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DISCLOSING INFORMATION ABOUT POTENTIALLY HAZARDOUS TOYS AT MATTEL, INC.

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Abstract

On several occasions Mattel has paid fines to the Consumer Product Safety Commission (CPSC) over its failure to monitor product quality and report significant product safety concerns in a timely fashion. In August 2009, the CPSC announced that it was fining Mattel $2.3 million for its failure both to effectively monitor the use of lead paint on its toys and to notify the CPSC in a timely fashion. The issue of what constitutes a "timely" response to product safety concerns, and what is the "right" disclosure strategy raises a variety of ethical issues. For example, should Mattel comply with the CPSC regulations as written, or should it use its own standards for disclosing potential hazards in its products? Is it in the consumers' interest to be made aware of any and all potential hazards and risk information overload, or should potential hazards be thoroughly investigated before "unnecessarily alarming" consumers? Are the interests of consumers, shareholders, suppliers, regulators, and employees all congruent with regard to the disclosure of product safety issues, or might different stakeholders prefer alternative strategies for disclosure?

The Teaching Note is available from the author to bona fide case users.

KEY WORDS: product safety, disclosure, consumer hazards, toys, Mattel, Inc.

INTRODUCTION

Mattel Corporation, the world's largest maker of children's toys, has on several occasions "taken its time" to gather information and collect data before reporting possible defects to the United States Consumer Products Safety Commission (CPSC). Mattel claims it must evaluate potential problems carefully and not cause undue alarm to consumers, shareholders, and other stakeholders. Problems reported by consumers may be serious and have widespread consequences for consumers and for the firm's products. Other times, problems may simply be isolated incidents, with few repercussions beyond the reported incident. Finally, some consumer complaints are best characterized as attempts to defraud the company with false claims of injury and emotional distress. CPSC regulations (with few exceptions), require manufacturers to report all concerns over potentially hazardous defects to the CPSC within 24 hours (Casey and Pasztor, 2007). In August 2009, the CPSC announced that it was fining Mattel $2.3 million for its failure to effectively monitor the use of lead paint on its toys and notify the CPSC in a timely fashion. On other occasions, Mattel has paid fines to the CPSC over its failure to immediately report significant product safety concerns. For Mattel, these fines are viewed as a cost of doing business and are potentially less costly than the costs that might accrue if every potential product issue was immediately reported to the CPSC.

> *Mattel Chairman and Chief Executive Robert Eckert said in an interview that the company discloses problems on its own timetable because it believes both the law and the commission's enforcement practices are unreasonable. Mattel said it should be able to evaluate hazards internally before alerting any outsiders, regardless of what the law says. … In two [recent] cases, it [Mattel] collected scores of complaints for months before disclosing them to the [CPSC].* [Casey, Nicholas and Andy Pasztor, 2007, Safety Agency, Mattel Clash over Disclosures, *Wall Street Journal*, September 4, Page A1]

The issue of what constitutes a "timely" response to product safety concerns, and what is the "right" disclosure strategy raises several ethical issues. For example, should Mattel comply with the CPSC regulations as written, or should it use its own standards for disclosing potential hazards in its products? Is it in the consumers' interest to be made aware of any and all potential hazards -- and risk information overload -- or should potential hazards be thoroughly investigated before "unnecessarily alarming" consumers? Are the interests of consumers, shareholders, suppliers, regulators, and employees all congruent with regard to the disclosure of product safety issues, or might different stakeholders prefer alternative strategies for disclosure?

MATTEL BACKGROUND

Mattel was founded in 1945 by Harold Matson and Elliot Handler to produce picture frames in a converted California garage. Shortly thereafter, Handler began manufacturing dollhouse furniture from picture frame scraps, thereby beginning Mattel's involvement in the toy industry. In 1948, Matson sold his shares to Handler and his wife, Ruth. Mattel was incorporated in Culver City, California.

By the 1950s, the company's toy line included burp guns and musical toys. In 1955, the Handler's revolutionized the way toys were marketed by purchasing fifty-two weeks of advertising on the new "Mickey Mouse Club" television show, making it the first time toys had been advertised on television. In 1959, inspired by her daughter Barbie's fascination with cutout adult paper dolls, Ruth Handler created a three-dimensional doll, "Barbie", and later introduced a male doll, Ken, named after her son. Barbie, with her fashionable wardrobe and extensive line of accessories, was an instant hit. The Barbie doll has excited generations of young girls and has become the most successful toy brand ever sold. The doll, which was introduced as a teenage fashion model, later took on many aspirational roles, such as a doctor, dentist, firefighter, astronaut, paleontologist, and a presidential candidate. The success of the Barbie doll was instrumental in Mattel entering the worldwide toy market. Other Mattel brands included Polly Pocket, Hot Wheels, Matchbox, Fisher-Price, and American Girl.

