

Manufacturers versus Component Part and Raw Material Suppliers: How to Prevent Liability

By Kenneth Ross *

Introduction

One of the more perplexing and potentially dangerous areas of product liability practice and law concerns the liability of the original equipment or finished product manufacturer (“OEM”) versus the liability of component part and raw material suppliers.

The plaintiff will always sue the OEM because the OEM’s name is on the product. However, determining liability is usually a complex analysis of the actions and inactions of everyone in the chain of production and distribution. In many situations, the OEM believes that the accident could have been caused by one or more of its suppliers. As a result, the plaintiff or even the OEM may ultimately sue other parties in the chain of production.

Involving such suppliers in litigation significantly increases the cost of the litigation and can cause damaging evidence since the defendants will tend to point fingers at each other. These disputes are very factually intensive and cannot easily be resolved early in the case. As a result, manufacturers of finished products and their suppliers need to consider the law and the ways in which they can minimize the chance of accidents before the product is sold and how, if accidents occur, they and others in the chain of production can defend themselves.

Basic Law

The relevant statement of law from the Restatement of Torts (Third): Products Liability (1998) says that if the component is itself defective and the defect causes harm, then the supplier is liable. In addition, the supplier is liable if the seller substantially participates in the integration of the component into the design of

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the product and the integration of the component causes the product to be defective and the defect causes the harm. *Restatement 3d, Section 5.*

In both of these situations, it seems fair to hold the supplier responsible. However, many times, the comparable responsibility of various suppliers, the OEM, and possibly the distributor of the component or finished product, can make a fair apportionment very difficult.

Where the component is not defective and the supplier did not participate in the selection or integration of the component into the final product, the law applies several doctrines to hold the supplier not liable. They are called the “raw material supplier defense” and the “bulk sales/sophisticated purchaser rule.”

These rules, which affect the burden of proof and do not really act as true affirmative defenses, are based on the premise that the OEM is the expert in the design and manufacture of the finished product and is a “sophisticated purchaser” as opposed to a supplier who may or may not know how its component or material is being used.

Is the component defective?

It is difficult enough with final products to determine whether they are defective. With components, it can be even harder. Components can be designed for many applications. And, there are component parts and raw materials that have different levels of function.

Some components, such as switches, do not function unless integrated into other products. Other components, such as motors, can function on their own but still may be incorporated into another product. The law may treat these differently, especially when considering the knowledge of the various parties when selecting and installing the component.

Usually, the OEM selects the product from a catalog or after discussion with personnel from the component manufacturer or their distributor. If the OEM did not consult the component supplier and selected the wrong component for the application, the product is not itself defective and the component manufacturer should not be liable. However, the OEM can still blame the supplier who provided incorrect or unclear information in the catalog and that is why they selected the wrong product.

The component can itself have manufacturing and design defects and defects in warnings and instructions. Liability of the component manufacturer under these theories would be based on the same law as that for OEMs.

Raw materials can be defective if they are contaminated or have the wrong formulation. These are manufacturing defects. While raw materials cannot be defectively designed, the supplier can fail to warn. If the OEM or component supplier uses the wrong raw material, it may be because the raw material supplier did not warn against such use. In addition, the supplier may have failed to warn about some hazard involving the use of the raw material or failed to instruct about how to use the raw material in the manufacture of the component or product. Or, maybe the OEM didn't ask and made certain assumptions or incorrect interpretations of sales literature or instructions.

On the other hand, the OEM or component supplier can fail to warn the user and, in that case, it may be their responsibility and not that of the raw material supplier. However, it may be the responsibility of the raw material supplier to warn or instruct the OEM or component supplier about any hazards that exist during foreseeable use of the component or final product made from the raw material.

One other area deals with incomplete products. Manufacturers of products such as machines which seem like finished products are not responsible for failing to incorporate certain safety features when they do not know what the machine is to be used for. In that case, the law considers them the manufacturer of an incomplete product, similar to that of a component manufacturer, and not liable for failure to provide a safe product. Instead, the employer is responsible under worker's compensation law for providing the appropriate safety devices for the particular application and use. Of course, the OEM can still be sued in product liability, especially if they "substantially participate" in advising the employer about how to make the machine safe for its intended use.

Substantial participation

The component supplier can be liable if they are substantially involved in the integration of its component into a final product, and the integration causes a defect and harm. Of course, the OEM could also be responsible.

