that were there last year. Parents do not want the market for juvenile furniture, children's clothing, and other durable goods to shrink, reducing the choices that bring individuality, interest, and flair to a child's life.

This rosy future is by no means guaranteed. The CPSIA imposes so many new requirements all at once—including arbitrary lead and phthalates limits (not based on risk), third-party testing, certification, tracking labels, etc.—that it challenges the capacity of both small and large consumer product companies to comply. Even the largest entities, like Mattel, have indicated how difficult it is to decipher the law's requirements. Despite its sizable team of in-house lawyers, the company has said publicly that it has had to hire outside counsel to help understand the law and hold weekly conference calls discussing how to comply with the act while remaining cost competitive.[1] One can imagine even the largest toy manufacturers freezing-in-place their product lines to reduce their exposure.

[1] Andrea Foster, "Mattel Finds CPSIA to be a Challenge," Product Safety Letter, November 9, 2009.

The reality for smaller companies is that many of them will ***not*** figure out the law correctly, at least at the beginning. Implementing CPSIA-mandated processes from scratch is complicated, costly, and inevitably imperfect. Many industries and products affected by CPSIA are now participating in a "regulated industry" for the first time. Although such companies may have good intentions and excellent safety track records, if they have never had to have elaborate protocols in place before, they may not be very good at it yet.

Even for more experienced companies with good processes in place, the sheer number and kind of potential new violations makes perfect compliance unlikely and an unreasonable expectation. There is a reason why you do not find "mom and pop" banks, electrical utilities, and oil refineries. The regulatory burden of traditional regulated industries is far too high for them to manage. We cannot simultaneously preserve small manufacturers, "mom and pop" retailers, and the like while turning the children's product market (or any similar market) into a regulatory morass. That conundrum leaves this agency with a choice: We can either signal that we will take a reasonable approach to enforcement, or we can fail to send such a signal and reap the consequences of market exit, job loss, and reduction in product variety.

Such consequences are already being felt and the Commission knows it. The CPSIA significantly raises the cost to bring a new product to market, including products in categories that have rarely if ever posed a safety problem in the past. Even without the threat of civil penalties, companies already suffer expense and reputational cost if they face a recall, fail a final product test and have to condemn a portion of their inventory, stop sale, or have a product impounded at the port or refused by a retailer if the paperwork is not correct. These regulatory risks explain why certain markets are shrinking. In meetings with industry groups and companies, we repeatedly hear these refrains: "Our small companies are leaving the market;" "We have dropped all our children's products;" "We are reducing the number of colors on this item;" or "We have decided not to expand into the children's market."

In today's vote on the Final Rule Interpreting Civil Penalties, the Commission had a chance to moderate the statute's harshest effects by overlaying a reasonable enforcement regime. While the new law greatly expands the allowable penalties, this is one area, and one of the few, where the law is not completely prescriptive. Here the CPSC had freedom to use its creativity and expertise to do what it does best: evaluate risk as an important factor. Unfortunately, this rule compounds the problem.

Specifically, I am concerned that the rule: 1) fails to treat technical violations differently enough; 2) gives limited credit for good faith and good effort, and 3) uses language that is too vague and noncommittal to reassure good actors. Although one may read a proper regard for each of these concerns into the rule—and I hope the agency's staff will do so—the rule as written does not require it, and the Commission's legal staff could just as easily disregard the relative risk created for consumers, ignore positive incentives for compliance, and eschew predictable enforcement.

<u>Treatment of Technical Violations</u>

Considering all the new requirements, the rule should have specifically stated that the agency will view technical violations differently, which I would define as compliance with a paperwork requirement rather than its corresponding safety standard. To use a traffic law analogy, an out-of-date parking permit (a paper violation) is not the same kind of offense as running a red light (a real safety violation) and the Commission could have said explicitly that it would not treat the two kinds of violations the same way. The agency historically has not sought substantial civil penalties for technical violations of the statutes we

enforce, and it should continue to distinguish between what might be termed safety offenses and status offenses. Unfortunately, all efforts to include such explicit distinctions were refused by the Majority.

To be fair, the rule does leave room for ***allowing*** the agency to consider technical violations differently. Severity of the risk of injury is specifically mentioned in the statute. Considering the gravity of a violation likewise provides an opportunity to take the risk created by a violation into account. The preamble to the rule recognizes that the "CPSIA has greatly expanded the number of prohibited acts" and indicates the Commission's corresponding intention "to use its civil penalty authority in a manner best designed to promote the underlying goals of the CPSA—specifically that of protecting the public against unreasonable risks of injury associated with consumer products."

However, the rule does not explicitly say that risk will be the most heavily weighted factor or that the agency will not ordinarily seek civil penalties for technical violations. Not only would such concrete guidance have ensured that the riskiest activities get higher penalties, but it also would have better enabled companies to align their finite compliance resources with the agency's enforcement priorities. Making this consideration explicit would have alleviated concern in the regulated community about the capability to comply with the myriad of new prohibitions that are still being defined and resolved lingering uncertainty over the agency's expectations of the regulated community. By refusing to say that we will not swat flies with sledgehammers, we instead leave people guessing.

The agency may instead use its enforcement discretion—including its enforcement discretion in establishing factors for the assessment of civil penalties—to clarify that it will adjust penalties according to the degree of risk that a particular violation creates for consumers. Such a policy would also maximize the agency's limited enforcement resources. To achieve the greatest safety gains for our finite enforcement dollars, we must focus penalties on those violations that pose the greatest risk to consumers.

