

**CALIFORNIA TRIAL COURT FINDS FORD ACTED
FRAUDULENTLY BY NOT REPORTING SAFETY
INFORMATION TO FEDERAL AGENCIES AND ORDERS
RECALL OF 1.3 MILLION VEHICLES**

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California Trial Court Finds Ford Acted Fraudulently by not Reporting Safety Information to Federal Agencies and Orders Recall of 1.3 Million Vehicles

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Last month, a California Superior Court judge issued an opinion following a non-jury trial in which he ordered the recall of nearly 1.3 million Ford motor vehicles due to Ford's failure to disclose and correct defects in its vehicles' ignition systems. This case, *Howard v. Ford Motor Company*, represents the first successful attempt by plaintiffs in a products liability class action to gain both monetary damages and equitable relief in the form of a product recall.

After considering voluminous evidence presented at trial by both sides, Judge Ballachey found that since 1982, Ford had been aware of a defect in its ignition-system modules and that it withheld knowledge of this defect from federal regulatory agencies. Judge Ballachey observed that Ford used what he described as "creative rhetoric" and omitted known facts throughout the course of several federal agency investigations into its vehicles' stalling problems to prevent those agencies from discovering defects in the ignition module's design. Even though the National Highway Traffic Safety Administration ("NHTSA") had declined to recall the Ford vehicles, Judge Ballachey found that Ford had a duty to federal and state "watchdog" agencies, such as NHTSA, the Environmental Protection Agency ("EPA"), the California Air Resources Board ("CARB"), and to the consuming public, to reveal its knowledge of the ignition module failures. As a result, the judge concluded that Ford was liable to the plaintiffs under California's Unfair Competition Law ("UCL") and its Consumer Legal Remedies Act ("CLRA").

The *Howard* decision is significant to manufacturers of consumer products. In light of the Bridgestone/Firestone recall and proposed legislation in the United States Senate to criminalize the knowing introduction of a defective product into interstate commerce, the *Howard* decision adds to a growing trend of judicial and legislative activism in policing corporate knowledge of alleged product defects. The opinion also sends a green light to plaintiffs' counsel to seek additional avenues of recovery beyond monetary damages in product liability class actions.

Background

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As government agencies mandated stricter standards for automobile emissions, car manufacturers, such as Ford, felt pressure to upgrade their ignition technology to more efficient, electronic ignition systems. Designing electronic ignition modules to properly function in the hot environment of a car's engine posed significant technical challenges, and Ford ultimately decided to mount its ignition modules on its vehicle's distributors. This solution, Ford contended, was the only viable design because other alternatives posed different technical problems that made the ignition modules prone to even greater failure. Plaintiffs, however, asserted that Ford's design was flawed and that its decision to mount the modules near the engine, as opposed to inside the passenger compartment as some Ford engineers had advocated, was motivated by cost concerns.

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Plaintiffs offered evidence that after Ford installed the ignition modules near the vehicles' distributors, the modules began to fail, causing cars to stall without warning. Drivers complained to Ford and to NHTSA, which initiated five different investigations over several years. Ford responded to consumers by replacing ignition modules that remained under warranty, and by informing NHTSA that the vehicles stalled for a variety of reasons. It also conducted in-house tests and eventually issued an "Owner Notification," or partial recall of the vehicles most affected by ignition module failures. Ford did not replace failed modules that were out of warranty, however, and allegedly did not report the failure of any ignition modules to the EPA.

NHTSA closed its investigations without ordering a recall. In addition, Ford settled private product liability claims on the condition that plaintiffs return any information disclosed to them during discovery. NHTSA later reviewed the matter again, and when provided with additional information regarding the failure of the ignition modules, decided not to reopen its investigation.

The *Howard* plaintiffs sued and moved for class certification in 1997. Plaintiffs alleged Ford's failure to disclose an allegedly known defect in its ignition systems amounted to fraud in violation of the California UCL, which prohibits "unlawful, unfair or fraudulent business act[s] or practice[s]. . . ." Plaintiffs also asserted claims under the CLRA, which prohibits certain unfair or deceptive acts or practices which result in the sale of goods to a consumer. By way of relief, plaintiffs sought monetary damages and a recall of all vehicles affected by the allegedly defective ignition modules.

Holding

In his 21-page post-trial opinion, Judge Ballachey found that, in failing to disclose what he concluded was a known defect in its ignition modules, Ford concealed vital safety information from government "watchdog" agencies and the consuming public. Given what he found the company knew about the modules, the judge concluded that this amounted to Ford's fraudulently concealing the failures of the modules. In this regard, Judge Ballachey noted that "by not telling the government and the consuming public about the defects in the distributor-mounted TFI modules, Ford was, in effect, making positive statements about the durability and safety of the device."