Determining substantial participation is a very difficult factual and legal issue. In addition, it places the various parties in a quandary when the product is being designed and manufactured. Under the law, the component or raw material supplier is “discouraged” from substantially participating in the selection or integration of their product into a finished product. This is not a desired result but certainly an understandable one. Unfortunately, that lack of participation may create a problem in the final product and result in incidents and lawsuits.

While the component supplier has an interest in having its products installed and used safely and correctly, it does not want to increase its potential liability by offering advice that may or may not be correct. Despite that, if there are any questions by the purchaser concerning selection, installation, use and maintenance of the component, the supplier should provide assistance if they feel competent to do so.

There is some case law that says that merely designing a component to a manufacturer’s specifications does not necessarily constitute substantial participation. Also, providing technical services or advice concerning the use of a component part does not, by itself, constitute substantial participation. However, if a jury believed the supplier knew or should have known of a problem with the OEM’s use of their component and didn’t say anything, then they may want to try to keep them in based on negligent omission rather than substantial participation.

Again, the possible fact scenarios are plentiful and can become very complex as the number of possible culpable parties increases. As these parties try to blame each other, the plaintiff’s attorney can sit back and have the defendants make his case.

Preventive Measures

From the supplier’s side, I think you want to deal with OEMs who seem to be careful about the selection of components and knowledgeable about the uses to which it will be subjected. If the OEM asks questions, it is incumbent on the supplier to be as helpful as they can be to assist the OEM in selecting the correct component and installing it correctly. While this will fall over the line into “substantial participation,” hopefully problems are minimized or prevented and the issue of who is liable never needs to be addressed.

The supplier also wants to deal with OEMs who know how to correctly install the component and OEMs who adequately warn and instruct the final product user or maintenance personnel on how to install, use, and maintain the final product and its components. Even if the supplier is innocent, it can be very expensive to convince a plaintiff, a judge, or a jury of that fact.

For OEMs, I think they should buy components and raw materials from suppliers who are willing to be of assistance to the extent it is necessary. If the supplier, usually on the advice of counsel, takes the position that it gives no advice other than what is contained in the sales literature, and the OEM makes the final decision, then maybe the OEM wants to go to another supplier. Whether to change suppliers should be based, in part, on the OEM's comfort with making the final selection of the component.

In addition, the OEM wants to purchase from a supplier who manufactures the product correctly and in compliance with specifications and who supplies to the OEM all warnings and instructions necessary for the proper installation of the component and for the proper and safe installation, use and maintenance of the component.

In the post-sale area, OEMs want to be sure that the suppliers will inform the OEM if there are any problems with the component or raw material as used by other customers. And the supplier wants to confirm that the OEM has a good post-sale monitoring system and will quickly inform the supplier if there is a problem that is potentially being caused by the component.

If some problems do occur, the parties will need to reconstruct what advice was given by each party and what was the basis of that advice. Unfortunately, many times memories fade and documentation of the sale or design process is unclear, especially many years after design when most problems arise.

The best way for the respective parties to deal with this issue is to have clear and documented communications on what is being supplied, who selected the part, and what was the basis of the selection. If the component part supplier suggested the part, there should be documentation on what information was used by the supplier to make the recommendation. Similarly, if the OEM makes the final decision, they should clearly document the basis for the decision. And, one or more parties need to keep this documentation for a long enough time to use in the defense of litigation.

Each party must evaluate whether their actions and decisions are justified and how critical of a problem might arise if there has been a mistake. Selling the wrong shade of paint can be a big financial problem, but no safety problems will result. Selling the wrong plastic, engine, valve, switch, or chemical can, in many situations, create big problems.

It is difficult for the purchase order terms and conditions or sales documentation to anticipate all issues in this area. At a minimum, the contracts could contain mutual indemnification provisions which provide that the responsible party will indemnify the non-responsible party to the extent they are responsible. That, at least, raises the possibility in which, if culpability is determined, the responsible party will protect the blameless party in the event of a claim or litigation or some other problem such as a recall.

Unfortunately, culpability is usually in dispute and these contractual provisions, if they come into play, may not work until the litigation is almost over. However, at least there is a common understanding that fair apportionment of financial responsibility is the goal.

Conclusion

It is important for all parties to be proactive and consider the consequences of bad decisions. Each of the parties should do what they can to prevent themselves and someone else from making a bad decision and not just rely on the law or an indemnification agreement to protect them. Such protection may not work and innocent product users may suffer. Working together to prevent safety problems in products will benefit all parties in the chain of production and distribution.