

Liability of a Third Party Auditor in Food Safety Litigation

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As applied to claims by consumers, why does this matter?

- Third party auditors traditionally have not been defendants in foodborne illness outbreaks, but recently liability has become a consideration when there may be insufficient assets from the supply chain.
- Regulators are looking for consistency, reliability.
- But both must look to the law in order to hold auditors liable.
- The law looks for a duty.
 - Law is not settled in regards to if a duty exists or not.
 - So where could this duty come from?

If auditors have a legal duty, where does it come from?

■ Contract

- Pros: Parties can set the standard based on their expectations.
- Cons: Inconsistent between facilities and auditors; unlikely to reach consumer.

■ Statute

- Pros: Provides consistency and gives set expectations; can limit damages.
- Cons: Rigid, slow to change, and could impose too heavy a burden.

■ Common Law

- Pros: Can adapt to the realities of the industry.
- Cons: State-by-state variations don't give the industry much predictability; could lead to exorbitant damages.

Potential Liability to Consumers Based on Contract

- Breach of Contract
 - Because contract claims are limited by privity, only likely avenue for the consumer to reach the auditor is through assignment of the claims.
 - Parties can limit liability beforehand by setting out clear standards for and purposes of the audit and/or disclaiming liability and prohibiting assignment.
 - New York once explicitly rejected this approach for accountants due to privity issues. *See Ultramares Corp. v. Touche*, 255 N.Y. 170 (1931) (later superseded by statute).
- Typical audit not likely liability inducing
 - Auditor typically contracted to make visual inspections, not testing.
 - Different audits of different depths performed based on company requests – could be focused on GAP (Good Agricultural Practices), GMP (Good Manufacturing Practices), HACCP or other standards.

Potential Liability to Consumers Based on Contract

■ Potential Issues

- Liability under contract would only be helpful to the degree a facility has a viable claim against the auditor.
- Liability insurance will be impacted if consumer claims can be asserted based on contract.
- This type of liability will only come into play at facilities willing to pay for such an audit, meaning a “problem” facility will likely not be monitored properly.
- If courts find a statutory or common law source of liability, they may prohibit parties from disclaiming this liability (or simply ignore it when a case is brought).

Not a likely source of liability without assignment

Statutory Basis for Liability to Consumers

- Historically, the US government has given little guidance on how an audit should be performed.
- No universal audit standard or focus for audits.
- Currently, no statutory reporting requirements for domestic auditors, and some contracts could even prohibit disclosure.

Statutory Basis for Liability to Consumers

- Title III of the Food Safety Modernization Act (“FSMA”)
 - Governs foreign food processors that export foreign products or ingredients to the United States.
- Section 307 of the FSMA, Accreditation of Third-Party Auditors
 - Establishes FDA authority to recognize auditor accreditation bodies.
 - Auditors must issue written and electronic certifications that are monitored by the FDA.
 - Auditors are required to notify the FDA if they discover a condition that could cause or contribute to a serious risk of public health.
 - Auditors who certify a facility later linked to a foodborne illness outbreak can lose their accreditation .

Statutory Basis for Liability to Consumers

- Potential Issues

- This Section currently does not apply to purely domestic products, although the FDA has asked for comments on potential domestic application.
- The FDA has not even promulgated regulations under this Section, so courts have had little opportunity to review the underlying statute or proposed regulations. Thus, there is little guidance as to how it will work in practice.

Statutory Basis for Liability to Consumers

- Potential Issues Cont.
 - The statute currently contains no private right of action, so traditional statutory construction arguments will apply to whether or not an auditor's failure to comply supports a private civil suit. *See Transamerica Mortg. Advisors v. Lewis*, 444 U.S. 11, 15–16 (1979).
 - Could lead to decreased cooperation by companies with auditors if the company knows issues could be reported (potentially leading to loss of licensing or public relations issues).

Likely a future source of liability, but not a major issue currently for companies that do not fall under the statute.