In addition to developing its own toys, Mattel also licensed a wide variety of toys from other firms, including The Disney Disney Company (e.g., Mickey Mouse, "CARS" characters), DreamWorks Studio (e.g., Kung Fu), Sesame Street (e.g., Elmo, Big Bird), and book publishers (e.g., Winnie-the-Pooh).

In 2007, Mattel was the world's largest toy company, with net sales of just under $6 billion, and a profit before taxes of over $700 million. Products were marketed worldwide, with about half of sales coming from the U.S.A., just over a quarter from Europe, and the remainder from the rest of the world. Most products were marketed similarly worldwide, although some, such as the American Girl line, were targeted to specific national markets. Manufacturing took place in both company-owned facilities and at third-party contractors. Core products were generally produced at company-owned facilities in China, Indonesia, Thailand, Malaysia, and Mexico. Products of a more seasonal nature or those tied to the release of a movie or other co-branding arrangement were produced in third-party manufacturers' facilities in the U.S.A., Mexico, Brazil, China, India, New Zealand, Australia, and other Asian countries. Demand for toys was highly seasonal, with strongest sales in the fourth quarter of the calendar year. Mattel's three largest customers accounted for approximately 41% of revenue ($1.1 billion for Wal-Mart, $0.7 billion for Toys-R-Us, and $0.6 billion for Target).

LEAD PAINT IN TOYS

In June 2007, a firm that did testing for Auchan (a French retailer) reported unacceptable levels of lead in paint on a batch of Mattel toys from China. Mattel in China was informed and began to investigate the source of the toy and paint. Auchan reported high lead levels on a different toy in early July, and a consumer in the U.S.A. using a home lead test kit also reported the existence of lead paint on a toy. Until that time, internal Mattel monitoring of products had not identified unacceptable levels of lead in paint. Further investigations by Mattel in China found that all the identified products came from a single contractor, Lee Der Industrial, with which Mattel had a long-standing supply relationship. On August 2, 2007, Mattel announced it was recalling a number of toys that had been produced by Lee Der and which might contain unacceptable levels of lead in the toy's paint. On August 14, Mattel announced a further recall of toys with lead paint that had been produced by another Chinese contractor, Early Light Industrial. In both cases, the companies had experienced a paint supply problem with a regular subcontractor and had turned to a different paint supplier to fill the gap and meet production targets. In total, 848,000 toys were recalled, with a recall cost estimated at $30 million. Two years later, in August 2009, the CPSC announced that it was fining Mattel $2.3 million for its failure both to effectively monitor the use of lead paint on its toys and to notify the CPSC within the timeframe required by regulations.

MAGNETS IN TOYS

Beginning in 2003, Mattel had started using small powerful magnets in some toys. If the toys broke or the magnets became dislodged, it was possible that a child might ingest them. If more than one magnet was swallowed, they could attach to each other and cause intestinal problems, including blockages and perforations. In total, 63 toy models, including Polly Pocket sets, had been sold by Mattel between 2003 and 2007. In 2005, one child's death was caused by swallowing the toy's magnets, but that toy was made by another toy company. The CPSC issued a recall of various products made by that company (Casey and Zamiska, 2007). (Neither Mattel nor its products were directly affected by this recall. The magnets in Mattel toys were carefully imbedded in the toys, whereas in some other companies' products, the magnets were loose or could be removed easily by a child.) Starting in late 2006, Mattel products using the magnets were redesigned in order to improve retention and decrease the likelihood of magnets becoming loose. Mattel issued a recall for 2.3 million products. In August 2007, this recall was expanded to cover another 7.3 million products. Toys that had been sold since the redesign in late 2006 were not part of this recall, although they did contain the magnets.

CONCLUSION

During the last half of 2007, Mattel's stock fell by about 30%, as did the market value of several other toy makers. In the same period, the S&P 500 and Dow Jones Industrial were relatively flat. Mattel's sales and profits increased between 2007 and 2011. In 2011, Mattel reported record revenues and profits, with strong sales in developing countries and poorer performance in the U.S.A. The stock price in July 2012 was more than triple its value in April 2009. In its 2007 10-K report, Mattel stated that "Product recalls, post manufacture repairs of Mattel products, product liability claims, absence or cost of insurance, and associated costs could harm Mattel's reputation, divert resources, reduce sales, and increase costs and could have a material adverse effect on Mattel's financial conditions." Similar, but slightly different language was used in subsequent 10-Ks through 2011. Potential litigation risk over product liability was also regularly listed as a risk. However, the actual costs of recalls, fines, and litigation were not typically reported as having an unusual impact on financial performance.

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