In a broader sense, I am amazed by those who have adopted the position that nothing has changed with this new interpretive rule and statute, inferring that this rule just continues the current process for assessing civil penalties. In reality, everything has changed for those industries that must comply with the CPSIA. As Commissioners, we have to step back and remember that the CPSIA has removed the previous regime of assessing products and their lead or phthalate contents based upon risk. The new statute has introduced enormous new compliance requirements (including various paper requirements), such as testing and certification requirements on all children's products. And, the statute has added the new threat of multimillion dollar penalties for violating any of these requirements. In fact, I believe status violations, like paperwork violations, will emerge as the simplest and most likely offenses we catch rather than the truly high-risk violations. Given this new and still evolving regulatory regime of the CPSIA, today's rule interpreting civil penalty factors could have ameliorated some of the sweeping effects of the law, rather than add to them.

<u>Credit for Good Faith and Good Effort</u>

The rule also does not go far enough in giving credit to companies for their good faith in following compliance policies and good efforts in reacting to the occasional problems that will inevitably arise. While the final amendment allows compliance with Mandatory and Voluntary Standards and timeliness in reporting to be considerations, these provisions are too nebulous to be dependable factors in penalty cases. Given the

blow-up surrounding one Commissioner's statement to the press following the hearing, where a question was asked regarding the Commission's inclusion of Mandatory and Voluntary Standards in the Nord amendment, it was clear that the manner in which this interpretive rule is treated by staff is still quite debatable—even amongst the Commissioners. As firms spend money, check and recheck, and invest in new oversight internally, they deserve to know with specificity what actions will help protect them from a potentially over-reaching prosecutor. This is especially important in the first few years of implementation of compliance regimes.

Making lemonade out of lemons is a familiar concept, but this rule takes carrots and makes carrot sticks—that is, it mentions most examples of good behavior only by way of noting that their lack could ***increase*** the base level of punishment. That approach creates a rather warped incentive system. Nonetheless, I sincerely hope that the amendments to the Final Rule that Commissioner Nord negotiated with our fellow commissioners have a meaningful effect. Given their staunch resistance to similar changes for several weeks prior, future foot-dragging and recalcitrance on crediting good behavior seem more likely—though I will be delighted to be proved wrong.

The preamble and final rule give even shorter shrift to many of the other thoughtful comments submitted in response to the interim final rule. Although most, if not all, of the suggested factors can still be considered in future cases (as part of the nature and circumstances of the violation), it would have been far better if the rule explicitly acknowledged that credit will be given for following best practices in compliance, benchmarking compliance efforts within the industry, having a previous record of solid compliance, timely responding to violations, and several others. Along these same lines, and for the same reasons, the rule should explicitly distinguish violations committed with actual knowledge from those committed with mere presumed knowledge. The claim that actual and presumed knowledge are treated equally under the statute is simply incorrect. The statute would not provide for both kinds of knowledge if it did not wish to make a distinction. It would only have the lower negligence provision. The fact that actual knowledge is also mentioned in the definition means that the distinction can—and should—be taken fully into account in assessing civil penalties.

<u>Too Vague and Noncommittal</u>

It does not take very many civil penalty cases before one gets a sense for the differences between good actors and bad actors. Of course, that is a subjective judgment. The trick with civil penalties is to identify the good actors and bad actors with objective provisions under which any party can adjust their conduct in advance to avoid the cut of the law. That way we can rein in the bad actors without demoralizing the good ones. This rule does not accomplish that. Instead, the language is too vague and flexible to reliably sort the good from the bad and instead catches everyone in the same net and tends to presume that anyone caught in the net is bad. I believe the lack of specificity comes from the agency's desire to preserve flexibility, not a fundamental unwillingness to sort behavior. But the problem is that too much flexibility undermines predictability, and more than anything else we have heard from businesses about the uncertainty created by the CPSIA.

At an unsettling time when a multitude of new prohibited acts have been generated and maximum penalty levels raised, these factors do not contain enough specificity to give the regulated community confidence that the agency will wield its enforcement hammer fairly or predictably. We should want companies believing they can comply, not that the stakes are too high to risk playing at this table.

Unfortunately, I do not believe the lightweight language in the Final Rule Interpreting Civil Penalty Factors is sufficient to encourage good but small corporate citizens to stay in the game.

Despite my vote today, I do appreciate my colleagues' inclusion of certain clarifying language that I requested. In particular, I believe it was important to include language specifying that the number of defective products counted for penalty purposes does not have to be the same as the (larger) total number of products recalled. Likewise, I appreciate the concession to include language compelling the agency to notify parties facing civil penalties of any additional aggravating factors it relies on that are not specifically enumerated in the statute. I was also pleased to support the amendment offered by Commissioner Nord today, which contained many further specific improvements that we had both sought—albeit, in stronger terms—at an earlier stage.

Conclusion

As I noted at the outset, we are going through a process now where we are asking how we want the agency to look in five years to different stakeholders. I want the agency to be perceived by consumers as protecting them and by industry as a fair cop—not as a mindlessly punitive bureaucracy. I want consumers to have safe products and vitality in the marketplace. I want industry to see that efforts made toward compliance matter, not that the hammer will fall whenever an inevitable mistake occurs. To achieve these goals, we need to avoid taking such a heavy-handed approach to enforcement. Companies who put products on store shelves that consumers want should not be treated like the enemy. The focus should be on education in the early years of this new regulatory regime—particularly with regard to violations of new provisions. We could impose the lowest penalties consistent with ensuring product safety and a level playing field.

In sum, the statute does not compel the overly punitive view of civil penalties adopted today. That is a policy choice this Commission is making, and with which I disagree. We should not be piling on at a time when the regulators and those subject to the statute are still feeling their way and a lot of uncertainty exists. Because the Final Rule Interpreting Civil Penalty Factors does not lead us in the right direction, I decline to support it.