Industrial property: legal protection of designs

2004/0203(COD) - 14/09/2004 - Document attached to the procedure

COMMISSION'S IMPACT ASSESSMENT

For further information regarding the context of this issue, please refer to the summary of the Commission's initial proposal COM(2004)0582 concerning a Directive of the European Parliament and of the Council amending Directive 98/71/EC on the legal protection of designs.

1- POLICY OPTIONS AND IMPACTS

Given the impossibility of reaching a voluntary agreement by industry itself, the Commission decided to follow instead a regulatory approach and to propose an amendment to Directive 98/71/EC to liberalise the aftermarket in spare parts. With this in mind, the Commission launched an impact study of the possible options to liberalise the aftermarket in spare parts. The study focused on the automotive sector, given the importance of the economic impact in this sector. However its conclusions and subsequent harmonisation at European level will apply to any sector where replacement and repair of complex products occurs. The study examined how four alternative sets of legal rights in respect of design protection would translate into future impacts on competition, community industrial sectors and consumers, against a baseline corresponding to the present situation.

1.1- Option 1 - Present situation, "Status quo": in some EU Member States, spare parts do fully benefit from design protection, whereas in others, the use of a design protected product for the purposes of repair and maintenance is allowed ("repairs clause"). In only one Member State, design protection for spare parts is term-restricted and combined with a market shares (EU-15): 50% of the automotive aftermarket enjoy free competition, 24% are covered by design protection, in another 24% there is supposed to be a free market and in 2% there is a combined solution. The continuation of the status quo is considered to be the most risky option of all, as legal certainty is key for the smooth functioning of the internal market.

1.2- Option 2 - "Full liberalisation," i.e. no design protection of spare parts: this option assumes a revision of Directive 98/71/EC that would remove design protection for must-match parts across the European Union. The liberalisation option promises net benefits in many respects without serious drawbacks. It would improve the functioning of the Internal Market and would allow for more competition in the aftermarket and access and participation of SMEs in this market. The consumer would benefit from more choice and lower reasonable prices. Besides the increase of legal certainty, it would also have as a consequence the simplification of daily lives of administrations, courts, companies, especially SMEs and consumers.

1.3- Option 3 - A system seeking a short term of design protection: under this alternative, design protection for spare parts shall be effective for only a limited period of time. After this period, the spare parts could no longer be covered by design protection and any third party would be free to produce and/or market them. The rationale for this option would be to allow VM (vehicle markers) a certain time to recover their costs and appropriate profit from their "intellectual effort". A limited term of protection would risk making the spare parts market uninteresting for independent producers as the market share left after the expiry of the protection might not be worth the necessary investment. In this case this option would have *de facto* the same impact on the market as full protection.

1.4- Option 4 - A remuneration system for the use of protected designs, including the appropriate level for remuneration: in the context of this option, independent producers could produce spare parts in exchange for a reasonable remuneration to be paid to the holder of the design right.

1.5- Option 5 - A combination of both the systems previously mentioned: a short term of design protection and a remuneration system.

The options including a remuneration systemseem not to be practical. They appear to be too complicated and administratively costly without promising significant benefits in comparison to both the status quo and the other options.

CONCLUSION: after the extended impact assessment of all the above options, the Commission is of the opinion that **the option not to extend design protection to spare parts in the aftermarket is the only effective one to achieve complete harmonisation in the internal market on the principle of liberalisation, in line with its intention in the original proposal in 1993 and the spirit of the Block Exemption Regulation.** Moreover, it fits with the spirit of the transitory agreement on the design regime on spare parts agreed in Directive 98/71. The extended impact assessment showed that the liberalisation provides the greatest net benefits compared to both the status quo and the other options considered.

IMPACTS

As there are no significant environmental and social impacts, impacts will be analysed in detail only with respect to certain aspects of the socio-economic dimension, namely, benefit for the consumer, safety, competition and employment, market behaviour, legal certainty and innovation.

Environmental impact: the proposal would not have any major effect on the environmental impact of production of spare parts. It is, however, expected that the level of production increases as demand should increase with falling prices. Yet, it is impossible to assess the environmental impact of this or of the possible changes in trade patterns.

Impact on consumer and prices: it is difficult to exactly foresee in quantitative terms how a liberalised aftermarket would develop. However it is interesting to compare spare part prices in EU markets. The situation in the US market was also examined. Using regression analysis, it was demonstrated that spare parts are more expensive in Member States with design protection in the aftermarket than in Member States without protection.

It is considered that these prices differences across countries with and without design protection for spare parts underestimate the price differences in prices between OEM (original equipment manufacturers) and independent manufacturers for similar parts. Given that the market share of vehicle manufacturers is around 85%, this means that even in countries without protection, most of the parts sold are OEM-made. Hence, the average price in those countries is heavily influenced by OEM prices.

