HUNTON& WILLIAMS

2016

RETAIL INDUSTRY

Year In Review

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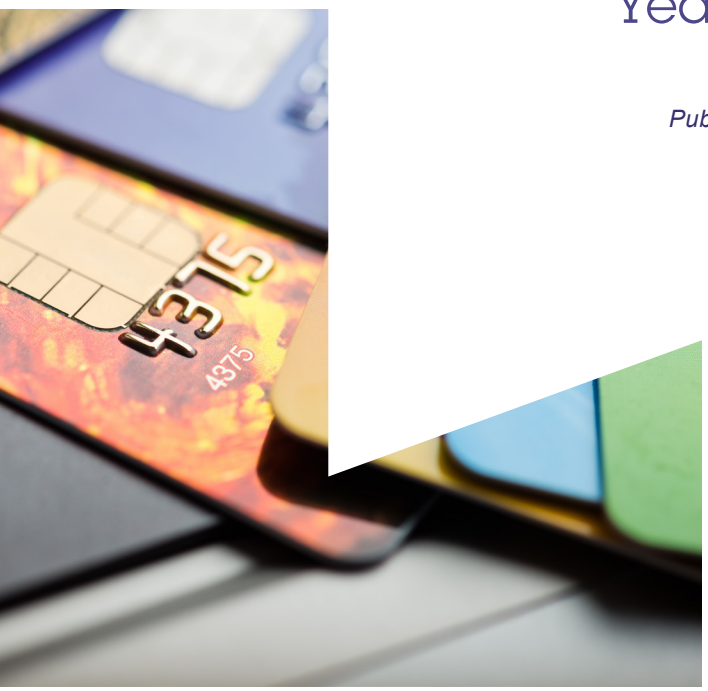

PROP 65 AMENDMENTS AFFECTING RETAIL

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The Safe Drinking Water and Toxic Enforcement Act of 1986, aka Proposition 65, among other things, requires warning California consumers prior to exposing them to even minute amounts of any of the 900+ chemicals listed as causing cancer or reproductive harm. The law has been on the books for 30 years. It is implemented by the Office of Environmental Health Hazard Assessment (OEHHA) and enforced by California's Attorney General and private citizens through citizen suits. It is enforceable against every entity in the chain of commerce, from the raw materials supplier to the retailer or a website seller. This past year saw significant amendments to the "safe harbor" warning requirements. For more background on Prop. 65, go to www.oehha.ca.gov/proposition-65 or www.HuntonProp65.com.

The new warning regulations place a burden on the retail seller by allowing upstream entities to shift the warning responsibility to them.

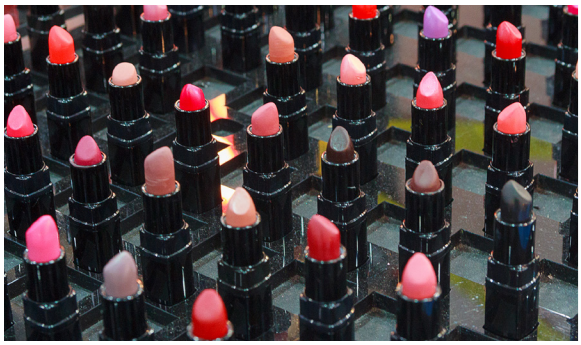
The new warning regulations contain two sub-articles aimed at bolstering warnings provided to California consumers. The first significantly impacts relationships between manufacturers, producers, packagers, importers, suppliers and distributors on the one hand (upstream entities) and retailers on the other hand and is the focus of this article. The second sub-article, not discussed here, details the methods of transmission and the content required for a warning to be judged a "safe-harbor" warning (i.e., deemed to be in compliance with the statutory warning requirements).[1]

If businesses faithfully follow the new provisions for the method of delivery and the content of a warning, then the warning is deemed to comply with the statute. This is important! Over the past three years, there have been over 1,600 claims by citizen enforcers and more than $73,000,000 paid by businesses as penalties and plaintiff's attorney's fees relating to Prop. 65 claims. These figures do not include business interruption costs, defense attorney fees, experts' costs or the costs to implement "fixes" to comply with settlements.

How Does The New Regulation Impact The Relationship Between Retailers And Upstream Entities?