From this premise, the Court concluded that Ford violated the California statutes prohibiting unfair, fraudulent and deceptive practices. The Court rejected Ford's argument that plaintiffs were seeking to enforce federal statutes under which there are no private rights of action. In so doing, the Court invoked the very broad standards for liability under the California statutes, stating that "Plaintiffs are not enforcing the predicated statutes, they seek to enforce the UCL and CLRA."

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In discussing the appropriate remedy, Judge Ballachey rejected plaintiffs' claim for disgorgement damages, absent proof of "ill gotten gains" in the form of "avoided costs," but granted other monetary damages for restitution and equitable relief in the form of a recall. Specifically, Judge Ballachey granted class members monetary damages for any sums actually paid to Ford for the replacement of ignition modules, regardless of whether the modules were replaced after the warranty had expired, and ordered that a "fluid recovery fund" be established in favor of class members who sustained a monetary loss but could not be located. Most significantly, he granted the plaintiffs equitable relief, requiring that Ford fix "the problem giving rise to liability, namely the hidden defect" in the ignition modules. Judge Ballachey suggested that Ford implement a replacement program, replace old ignition modules with new ones, or, if it is more economical, implement a buy-back program. Nevertheless, the Court left the details of the recall to a Court-appointed referee. Finally, the Court ordered Ford to pay the costs for implementing the remedy and granted the plaintiffs attorneys' fees.

Analysis

In their briefs, plaintiffs stated that the "outcome of this case will affect the way product manufacturers do business in this country." They are likely correct. The *Howard* decision brings together a number of issues of which manufacturers of consumer products must be aware in addressing federal agencies such as NHTSA, Consumer Product Safety Commission ("CPSC"), EPA, and Food and Drug Administration ("FDA"), and anticipating consumer or class action litigation.

First, the Court appears to have concluded that it had the power to determine whether Ford met its obligation to report certain information to various federal governmental agencies. Unlike the agencies themselves, however, state courts lack the extensive backgrounds of the agencies in interpreting the statutory provisions at issue. Particularly given the breadth and generality of certain federal statutes that impose reporting requirements, there is a significant risk that economically motivated plaintiffs will urge courts of general jurisdiction to "impose" a reporting requirement when Congress or the federal agency would decline to do so.

Second, manufacturers must be mindful of the Court's conclusion that Ford's failure to report to the federal agencies constituted an act of "fraud," even in the absence of a misleading statement. This holding represents a significant expansion in civil liability. Despite the Court's insistence that it was merely enforcing California law, in reality the Court recognized private state-law causes of action predicated upon alleged violations of federal statutes imposing reporting requirements. Although in clear cases it may be hard to challenge the notion that state courts have the ability to determine whether or not a federal reporting violation has occurred, in many cases courts will struggle to discern whether a

manufacturer complied with the federal requirements. As a result, courts may adopt divergent standards of conduct concerning a federal act that was intended to be interpreted by a single federal agency.

Third, these risks are magnified where a court determines that it has the power to order a "recall" or other remedial action as a result of these "violations." In evaluating matters within its sphere, a federal agency will develop standards and responses to a wide variety of issues, taking into account information it has developed over the years relating to safety, levels of risk, industry standards, consumer practices, economic impact and other factors. Ideally, agency responses are based upon policy judgments that transcend the facts of a particular case and that attempt to fit that particular case into an overall regulatory scheme.

Unlike an agency, however, a court of general jurisdiction is poorly situated to consider all of these factors. Moreover, there is a distinct risk that state court judgments will interfere with the policy objectives of the agency itself. Although some cases will cry out for the application of federal preemption to bar such state law causes of action and preserve agency hegemony, current preemption principles may be insufficient to avoid these risks in many cases.

Finally, it bears noting that in the aftermath of the Bridgestone/Firestone recall, there are at least two federal bills (S. 3014 introduced by Senator Specter and S. 3070 introduced by Senators Feinstein and Kohl) that would establish criminal penalties relating to the distribution of "defective" products. Howard adds yet another challenge to product manufacturers. The trend to greater government involvement with regard to consumer products is demonstrably on the rise.

Recommendation

Companies manufacturing consumer products must be aware of these developments and must consider them in their legal and operational strategies for dealing with potentially defective products. It is vital that companies vigilantly adhere to their compliance programs relating to disclosing product defects and be able to substantiate any non-disclosure decisions. Finally, these companies must take seriously attempts by class action plaintiffs to use state law to create private rights of action predicated upon alleged violations of federal regulatory requirements.

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