Common Law Liability

- Tort claims for negligence
 - Duty of Care: A duty of care could be owed to any individual where the “end and aim” of the audit is for representation to, or reliance on by, third parties. *See Glenn K. Jackson Inc. v. Roe*, 273 F.3d 1192 (9th Cir. 2001) (rejecting the foreseeability approach below).
 - This theory is favored by some because the duty of care could change depending on the purpose of the audit. *See NCP Litigation Trust v. KPMG LLP*, 187 N.J. 353 (2006) (holding an auditor was liable to company shareholders, but that liability was still limited by the scope of the agreement with the company).

Common Law Liability

- Tort claims for negligence, cont.
 - Reliance: Some courts have looked to the foreseeability that a party would rely on the audit as a basis for finding liability. *See Citizens State Bank v. Timm, Schmidt, & Co.*, 113 Wis.2d 376 (1983).
 - However, such a duty is harder to nail down because it is based on the actions of the consumer, not the purposes of the audit to the company.

Common Law Liability

- Liability under the Restatement (Second) of Torts
 - Under Restatement (Second) of Torts §324A(b), a party can be liable if he undertakes another's duty owed to a third person, if:
 - His failure to exercise reasonable care increases the risk of harm;
 - He has undertaken to perform a duty owed by the other to the third person; or
 - The harm is suffered because of the other or the third person relying upon the undertaking.
 - A consumer's lawyer could argue an auditor undertakes the company's duty of reasonable care to consumers.
 - This theory has been used to reach corporate parents who monitor the safety protocols of their subsidiaries. *See Merrill v. Arch Coal, Inc.*, 118 Fed. Appx. 37 (6th Cir. 2004) (congruent with §324A, a parent corporation had assumed the safety of a coal miner that worked for a subsidiary mining company).

Common Law

- Issues:
 - Imposing liability without accompanying reporting requirements or other oversight would essentially hold a party (the auditors) liable for a situation that they have no authority to change (the running of the corporation).
 - Are auditors there for the benefit of the consumer, the company, or both?
 - What is the nature and scope of the duty which the auditor is alleged to have assumed?

Probably the most likely source of liability relied upon by a consumer plaintiff, but there is still much to work out with the underlying theories

Example of Liability Claims: *Primus Labs* in Colorado

- Listeria outbreak in cantaloupe.
- While claims were brought in a number of different jurisdictions, the case in Colorado is an instructive case study on liability.
- Jensen Farms, the producer of the contaminated cantaloupe, assigned all of its rights against Primus Labs, its auditor, to the plaintiffs.
- Along with claims against supply chain defendants, consumers alleged that the third party auditor, Primus Labs, was liable for damages. Plaintiffs alleged Primus Labs conducted an audit of the source contamination facility and did not give it a “failing” score (the score plaintiffs allege it deserved), making Primus Labs liable for the contamination.

Example of Liability Claims Cont.: *Primus Labs* Theories

- Defendant Primus Labs moved to dismiss the complaint for failure to state a claim (in regards to auditor liability).
- Plaintiff responded under a number of theories of liability:
 - Plaintiff alleged misfeasance (defendant's active misconduct injures others) rather than nonfeasance (defendant failed to act where he had an affirmative obligation to do so).
 - Defendant owed plaintiff a duty under common law negligence theories in Colorado as the plaintiff's reliance on defendant's action was foreseeable.

Example of Liability Claims Cont.: *Primus Labs* Theories

- Theories of liability continued:
 - Plaintiff was a beneficiary of defendant's contract with the company (the company, Jensen Farms, had assigned all rights it had to the plaintiffs, thereby destroying the privity defense).
 - Defendant owed plaintiff a duty under §324A Restatement (Second) of Torts (liability to third person for negligent performance in undertaking).
 - Defendant owed plaintiff a duty under §311 Restatement (Second) of Torts (to avoid negligently giving false information).
 - Defendant owed plaintiff a duty under §213 Restatement (Second) of Agency (to exercise reasonable care in hiring the specific auditors).

Example of Liability Claims Cont.: *Primus Labs* Rulings

- The court initially granted defendant's motion to dismiss, but then granted plaintiff's reconsideration under the theory of §324A Restatement (Second) of Torts (liability to third person for negligent performance in undertaking).
- The uncertainty of the status of liability for third party auditors is reflected in the fact that similar suits have been brought against Primus Labs in other states, resulting in a variety of different rulings from the courts on Primus Labs' motions to dismiss.

QUESTIONS?