

BACK HOME AGAIN, INC AND THE NERDLY ALARM:

A CASE STUDY

I. Background.

Joe Hoosier's grandfather started a small dry goods business in Westfield, Indiana. The store located in rural farming community was prosperous. Hoosier's grandfather liked to travel around the country, looking for the latest gadget to peddle to local farmers. When Hoosier inherited the business, it had become a relatively well-known retailer in central Indiana called Back Home Again, Inc. or BHA. Hoosier was one of the first to convince local farmers of the benefits of using personal computers in their farming operations. Hoosier also developed an upscale electronics business. Over the last thirty years, Hoosier opened stores throughout the Great lakes region (Indiana, Michigan, Ohio, Illinois and Wisconsin.)

Like his grandfather, Hoosier always had his eye out for new gadgets to market. While on a business trip to Hong Kong, Hoosier met with a marketing representative of Far East Export, Ltd. The representative introduced Hoosier to the Nerdly Alarm System. The home alarm, named for the famous Arkansas inventor, Ernst Nerdly, consisted of a black box that would throw out infra red beams to detect intruders. A computer in the box analyzed any interruption in the infrared signal. This would guard against the alarm tripping if a household pet inadvertently crossed one of the beams. The computer could actually sense whether a human intruder had entered a room. If the computer sensed an intruder, a recorded voice would say "Halt--The local authorities have been notified." If the owner tripped the alarm the owner could orally deactivate the alarm, simply by stating a password. Otherwise, the alarm would make a cellular 911 call informing appropriate authorities of the intrusion.

Hoosier loved the Nerdly alarm. The alarm system fit perfectly into BHA's upscale product lines. Hoosier asked for more details and was assured that the alarm met Underwriter's Laboratory standards. Far East Export used East Asian parts and labor to assemble the alarm. Hoosier thought he could resell the alarms in the US at a decent margin. Far East would sell to BHA but BHA would not be the exclusive US seller. Far East agreed to sell other versions of the alarm to other retailers. However, only BHA would be permitted to sell alarms with the prestigious Nerdly brand name.

BHA started with 100,000 units at a retail price of \$499.99. As expected, the alarms sold quickly. BHA's marketing of the alarms increased demand and quickly ordered 260,000 more within the first month of placing the item in its stores and offering for sale through its internet and mail order business.

II. Initial Complaints.

Within a few weeks of beginning US sales, BHA started receiving email complaints through its website. Consumers began complaining that the alarm would just go dead after sounding the warning message. BHA's customer complaint department typically asked the consumer to send the unit back and upon receipt would send out a replacement. This was BHA's usual practice. A couple more weeks went by and a few customers complained that the replacement units also failed. Some customers complained the alarm made a popping sound.

Concerned that replacement units reportedly failed, BHA's marketing department tasked an employee to follow up with several customers. BHA wanted to maintain customer loyalty and also try to determine what was happening with the product. The follow up calls did not yield many clues. A couple of customers vented frustrations. One woman complained that she thought her house would burn down. When pressed for the basis of such a statement, the woman responded that she smelled smoke or an "electrical odor" after hearing a "pop." In an email, a man from Michigan related that he saw a puff of smoke emanate from one of the alarms. Still BHA received what it thought were relatively few complaints (about 36) given that it had sold just about 360,000 units. What disturbed the marketing department was the quick rate it received complaints and the fact it had already received second complaints from some customers. Of the 36 complaints, 12 complaints stated that the failure was associated with a smoke smell or audible popping noise.

III. Dealings With the Manufacturer.

BHA's purchasing department contacted Far East about the problem. Far East at first denied there was any problem, attributing the failures to misuse, AC current problems, or other unspecific causes. After a couple of more weeks, BHA received more complaints. It now had 35 complaints associated with a smoke smell or popping noise. One man in Wisconsin reported that he saw some kind of brief "glow" inside the unit when it failed.

BHA's purchasing department contacted Far East again, seeking design drawings and related materials. Far East refused to provide any material and again took the position that BHA customers were experiencing failure because of unique circumstances. On a Friday morning, BHA purchasing and marketing personnel then brought the matter to Hoosier's attention. Joe Hoosier had inherited his grandfather's conservatism and became a little alarmed. Hoosier had a vague recollection that someone needed to make a report to the Consumer Product Safety Commission if a product posed a safety hazard. He just did not know when a duty to report arises and how to determine whether the alarm posed a hazard. Hoosier decided to send some units to an engineer at Purdue University for evaluation. In the meantime, Hoosier himself called Far East's representative. Hoosier asked if Far East had encountered these problems with units sold through other outlets. Far East's representative was very unspecific. Hoosier then said that he thought that Far East should inform the CPSC of the problem. Far East refused to acknowledge any problem existed and threatened Hoosier with a lawsuit for trade disparagement if Hoosier made a report. Hoosier called the Purdue University engineer. The engineer said she had just started his evaluation but needed the weekend to complete her work. The engineer said she would get back to Hoosier on Monday morning.

IV. Tragedy Strikes.

Meanwhile, a well respected music professor at the Indiana University School of Music has just purchased one of the alarms. The professor was due to perform on Saturday night with the Indianapolis Symphony Orchestra's annual "Vivaldi Strings Gala Fundraiser." The professor planned to drive up to Indianapolis early Saturday morning and packed her Eighteenth Century violin in the car. Worried about the safety of the fine instrument in the car parked in her garage, she plugged in a Nerdy alarm, and left the alarm in the garage. Shortly thereafter, an explosion occurred. The professor's home burned to the ground and the professor was killed in the fire.

An investigator with the Bloomington, Indiana fire department attributed the explosion and blaze to a faulty switch in the alarm. “A spark from the alarm ignited gasoline fumes from a gas can left next to a power mower in the garage,” the investigator concluded.

The professor’s death sparked nationwide front page news. The Sunday New York Times ran the headline: “America’s Mozart Killed By Nerdly.” The Indianapolis Star gave the story a local spin: “Back Home Again Device Claims Life Of Icon.”

V. Additional Investigation.

Hoosier discovered the sad news when he glances at the paper Sunday morning. By the time he reached the office on Monday, Hoosier had already received a call from the CPSC staff asking for a complete Section 15 report. Hoosier asked the firm’s general counsel to get involved. The general counsel related that one of the attorneys on the staff had mentioned that over the last month she had noticed that 11 small claims cases had been filed by dissatisfied customers. This was a little unusual but did not cause any alarm to go off. The small claims lawsuits were spread around various states and were usually handled by local managers and not attorneys. The general counsel also told Hoosier that his department had just received a letter from an insurance company asking to settle a subrogation claim for a small fire it claimed the Nerdly caused. The General Counsel’s office had just sent a letter asking for the insurance company to forward additional information. The General Counsel said that he was unaware there was any problem with the Nerdly generally. In addition, a consumer group called “Advocates for Safe Electricity” had caught wind of the incident and sent a FOIA request demanding access to all incident records related to this product and for a rulemaking banning Nerdly and all related products. ASE has also filed a class action lawsuit in Federal court against the manufacturer ASE on behalf of all consumers injured by products similar to the Nerdly alarm.

VI. The Issues.

- ◆ What should the company say and give the CPSC? What is the likely CPSC response? What strategy should the company adopt for dealing with the CPSC in this matter? What impact will the publicity have on the CPSC?
- ◆ Should BHA have reacted differently? Was it the unfortunate victim of circumstance or was its delay in reacting sooner excusable despite the tragic accident?
- ◆ What role should Advocates for Safe Electricity play in this case? Should the CPSC grant ASE access to documents?
- ◆ What system could BHA have in place to realize early warning signs of a problem?