It can be seen from the UK and the US experience, even after liberalisation, OE manufacturers will probably keep a sizeable market share. However, price reductions at least similar to those presented above could be expected Member States that currently enforce design protection. Prices are also likely to fall in other Member States, but only insofar as independent manufacturers compete in price and increase their market share in those countries.

Impact on Innovation:the core aim of any intellectual property right (IPR) is to encourage innovation. The protection of an IPR should enable the right holder to recover the expenses he had to bear for the invention/innovation. In addition to that, it should allow for an adequate reward of his efforts. This argument is of course also valid in the case of design protection. It is inherently difficult to precisely assess the impact of IPR protection on the innovative activity of an economy. It is equally difficult to assess the additional revenue a right holder can generate from an IPR. IPRs do not guarantee that the right holder can amortize his investment. They only give him a zone of exclusivity, but the “reward” is exclusively fixed by the market as a result of consumer preference. This preference is exercised at the

primary market (new cars) when the car is sold but not at the spare parts market, where the consumer has no choice regarding the spare part, it must match to the original. In the latter case, the vehicle manufacturer as a right holder, instead of getting a design premium (primary market), receives a monopoly premium.

It is even more difficult to estimate the effect of design protection for spare parts on the innovative activities of manufacturers, their costs and their profits. Two factors should be taken into account. First, the true purpose of creating car designs is to sell cars; here, design has an impact on consumer behaviour, in the spare parts sector, it does not. Thus, vehicle manufacturers will certainly continue to use design as a marketing instrument for their core business irrespective of whether or not there is protection in the aftermarket. Secondly, the available evidence suggests that the investment in the design of the outer skin of a car is relatively modest.

The Commission concludes that the impact of liberalisation on innovation is at any rate negligible.

Impact on employment: shifts in the market shares of spare parts producers would necessarily be reflected in employment. However, this is not necessarily a one-to-one matching. The net impact depends rather on relative labour productivity levels. For EU employment it is, of course, also relevant where the production is located. In addition, to estimate the overall impact on employment dynamic effects have to be taken into account as well as impacts on other markets and especially the distribution level. These impacts have to be isolated from other influences like global competition and outsourcing. Independent of the design protection regime the respective producer, be it a VM, an OE supplier or an independent producer, will allocate its production facilities as efficient as possible.

The liberalisation of the aftermarket might benefit SMEs in the EU as a continued lack of harmonised rules in this area is burdensome for companies. In contrast to car manufacturers, most producers of spare parts are SMEs. Liberalisation might hence encourage investment by independent producers in an open aftermarket for spare parts.

Impact on safety: in its paper, the Commission states ‘Prima facie, design and safety are completely unrelated issues’. The issues of the safety, quality and structural integrity of spare parts have been raised repeatedly. They are clearly crucial for consumers. However, design protection is meant to reward the intellectual effort of the creator of a design and to protect the appearance of the product, but not its technical functions or quality. These characteristics could be subject respectively to patent or trademark protection, but cannot be the subject of design protection.

Impact on competitiveness:the abolition of design protection in the aftermarket would impact on all car producers in the EU market in the same way as design protection can be obtained independent of the origin of the product. That is while imports into Member States with design protection would lose this advantage, exports of EU producers to third countries would not be affected in any way. Therefore, the argument that liberalisation would have a negative impact on the competitiveness of EU car manufactures vis-à-vis producers in third countries cannot be sustained.

As concerns the aftermarket itself, liberalisation would open business opportunities to independent spare parts producers. While the car industry argues that the market would be immediately dominated by large producers from third countries, ECAR is more confident that the specialised European producers will be able to compete in the market. The discussion on competitiveness should also take the business opportunities into account which the liberalisation will open for European producers in the spare parts markets in third countries without design protection.

Impact on legal certainty: all options would improve the situation concerning legal certainty compared to the status quo. However, different periods of protection for spare parts and original designs in the "term-limited protection" and the combined option could create confusion. A remuneration system could lead to legal uncertainty in the sense that it might result in frequent and lengthy litigation cases.

Impact on market structure:the harmonisation of the law in the EU by the denial of design protection for spare parts would complete the internal market and allow full competition. In countries where design protection in the aftermarket is not possible, new entrants may enter the market from both inside and outside Europe. The extent of this effect depends on both, the ability of these new entrants to gain confidence of insurers and, ultimately, the consumer; and on the European suppliers' ability to remain innovative and competitive in order to keep in pace with globalization. However, this is a trend that is unrelated, or only very remotely, to the issue of design protection, and much more to global competition.

2- FOLLOW-UP

This proposal will be implemented by its transposition into national laws. A revision clause and analysis of its implementation is already foreseen in Article 18 of Directive 98/71.