For the retail industry, the most significant provisions in the new Clear and Reasonable Warning regulations is Title 27 of the California Code of Regulations (CCR) Section 25600.2, **Responsibility to Provide Consumer Product Exposure Warnings**. While the Prop. 65 statute requires minimizing the burden on retail sellers of consumer products to provide warnings,

[1] Notably, the new regulation is clear that nothing precludes a person from providing a warning using content or methods other than those specified in the second sub-article, so long as the warning meets the statutory requirements (i.e., that the warning is "clear and reasonable").



CCR §25600.2 seems to contradict this mandate. *See* Cal. Health & Safety Code §25249.11 (f).

According to CCR §25600.2 (b), upstream entities can comply with the warning obligation when there is a requirement to warn, by shifting that obligation to retailers. The regulation states, "[Upstream entities] may comply…either by affixing a label to the product bearing a warning that satisfies [the duty to warn], or by providing a written notice directly to the authorized agent for a retail seller…," thereby requiring them to comply with the warning requirements. Sections 25600.2 (b) and (c) go on to specify the details that the upstream entity must adhere to in order to shift the compliance burden to the retailer. But, if those conditions are met, then the retail seller is responsible for providing the warning.

In sum, the new warning regulations place a burden on the retail seller by allowing upstream entities to shift the warning responsibility to them.

Retailer Concerns

During the rulemaking process, retailers expressed concerns about the new regulations and their impacts. While some concerns were recognized and corrected, a good number were not. Some of the concerns raised include:

- Retailers typically are not knowledgeable about the manufacturing process or chemicals in products they sell.
- Many retailers may have thousands of products in their stores and cannot keep up with ones that may, or do, require a warning.
- Posting and maintaining in-store labeling, shelf signs or tags, and warning language would become unwieldy in stores that stock many products.
- Retailers cannot control the wording of labels provided by upstream entities, but would be required to post them in their stores. If a retailer chooses to change the wording provided to them, then the retailer is at risk vis-à-vis the upstream entity that provided the warning language.
- Deeming the retailer to have actual knowledge of an exposure within several days after the receipt of a 60-day notice was insufficient.
- Placing additional burdens on retailers resulting in increased administrative costs would prove problematic for small and medium-size retail businesses.

As one commenter wrote, "by allowing [upstream entities] to unilaterally bind retailers to providing warnings …, OEHHA has transformed the 'safe harbor' nature of consumer product warning methods…

into a mandatory warning regime for retailers, at the sole discretion of those supplying the products to the retailers." California Retailers Association, dated April 25, 2016.

One saving grace is that the new regulation, so long as consumers receive a compliant warning, allows upstream entities and retailers "to allocate legal responsibility among themselves for providing a [product warning]." §25600.2 (i)

Practical Steps Retailers Can Take To Reduce Their Liability And Help Manage Their Risk

Keeping in mind that there are nearly 1,000 chemicals on the Prop. 65 list and that the list is constantly updated, business owners should conduct periodic assessments to identity the products they sell that contain chemicals of concern, whether products can be reformulated to remove those chemicals and, when warnings are needed, how best to provide such warnings.

In light of the warning regulation changes and the constant slew of notices issued to businesses in California, concerned retailers should first develop a comprehensive understanding of the new warning regulations and how they potentially impact California operations and catalog and internet sales into California. A firmer grasp of the regulations can potentially be achieved by engaging in a dialogue with industry peers and trade groups or associations.

Second, retailers doing business in California must determine whether they will allow upstream entities to impose in-store warnings.

Third, depending on how that issue is resolved, retailers will likely seek agreements with upstream entities detailing how warnings may be given. We suspect that many retailers will negotiate arrangements that require upstream entities to place warnings on products and that they will not accept any, much less a glut of, in-store warnings.

Fourth, to the extent that upstream entities are not willing to resolve the warning obligations in ways satisfactory to retailers, then the real possibility exists that retailers will terminate relations with such upstream entities.

Fifth, we anticipate that many retailers will review and enhance Prop. 65 "shield" clauses in agreements with upstream entities to ensure that ultimate liability will rest with the upstream entities.

Finally, it is important for retailers to also pay attention to their private label products and ensure that they have appropriate warnings, if necessary.

Conclusions

It is important for all players in the chain of commerce to know and understand the new warning regulations. Given the position that retailers occupy in the process, businesses should consider what the best arrangements to make with upstream entities are to clearly allocate Prop. 65 liability and to minimize the burden that falls on retailers.