

## **Foreign Tire Sales – A Cautionary Tale**

**By: Peter H. Gunst & Julia A. Carolan**

In June 2007, Foreign Tire Sales, Inc. notified the public and the National Highway Traffic Safety Administration that close to a half million of the light truck radial tires it distributed were lacking an important safety feature – a .6mm gum strip designed to protect the tire from belt and/or tread separations. This notification was prompted in part by a May 2007 lawsuit filed in Philadelphia against FTS and others involving a fatal car accident in which the defective tires were the alleged cause.

In its notification to NHTSA, FTS identified itself as the importer and Hangzhou Zhongce Rubber Co. Ltd. (“Hangzhou”), a Chinese company, as the manufacturer. FTS informed the NHTSA that due to its small size – FTS has 13 full time employees – it did not have the financial ability to recall nearly a half million tires, and requested NHTSA’s assistance in determining the universe of affected tires and conducting the recall.

NHTSA was unmoved by FTS’ pleas for help. It reminded FTS that, as an importer of motor vehicle equipment, FTS bore responsibility as a “manufacturer” pursuant to The National Traffic and Motor Vehicle Safety Act, 49 U.S.C. Chapter 301. As a manufacturer, NHTSA emphasized, FTS was responsible not only to provide notice, but also to remedy the safety defect.

FTS responded by submitting a plan for recall of the tires to begin on July 16, 2007. Its attorney, Lawrence Lavigne, warned that FTS will recall tires until it runs out of money, and “at that point, consumers are on their own.”

How did a company that does not even own a warehouse become a tire manufacturer? The United States Code, 49 U.S.C. § 30102, includes in its definition of “manufacturer” all persons who import motor vehicles or motor vehicle equipment for resale. Thus, American tire

importers step into the shoes of their foreign manufacturers and face all the legal consequences of a safety violation, including NHTSA enforcement actions and product liability lawsuits.

A manufacturer who realizes that its tires have a safety defect must follow the steps set forth in the Safety Act and related regulations. It must report the defect to NHTSA, notify all tire purchasers and remedy the defect. It has only five working days after learning of a safety defect to submit a detailed report to NHTSA. At a minimum, the report must include a plan for remedying the defect – including notification to owners, purchasers and dealers and intended recall efforts.

The manufacturer must remedy the defective tire within 60 days of the owner's receipt of notification of defect. The Secretary of the Department of Labor may extend this 60-day window for good cause. Manufacturers also are responsible for reimbursing dealers who provide remedies to their customers for defective tires.

Recalling a half million tires is no small task and comes at no small price. FTS' attorney estimates that it will cost \$80 million to perform a full recall of the defective tires – only a tenth of which FTS says it can afford to pay. And the costs do not stop there.

NHTSA can fine a manufacturer up to \$6,000 per violation of the Safety Act and regulations, with a maximum of \$16,375,000 in penalties. A manufacturer can be fined for failure to provide timely notice of a defect to NHTSA, or for failure to provide tire purchasers with timely and proper notice of or sufficient remedies for defective tires.

If a defective tire causes death or serious bodily injury, as is alleged in the case filed against FTS, criminal penalties may be pursued against any person who knowingly and willfully submitted false information to the Secretary concerning the defect. These include a substantial fine or imprisonment of not more than 15 years, or both. There is, however, a "safe harbor"

provision protecting individuals who attempt to correct a falsification within a reasonable period of time.

There is probably no way to totally avoid the high costs associated with recalls and product liability lawsuits because there is no way for a tire importer or manufacturer to completely ensure that its tires are free from defect. But there are ways to decrease your risks.

Besides the obvious – complying with all safety regulations – tire importers who are too small to do their own continual testing might want to rethink their distribution channels. One of FTS' problems appears to have been its reliance on Hangzhou's testing. A tire importer should have the financial capability to perform its own safety tests, and to effectuate a recall upon realization of a defect.

Do not hide the ball. Tire importers and manufacturers must immediately notify NHTSA and consumers of a defect. Failures to follow NHTSA's provisions for reporting and notification will result in steep financial and possibly even criminal penalties.

Tire importers must take special precautions. Daryl Allegree, manager of Risk Engineering for the Direct Underwriters business unit of Zurich, formerly known as Universal Underwriters, suggests that importers only do business with reputable companies that will provide proof of product liability insurance coverage. He cautions that the importer should pay close attention to the limits of such insurance.

Gary Cecil, Zurich's National Account Executive for its Direct Underwriters business unit offers these suggestions if you decide to import directly:

- Consult qualified legal counsel regarding the negotiations. Discuss with counsel your potential liability and how to obtain certifications of insurance.

- Negotiate and put in writing how you and the manufacturer will handle recall and warranty issues.
- Obtain a certificate of insurance from the manufacturer's liability insurance carrier that does a substantial amount of business in the United States. Have your insurance representative and qualified legal counsel review the certificate to ensure that the manufacturer has adequate limits.
- Obtain additional insured vendor's status on the certificate and get 30-day notice of any cancellation or non-renewal.
- Place the certificate in a dated file to follow up on 30 days prior to expiration.

Tire importers and manufacturers should learn from FTS' unfortunate situation. Importers must always remember they are functioning as manufacturers. This means that they have a legal duty to ensure the safety of the products that they sell, and that they must protect themselves as best they can against the unforeseen.